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CASE NOTE

Effectiveness of a Disclaimer in an Information Memorandum after the KAF Case

IN THIS ARTICLE, NICHOLAS TAN CHOI CHUAN REVIEWS THE RECENT FEDERAL COURT DECISION IN **KAF INVESTMENT BANK BERHAD V MIDF AMANAH INVESTMENT BANK BERHAD & 11 OTHERS** ON THE SIGNIFICANCE OF AN IMPORTANT NOTICE IN AN INFORMATION MEMORANDUM.

Introduction

An information memorandum ("IM") is a document typically included as part of the offering document in connection with a fund raising exercise on behalf of an issuer. It contains information relating to the issuer and its business and/or affairs. Under the current securities law framework an IM is not subject to the approval of the Securities Commission but it must be deposited with the Securities Commission within seven days after it is first issued pursuant to section 229(4) of the Capital Markets and Services Act 2007 ("CMSA").

A disclaimer set out under the heading "Important Notice" is usually included in an IM and aims to disclaim responsibility of the advisers for the accuracy, completeness or reasonableness of the contents of the IM on the basis that the IM is prepared based on the documents and/or information furnished by the issuers, and the contents of the same has not been independently verified by the principal advisers.

The significance of the Important Notice was examined at length in the recent Federal Court case of **KAF Investment Bank Berhad v MIDF Amanah Investment Bank Berhad & 11 Others**[1] (the "**KAF Case**").

The **KAF Case** was jointly heard with four other appeals. However this article will focus only on the aspect in the **KAF Case** that considered the significance of the Important Notice included in the IM issued by KAF Investment Bank Berhad ("KAF") for Pesaka Astana (M) Sdn Bhd ("Pesaka") in connection with Pesaka's issuance of RM140 million Islamic bonds (the "bonds").

Brief summary of the facts

Pesaka had obtained three government contracts and, in order to finance its implementation of the contracts, proposed a financing scheme which involved the issuance of the bonds. KAF was appointed as the lead arranger, facility agent and issue agent. The primary subscriber of the bonds onsold the bonds to the bondholders. For the issuance of the bonds, Pesaka set up a due diligence working group ("DDWG") whose primary role was to gather all information required for the issuance of the IM as well as to verify the accuracy of the contents of the IM.

Under the structure of the bonds issue, proceeds from the government contracts would be charged by Pesaka as security and they were to be paid into Pesaka's accounts. For the interest of the bondholders, Pesaka's accounts were to be ring fenced whereby all proceeds from the government contracts due to Pesaka would be deposited in Syariah Designated Accounts in which Maybank Trustees Berhad ("MTB") was the trustee and sole signatory. The proceeds were to be utilised in

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the manner as set out in the trust deed entered into between MTB and Pesaka.

At Pesaka's request, the DDWG agreed to use the existing conventional accounts belonging to Pesaka as the Designated Accounts and to convert them by making MTB the sole signatory. However, when the proceeds from the government contracts were deposited into the Designated Accounts by KAF, the Designated Accounts were not fully converted as MTB was not made the sole signatory. Pesaka, which was still the signatory that had control over the Designated Accounts, utilised the monies for its own purpose and failed to redeem the bonds and repay the bondholders on the maturity date.

The aggrieved bondholders commenced legal action against 12 separate defendants in the High Court, including KAF.

At the High Court

The High Court considered the IM on essentially two issues, namely (i) the liability of KAF for the statement made in the IM in relation to the forex claim; and (ii) the liability of KAF for the statement that new designated accounts would be opened and maintained. In relation to the first issue, the judge did not have to consider the effect of the IM, since the judge took the view that the statement relating to the forex claim was not misleading. In relation to the second issue, it was held that the statement became misleading when members of the DDWG decided to use existing accounts as designated accounts.

The High Court held that KAF owed a duty owed of care to the bondholders. This arose out of the proximity of the relationship between KAF and the bondholders which made it foreseeable that the bondholders would rely on the IM which KAF had played a substantial role in putting together. The High Court added that KAF had a duty to verify the information that was given by Pesaka against the original documents. The High Court judge held that KAF was negligent in failing to verify the contents of the IM, as a result of which the bondholders suffered damages. Liability between KAF and MTB was apportioned on a 60:40 basis by the High Court. It appears however that at the High Court level, KAF's counsel did not place much emphasis on the effect of the IM.

At the Court of Appeal

At the Court of Appeal, counsel for KAF contended, among others, that the High Court had failed to take into account the fact that the IM was not KAF's document but, rather, it was prepared by KAF based on information provided by Pesaka. Therefore, KAF should not be held liable for the information contained in the IM. KAF's counsel further contended that the High Court judge had failed to consider the effect of the Important Notice in the IM.

Nonetheless, the Court of Appeal affirmed the decision of the High Court. With regard to the Important Notice in the IM, the Court of Appeal considered section 65 of the SCA which reads as follows:

> *"An <u>agreement</u> is void in so far as it purports to exclude or restrict the liability of a person for contravention of section 55, 57 or 58 or for loss or damage under section 153." (emphasis added)*

The Court of Appeal took the view that the word "agreement" included the IM and, therefore, the Important Notice which disclaimed liability was void. Liability was re-apportioned between KAF and MTB on a 50:50 basis by the Court of Appeal.

At the Federal Court

The Federal Court took the view that the IM was issued by KAF on behalf of Pesaka to provide information to potential investors and it was not part of the Issue Documents which requires the approval of the Securities Commission. Premised on this, the Federal Court held that the IM was not an agreement falling within section 65 of the SCA. On this basis, KAF was free to include the Important Notice in the IM to exclude any liability arising from any claim that may arise from the IM. Further the bondholders in the **KAF Case** were sophisticated investors and experienced financial institutions who have vast experience in bonds. They are expected to act on independent and professional advice from their own sources in respect of the contractual obligations in light of the disclaimer as contained in the Important Notice.

The Federal Court further held that the most proximate cause of the loss was the failure on the part of MTB to ring fence the Designated Accounts or alternatively to stop Pesaka from operating the Designated Accounts as it was within the powers and rights of MTB to do so as vested upon it by the trust deed and the power of attorney. Therefore, MTB was wholly to blame for the loss and not KAF.

Observation

An issuer would form a DDWG (which typically consists of its financial advisers, legal advisers and accountants) to assist in the fund raising exercise, including the issuance of the IM. The DDWG would decide on matters relating to the IM, including the materiality thresholds to be adopted for the purpose of disclosure of material information in the IM. It is common that an Important Notice is included in the IM to exclude the liability of the members of the DDWG on the basis that they have relied on information supplied to them by the issuer, and not all the information contained therein has been independently verified by the members of the DDWG. Prior to the **KAF Case**, there appears to be no court decision on the effect of an Important Notice in an IM.

The **KAF Case** is indeed a significant decision as the Federal Court, being the

final appellate court in Malaysia, clarified the effect of the Important Notice in an IM and held, among others, that the principal adviser may disclaim liability in the IM through the use of the Important Notice.

The judgment of the Federal Court in the **KAF Case** with regard to the effect of the Important Notice appears to adopt a more business-friendly approach as evident from paragraph 63 which reads as follows:

> *"The IM is widely used in other jurisdictions and it is generally accepted that the IM is merely to provide the potential investors with the necessary overview of the product before deciding whether to participate in bonds issue or otherwise. It is also common practice for a lead arranger to insert the notice of disclaimer." (emphasis added)*

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[1] Civil Appeal No: 02(f)-29-04/2012(W)

FINANCIAL SERVICES

Insurance Regulatory Framework under the Financial Services Act 2013

IN THIS ARTICLE, KRYSTLE LUI SHU LIN EXAMINES THE IMPACT OF THE FINANCIAL SERVICES ACT 2013 ON THE POWERS AND REGULATORY APPROACH OF BANK NEGARA MALAYSIA OVER INSURANCE COMPANIES.

The Insurance Act 1996 ("IA") was largely repealed by the Financial Services Act 2013 ("FSA") which came into force on 30 June 2013. The legal and regulatory framework for the insurance sector under the repealed IA is substantially preserved in the FSA and remains under the regulation of the Central Bank of Malaysia (Bank Negara Malaysia in Malay or "BNM"). Every guideline, direction, circular or notice under the repealed IA, issued and in force immediately before 30 June 2013, shall be deemed to have been issued under a corresponding provision in the FSA or any direction issued under the FSA and remains in full force and effect until amended or revoked[1].

An overview of the principal aspects applicable to insurance companies under the FSA is as follows:

- *Licensing requirements*

  Under the FSA, only persons carrying on an insurance business will be required to be licensed by the Minister. A licence granted under the IA shall be deemed to be a licence granted under the FSA[2]. The distinction between life business and general business in the IA is preserved in the FSA.

  Subsection 16(1) of the FSA prohibits a licensed insurer from carrying on both life and general business. An existing licensed insurer permitted to carry on both life and general business is given five years to comply with subsection 16(1) of the FSA, unless a longer period is specified by the Minister, on the recommendation of BNM, by a written notice to the insurer[3]. Therefore existing composite insurers will have to divest its insurance business within five years from 30 June 2013.

  The carrying on of an insurance broking business or financial advisory business now requires the approval of BNM (previously a licensed business under the IA). A licence granted to a person by BNM under the IA to carry on an insurance broking or financial advisory business shall be deemed to be an approval granted under the FSA[4].

  An adjusting business on the other hand would be a registered business under the FSA, and is not a licensed business. An adjuster licensed by BNM under the IA to carry on an adjusting business shall be deemed to be a registered person under the FSA[5].

  Schedule 5 to the FSA sets out the factors in which the Minister and BNM would consider in assessing the application for licence or approval sought under the FSA.

- *Acquisition and disposal of interest in shares*

  The acquisition and disposal of interests in shares in an insurance company in Malaysia has substantively changed under the FSA. Under the IA, "interest in shares" was defined as "a legal or equitable interest in a share".

Schedule 3 to the FSA sets out in detail what will be considered "interest in shares" under the FSA. Such an interest would include both direct and effective interests. The concept of interest in shares under the FSA applies to banks as well. Prior to the coming into force of the FSA, different definitions of "interest in shares" applied to insurance companies and banks.

The present restrictions under the FSA applying the concept of "interest in shares" include:

– *Acquisition of interests*

(a) the BNM's prior written approval is required for a person to enter into an agreement or arrangement to acquire any interest in shares of an insurance company which agreement or arrangement would result in such person holding (together with any interest in shares of that insurance company which are already held) an aggregate of 5% or more in the shares of the insurance company[6];

(b) the prior written approval of the Minister, on recommendation of BNM, is required for a person to enter into an agreement or arrangement to acquire any interest in shares of an insurance company which would result in such person holding an aggregate of more than 50% of the interest in shares of the insurance company[7];

(c) any person who has obtained an approval of BNM or Minister for such acquisition under paragraphs (a) and (b) above will require the prior written approval of BNM to enter into any subsequent agreement or arrangement which would result in his holding an aggregate interest in shares of an insurance company, or exceeding:

(i) any multiple of 5%; or

(ii) the percentage holding for a mandatory offer under the Malaysian Code on Take-Overs and Mergers prescribed under section 217 of the Capital Markets and Services Act 2007[8]; and

(d) a prior written approval of the Minister, on the recommendation of BNM, is required for a person to have control over an insurance company. This restriction however is not extended to:

(i) a director or chief executive officer of an insurance company in respect of the carrying out of the management duties and functions; and

(ii) a person who has obtained a prior written approval of the Minister to hold more than 50% of interest in shares of the insurance company.

– *Disposition of interest*

The prior written approval of the Minister (on the recommendation of BNM) is required for a person who has either more than 50% or 50% or less but has control over the insurance company to enter into an agreement or arrangement to dispose his interest in shares which would result in his holding an aggregate of interests in shares of less than 50% or ceasing to have control over the insurance company[9].

– *Financial holding company*

Any company (with the prior written approval of BNM) which holds an aggregate of interest in shares of more than 50% in an insurance company is required under the FSA to submit an application to BNM to be approved as a financial holding company[10]. Unless BNM otherwise approves, a financial holding of the insurance company shall not carry on any business, other than the business of holding investments directly or indirectly in corporations primarily engaged in financial services[11].

– *Maximum permissible holdings for individuals*

Under the FSA, an individual is only allowed to hold up to 10% interest in shares of an insurance company[12].

- The foreign equity participation in insurance companies was increased to a maximum limit of 70% pursuant to liberalisation measures announced in 2009[13]. BNM has indicated that a higher foreign equity limit beyond 70% for insurance companies will be considered on a case-by-case basis for players who can facilitate consolidation and rationalisation of the insurance industry.

Conclusion

The enactment of the FSA has standardised the legal requirements of BNM on banks and insurance companies in matters of, among others, control and acquisition of interests in shares. The powers of BNM are also strengthened under the FSA.

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[1] Paragraph 272(b) of the FSA
[2] Subparagraph 273(1)(a)(ii) of the FSA
[3] Section 276 of the FSA
[4] Subparagraph 273(1)(b)(ii) of the FSA
[5] Paragraph 273(1)(c) of the FSA
[6] Paragraph 87(1)(a) of the FSA
[7] Subsection 87(2) of the FSA
[8] Paragraph 87(1)(b) of the FSA
[9] Section 89 of the FSA
[10] Subsection 110(1) of the FSA
[11] Subsection 114(1) of the FSA
[12] Section 92 of the FSA
[13] Available at www.bnm.gov.my/index.php?ch=en_press&pg=en_press_all&ac=1817&lang=en

INTELLECTUAL PROPERTY

The TPP Agreement: Change for Better or Worse?

IN THIS ARTICLE, KHOO YEE MUN CONSIDERS THE POTENTIAL IMPACT OF THE TRANS-PACIFIC PARTNERSHIP AGREEMENT ON MALAYSIAN PATENTS LAW.

The Trans-Pacific Partnership Agreement ("TPP Agreement") has received overwhelming criticism since the commencement of negotiations between the United States and 11 other negotiating governments[1], one of which is the Malaysian Government. While some of the technical and less contentious chapters such as Small and Medium Enterprises have been concluded, the negotiating governments are still struggling to agree on the other more controversial issues, particularly the chapter relating to Intellectual Property Rights on patents rights. Observers argued that the TPP Agreement would considerably benefit the big pharmaceutical companies as the proposed provisions in respect of patent rights seem to favour the commercial interests of big pharmaceutical companies over the interest of the general public. This article will highlight, among others, three proposals made in the TPP Agreement that would change the patents law in Malaysia.

1. Extension of patent protection term

In regard to patent protection term, it is necessary to refer to the Agreement on Trade-Related Aspects of Intellectual Property ("TRIPS Agreement") which came into force on 1 January 1995. The TRIPS Agreement binds all members of the World Trade Organization ("WTO") of which Malaysia is a member. Article 33 of the TRIPS Agreement provides that "*the term of protection available shall not end before the expiration of a period of twenty years counted from the filing date*". To conform to Malaysia's obligations under the TRIPS Agreement, amendments[2] were made to the Patents Act 1983 to change the duration of a granted patent from 15 years from date of grant to 20 years from the filing date of the application, with the exception of applications under the transitional provisions. At present, most countries have patents laws that stipulate a term of 20 years from the date of filing the application for a granted patent. However, the TPP Agreement requires an extension of a further five years patent term protection in addition to the 20 years patent protection. There are concerns that the continuous monopoly of five extra years would delay the entry of generics into the market and hinder the access to generics at affordable prices.

2. Lowering the threshold of patentability requirements

It is provided in section 15 of the Patents Act 1983 that an invention must involve an inventive step to be patentable. An invention is said to involve an inventive step if such improvement or advancement in the art would not have been obvious to a person having ordinary skill in the art. Hence, it is essential that the technical contribution of an invention must be over and above what is already known in the art. The TPP Agreement seeks to alter this basic patentability requirement in that even a minor modification made on a known or already-patented drug may be patentable, despite insignificant variation in its efficacy or absence of therapeutic benefits. Such practice is commonly known as "evergreening" which would prolong the existence of effectively the same patent in the market by patenting minor reformulations to the existing drugs. There are also concerns that if the proposed "evergreening" provision is to be allowed, the idea of an invention — a solution to a specific problem in the field of technology — would be fundamentally changed. Views have been expressed that such a provision would go against the principles of the TRIPS Agreement[3] which provide flexibility for member countries to formulate or amend their domestic intellectual property laws with a view to achieve a balance between intellectual property rights and socio-economic policies — which they consider necessary to protect public health. Lowering the threshold of patentability requirements would defeat the objective of the TRIPS Agreement to cater for public health needs as patenting of newer forms of drugs and availability of more affordable generics would be limited.

3. Patenting of medical methods

Malaysian patents law does not allow patenting of methods for the treatment of human or animal body by surgery or therapy, and diagnostic methods practised on the human or animal body[4]. Similarly, Article 27(3)(a) of the TRIPS Agreement also allows member countries to exclude "*diagnostic,*

therapeutic and surgical methods for the treatment of humans or animals" from patentability. The rationale behind this principle is ethical — it is to ensure that the general public has access to medical best-practices, knowledge and care at affordable costs. However, it is proposed in the TPP Agreement that surgical, therapeutic and diagnostic methods be patentable. Although the extent of patenting is yet unknown, it is now a matter of concern on how the negotiating governments would address the rising healthcare costs if medical methods were to be patented.

The impact of the TPP Agreement on access to medicines

On 30 August 2003, the WTO had proposed to waive the member countries' obligations under Article 31(f)[5] of the TRIPS Agreement thereby making it easier for poorer countries to import cheaper generics made under compulsory licensing if they are unable to manufacture the medicines themselves[6]. On 6 December 2005, the WTO member states agreed to accept a Protocol to Amend TRIPS Agreement ("the TRIPS Protocol"), making permanent the proposed interim waiver. As one of the signatories to the TRIPS Agreement, Malaysia is bound to make amendments to the Patents Act 1983 in order to conform to the TRIPS Protocol in the near future. This TRIPS Protocol and impending amendments to the Malaysian Patents Act 1983 would safeguard the interests of public health by giving leeway to poorer countries to gain access to affordable generics, even without relying on the proposed provisions of the TPP Agreement.

Conclusion

Concerns over the proposed provisions in the TPP Agreement should be considered fully, before a stand is taken on the same.

It is pertinent to note that the above proposed provisions are still under negotiation at the time of publication. This article shall be treated as an introduction to the subject matter and will be duly updated when further development of the negotiation is made available to the public.

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[1] Australia, Brunei, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, Vietnam

[2] See section 5 of the Patents (Amendment) Act 2000 (Act A1088)

[3] Article 8 of the TRIPS Agreement provides that "Members may, in formulating or amending their laws and regulations, adopt measures necessary to protect public health and nutrition, and to promote the public interest in sectors of vital importance to their socio-economic and technological development, provided that such measures are consistent with the provisions of this Agreement.

[4] Section 14 of the Patents Act 1983

[5] Article 31(f) of the TRIPS Agreement stipulates that patented products made under compulsory licensing "must be authorised predominantly for the supply of the domestic market of the Member authorising such use". This provision has effectively limited the ability of countries that cannot make pharmaceutical products from importing affordable generics from countries where pharmaceuticals are patented.

[6] See Doha Declaration on TRIPS and Public Health

EMPLOYMENT LAW

Who is my Employer?

IN THIS ARTICLE, PARVATHY DEVI RAJA MOORTHY LOOKS AT THE IMPORTANCE OF ASCERTAINING THE IDENTITY OF THE EMPLOYER WHEN LODGING A COMPLAINT OF UNFAIR DISMISSAL ESPECIALLY IN SECONDMENT CASES.

The correct identification of an employer is essential in the lodging of an unfair dismissal complaint pursuant to section 20 of the Industrial Relations Act 1967 where the relationship between the employee and the company is unclear. The court would have to determine whether the company before it is the employer prior to determining whether it is guilty of the complaint. In such a situation, the employee bears the burden of proving that the company he named is his employer. If he fails to do so, his claim against the company would fail.

A dispute as to who the employer is usually arises in cases of secondment where, unlike a transfer, the company posting the employee to another company still remains the employer. The Industrial Court in the case of **Bank Simpanan Nasional Finance Bhd & Anor v Omar Hashim**[1] held that secondment is a temporary transfer where the employee is subject to recall by his employer and is not a permanent employee of the other.

Based on the above definition, it would appear that the company to which the employee was seconded cannot be liable for a claim of unfair dismissal

since it was not the employer and, therefore, did not have the power to fire and hire[2]. This suggestion is supported by the recent case of **Geoffrey Allan William** ("Geoffrey") **v The University of Nottingham in Malaysia Sdn Bhd**[3] ("UN") where the Industrial Court had to determine whether or not UN was Geoffrey's employer. In this instance, Geoffrey was seconded to UN vide a secondment contract executed with his employer in the United Kingdom ("UK"). After the secondment contract ended, Geoffrey reported back to his employer in UK. However, to complicate matters, UN later offered Geoffrey a two-year contract and paid his salary. This led to Geoffrey's claim that UN was his employer.

In considering whether the new contract resulted in UN being the employer of Geoffrey, the Industrial Court found that "*the new contract given by the Malaysian University still referred to the terms and conditions of the claimant's substantive contract of employment of 2003 with the UK University*" and in the circumstances held that "*a new contract of employment could not be made with the Malaysian University*".

Accordingly, the Industrial Court cited from *The Law of Industrial Disputes*[4]

> "*...so long as the contract of service is not terminated, a new contract is not made and the employee continues to be in the employment of the original employer even if the employer orders the employee to do certain work for another person. The employee still continues to be in his employment.... The hirer may exercise control and direction in the doing of the thing for which he has hired the employee ... But if the employee fails to carry out his direction, he cannot dismiss him and can only complain to the actual employer*"

and held that UN had no power to terminate Geoffrey's employment as it was a third party in the tripartite agreement.

The Industrial Court held that the fact of who pays the salary is not conclusive of who the real employer is[5]. This is consistent with the decision of the Industrial Court in the case of **Actacorp Holding Bhd v Helen Tang Chiew Yien**[6]. However, companies should be aware that the position is different when it comes to statutory contributions, as the Court of Appeal in **Chong Kim Sang v Metratrade Sdn Bhd**[7] has stated that it would be one of the factors which indicate whether or not a person is an employee.

Conversely, there have been instances where the court, in perusing the facts of the case, had determined that the company to which an employee had been seconded to was the employer. For example, in the case of **KPMG Consulting (ASPAC) Sdn Bhd v Christopher M Meneze**[8] the Industrial Court found the claimant to be an employee because he was not treated in the same manner as other secondees, but instead was treated in the same manner as other employees.

In light of the above decisions, companies may minimise the risk of being found to be an employer of a secondee by keeping in mind that they do not have the power to hire or fire a secondee and, therefore, in the event there are issues with a secondee's performance or conduct, companies should report the same to the secondee's employer. Accordingly, if a company intends to make any statutory contributions on behalf of the employer, it is essential to ensure that there is clear documentation that states that the same is paid on behalf of the employer and a record of the reimbursement for such contributions is kept. Although this is not foolproof, it would show that the company was merely doing it on behalf of the employer. It is therefore advisable for the company to ensure that the secondee is aware of this arrangement and the fact it does not create an employee–employer relationship in writing. Lastly, the company should as far as possible ensure that the secondee, who is not an employee, is not treated like an employee.

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1 [2002] 1 ILR 272
2 **Yen Chee Yung and Matrix Valley Holding Sdn Bhd** [Award No 859 of 2009] — "*This Court agrees that Matrix Valley Holding (Southern) Sdn. Bhd. being the employer of the Claimant should be the competent authority to terminate the Claimant's service since it is still in existence*".
3 (Award No: 491 Of 2014) Decision handed down on 8 April 2014
4 Vol 1, 3rd Edition by O P Malhotra at p 246
5 "*Under the new contract, the Malaysian University had offered to pay him in ringgit. But this was merely an agreement the Malaysian University had with the UK University, it did not have the effect of transferring the service of the claimant to the Malaysian University.*"
6 [2005] 2 ILR 641
7 [2004] 2 CLJ 439
8 [2007] 4 ILR 678

TAX LAW

Are "Plant" and "Setting" Mutually Exclusive Concepts in Tax Law?

IN THIS ARTICLE, FOONG PUI CHI ANALYSES THREE COURT OF APPEAL DECISIONS ON CLAIMS FOR CAPITAL ALLOWANCES ("CAs") IN LIGHT OF A RECENT DECISION OF THE SPECIAL COMMISSIONERS OF INCOME TAX ("SCIT").

In a tax appeal that was recently concluded at the SCIT level, the taxpayer ("Taxpayer"), the owner and operator of two USGA golf courses and a clubhouse, had claimed CAs on the capital expenditure incurred on the construction of its golf courses and clubhouse under Schedule 3 of the Income Tax Act 1967 ("ITA"). However, the Director General of Inland Revenue ("Revenue") raised notices of additional assessment to disallow such claims. The Taxpayer appealed to the SCIT under section 99 of the ITA and, having heard the evidence and legal arguments of the parties, the SCIT decided in favour of the Taxpayer and allowed the Taxpayer's CA claims in full.

The word "plant" has long been the subject of debate in various tax cases both within and outside Malaysia. In order to qualify for CAs, one would have to determine whether a particular asset constitutes "plant" if it does not fall within the ambit of "machinery".

However, the word "plant" is but one of the many terms such as "income", "trade" and others not defined in the ITA. Hence, it is left to the courts to interpret them. As described by Lord Wilberforce in the case of **Commissioners of Inland Revenue v Scottish & Newcastle Breweries Ltd**[1]:

> "*...It naturally happens that as case follows case, and one extension leads to another, the meaning of the word gradually diverges from its natural or dictionary meaning. This is certainly true of 'plant'. No ordinary man, literate or semi-literate, would think that a horse, a swimming pool, moveable partitions, or even a dry dock was plant — yet each of these has been held to be so...*"

So the question now is — can a building, a large permanent structure, a theme park or even a golf course which stretches over acres of land also constitute "plant"? Does size really matter?

- **Ketua Pengarah Hasil Dalam Negeri v Tropiland Sdn Bhd**[2] **("Tropiland")**

In the recent case of **Tropiland**, the taxpayer had sought to claim CAs on the capital expenditure incurred on the construction of a multi-storey car park. The Court of Appeal had not only affirmed that the word "plant" must be given a broad and purposive meaning but it also held that the categories of "plant" are not closed and will grow over time. The Court of Appeal also went on to hold that a court should take a "holistic" approach and look at the taxpayer's operations as a whole:

> "*There is thus clearly a need to take a holistic approach in every case and look at the taxpayer's business in its entirety instead of taking particular facts in isolation. The need to refrain from viewing the taxpayer's business in a fragmented fashion when determining whether an apparatus is a 'plant' was reinforced by the High Court of Australia in **W. Nevill & Co. Ltd. V. Federal Commissioner of Taxation [1937] 56 CLR 290** where it was held:*
>
> > *'In my opinion the answer to this contention is to be found in a recognition of the fact that it is necessary for income tax purposes, to look at a business as a whole set of operations directed towards producing income.'*" (emphasis added)

Further, the Court of Appeal referred to the decision of Sir Donald Nicholls V-C in **Carr v Sayer**[3] where his Lordship held that:

> "*...the expression 'machinery or plant' is apt to include equipment of any size. If fixed, a large piece of equipment may readily be described as a structure, but that by itself does not take the equipment outside the range of what would normally be regarded as plant. The equipment does not cease to be plant because it is so substantial that, when fixed, it attracts the label of a structure or, even, a building.*
>
> *...and this follows from the above, equipment does not cease to be plant merely because it also discharges an additional function, such as providing the place in which the business is carried out...*" (emphasis added)

To illustrate the above, the Court of Appeal in **Tropiland** referred to the following foreign superior court cases in which large and permanent structures were held to be "plant" rather than a "setting" or a "place of business" due to the function or role which they play

in the respective businesses:

(i) in **Commissioners of Inland Revenue v Barclay Curle & Co Ltd**[4], the House of Lords held that: "*...every part of this dry dock plays an essential part in getting large vessels into a position where work on the outside of the hull can begin, and that it is wrong to regard either the concrete or any part of the dock as a mere setting or part of the premises on which this operation takes place. The whole dock is ... the means by which, or plant with which, the operation is performed...*";

(ii) in **Schofield (HM Inspector of Taxes) v R & H Hall Ltd**[5], the Court of Appeal of Northern Ireland held that: "*...the Respondents' activities, in which these silos participate, should be viewed as a whole and not piecemeal, that the functions of the silos in the Respondents' trade should be considered. ... The silos are not just buildings capable of being put to any purpose. They were specially built having been presumably designed, for the purpose of rendering better and more efficient the process of unloading and distribution...*"; and

(iii) in **Commissioner of Inland Revenue v Waitaki International Ltd**[6], the New Zealand Court of Appeal held that: "*...I refer to the building as a whole because I consider a piece meal approach treating the panels on the one hand and steel frame, roof and floor on the other as separate components, to be totally unreal ... On my assessment of the evidence the freezer or cold-store structure is an essential part of the refrigeration process operated by these taxpayers. The crucial importance of insulation in the refrigeration process is strikingly reflected ... No sensible businessman would have constructed the buildings in this way unless they wanted substantial insulation, and in my view the insulated panels must be regarded as a major and integral part of the structure ... the freezer and cold-store form part of the taxpayers' operations and are to be characterized as plant*".

Accordingly, based on the facts of Tropiland, the Court of Appeal concluded that the multi-storey car park, considered as a whole, clearly constitutes "plant" under the ITA as it is an integral part of the taxpayer's business, without which the taxpayer could not have generated its income. In other words, the multi-storey car park is the company's apparatus or tool by means of which the company's business activities are carried on. The Court of Appeal also pointed out that the multi-storey car park is something that the taxpayer used in its business and it is not part of its stock-in-trade.

Based on the decision of the Court of Appeal in Tropiland, it is obvious that "plant" can be extended to buildings or structures where the same constitute "an apparatus or a tool of the taxpayer by means of which business activities were carried on". In the words of Donovan LJ in **Jarrold v John Good & Sons Ltd**:

> "*...'setting' and 'plant' are not mutually exclusive conceptions. The same thing may be both. ... All the Income Tax Acts require in this context is that the plant shall have provided 'for the purpose of the trade', an expression wide enough to cover assets which play a passive as well as an active role in the accomplishment of that purpose.*" *(emphasis added)*

- **Ketua Pengarah Hasil Dalam Negeri v Resort Poresia Bhd**[8] ("Poresia")

A more recent case is the case of Poresia which involves a golf club business. In this case, although the Court of Appeal had decided in favour of the Revenue, it is crucial to note that the claim in Poresia was only confined to the grass and turfing and it did not cover the entire golf course and clubhouse of the taxpayer. Grass and turfing are merely one of the many categories of capital expenditure that would be incurred when constructing a golf resort.

The facts found by the SCIT in Poresia were also very limited as the only fact found by the SCIT was that the types of grass used were not synthetic grass and neither were they artificial. No fact was found as to the species and special features of the grass used or if the grass complied with international golf championship standards.

Further, the fact that the Court of Appeal's decision in Poresia was "more recent" than that of Tropiland does not mean that Poresia is somehow "more binding" than Tropiland. Based on the trite and well honoured principles outlined in **Young v Bristol Aeroplane Co Ltd**[9], where there are two conflicting Court of Appeal decisions, the court may choose which to follow regardless of which decision was earlier.

- **Ketua Pengarah Hasil Dalam Negeri v MSDC Sdn Bhd**[10] ("MSDC")

Apart from Tropiland and Poresia, the Court of Appeal's case of MSDC also dealt with a building/structure, namely the training ground of a driving school. In this case, although the Court of Appeal had reversed the decision of the High Court and decided in favour of the Revenue, no written judgment had been issued to set out in clear terms what the reasons behind the decision were. Thus,

in the absence of a written judgment, it is manifestly unsafe for the Revenue or any taxpayer to speculate on the grounds of the Court of Appeal's decision in MSDC.

Analysing the claims in the above three Court of Appeal cases, it would appear that **Poresia** and **MSDC** are narrow and superficial as they are only concerned with "surface type claims". They do not extend beyond the surface to cover excavation works, earthworks, irrigation, drainage and piping systems, landscaping, rockworks and so on, all of which could play a functional role in certain businesses.

Accordingly, the case of **Tropiland** may well be the preferred precedent among the three as a comprehensive analysis of the case law on CAs was undertaken by the Court of Appeal in **Tropiland** but not in **Poresia** and **MSDC**.

Conclusion

From the above, it is clear that "plant" and "setting" were never meant to be mutually exclusive concepts because it has been widely recognised in various cases that a building or a large permanent structure such as a dry dock, silo or car park complex can not only be the place within which a business is carried on but also the means by which the business is so carried on. It is the function of the asset in relation to the business, and not the size, that really matters.

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1 [1982] 2 All ER 230
2 (2013) MSTC 7,701
3 [1992] STC 296
4 [1969] 1 All ER 732
5 49 TC 538
6 [1990] 3 NZLR 27
7 [1963] 1 All ER 141
8 Civil Appeal No J-01-577-10
9 [1944] KB 718
10 Civil Appeal No W-01-63-00

CASE NOTE

Malaysian Newsprint Industries Sdn Bhd v Bechtel International Inc & B E & K International Inc

IN THIS ARTICLE, AMANDA MAN MEI XEN DISCUSSES THE CASE OF **MALAYSIAN NEWSPRINT INDUSTRIES SDN BHD V BECHTEL INTERNATIONAL INC & B E & K INTERNATIONAL INC** ON THE IMPORTANCE OF EVINCING IN WRITING THE INTENTION FOR DISPUTES TO BE SETTLED BY ARBITRATION.

Facts

In this case, Malaysian Newsprint Industries Sdn Bhd ("MNI") appealed against the decision of the Court of Appeal in affirming the High Court's order to grant a stay of proceedings pursuant to section 6 of the Arbitration Act 1952 ("the Act") which has since been repealed by the Arbitration Act 2005. Section 6 of the Act provided as follows:

> "*If any party to an arbitration agreement or any person claiming through or under him commences any legal proceedings against any other party to the arbitration, or any person claiming through or under him, in respect of any matter agreed to be referred to arbitration, any party to the legal proceedings may, before taking any other steps in the proceedings, apply to the court to stay the proceedings, and the court, if satisfied that there is no sufficient reason why the matter should not be referred in accordance with the arbitration agreement, and that the applicant was at the time when the proceedings were commenced and still remains ready and willing to do all things necessary to the proper conduct of the arbitration, may make an order staying the proceedings.*"

MNI and Betchel International Inc and B E & K International Inc ("BI") entered into a Technical Service Agreement ("TSA") where BI was to perform certain services. The project services were due to end on 30 September 1996. However, before the end of the period, the parties entered into negotiations to extend the period of the project services beyond 30 September 1996. During the negotiations for the extended period of the project services, six proposals were submitted by BI. In the High Court, MNI sued BI for breach of contract, negligence and breach of statutory duty. It was MNI's position that the sixth proposal, upon which MNI contended the pleaded contract was based on and was unlike the first five proposals, had an omission to incorporate any reference to the TSA or an express arbitration agreement. BI's position was that although section 2 of the Act requires an arbitration agreement to

be in writing, there was no requirement that it was to be by way of a formal agreement executed between parties.

Issues

In deciding the appeal, the Federal Court considered three questions:

Question 1
Whether, for the purposes of an application for a stay under section 6 of the Act, an arbitration agreement can be incorporated into the contract upon which the action is based without a written incorporation of the arbitration agreement itself.

Question 2
Whether, for the purposes of an application for stay under section 6 of the Act, the court can look beyond the contract upon which the action is based for an arbitration agreement which does not appear in and has not been incorporated in writing into the contract which the action is based.

Question 3
Whether, for the purposes of an application for stay under section 6 of the Act, the court can investigate, determine and make a finding that the operative contract between MNI and BI is other than the one which MNI contends is the operative contract and upon which MNI had commenced its action.

The principal issue in the courts was whether the contract giving rise to BI's engagement included an arbitration clause. Both the High Court and Court of Appeal held that the engagement was subject to a clause requiring the dispute to be referred to arbitration and for that reason MNI's case before the High Court was stayed pursuant to section 6 of the Act.

Decision and analysis of the Federal Court

The Federal Court, in allowing the appeal, held that there was no agreement in writing in the pleaded contract to refer to any dispute in arbitration. As such no stay of proceedings should be granted under section 6 of the Act.

The Federal Court held that the Court of Appeal fell into error when it incorporated the arbitration agreement by drawing inferences from the conduct of parties or documents other than the contract document itself. The court was not at liberty to find an arbitration agreement by drawing inferences without such an agreement being produced in writing or evidenced in writing. It was irrelevant that there was another arbitration agreement that was applicable to another document as held by the High Court.

Although the courts have always adopted a minimal interference for parties wishing to have their dispute resolved by way of arbitration, such an intention must be evidenced by way of clearest terms reduced in writing as required under section 2 of the Act.

Conclusion

The case highlights the importance for parties wishing to have their disputes resolved by way of arbitration to ensure that such intention is expressly and clearly provided for in writing in the agreement entered between the parties.

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