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EMPLOYMENT LAW

Can an Employer Unilaterally Vary Service Charges?

IN THIS ARTICLE, WONG KIAN JUN DISCUSSES THE CASE OF *NATIONAL UNION OF HOTEL, BAR & RESTAURANT WORKERS, PENINSULAR MALAYSIA V AYER KEROH RESORT SDN BHD* ON WHETHER AN EMPLOYER CAN UNILATERALLY VARY SERVICE CHARGES

Facts

A hotly debated issue these past few months is the issue of service charge imposed by hotels and restaurants. In the recent case of *National Union of Hotel, Bar & Restaurant Workers, Peninsular Malaysia v Ayer Keroh Resort Sdn Bhd*, the Industrial Court considered whether Mahkota Hotel Melaka ("Hotel") could reduce the service charge imposed on customers from 10% to 5%. A collective agreement was entered into between the Hotel and the Union which had provided for the imposition of service charge of 10%.

The Industrial Court had previously held that a party can only vary the terms of a collective agreement under very special circumstances and financial distress would not amount to a special circumstance. In the case of *Prestige Ceramics Sdn Bhd v Kesatuan Pekerja Pembuatan Barangan Bukan Logam & Anor*, the High Court held that the Industrial Court cannot automatically assume that financial distress would not amount to a special circumstance without first evaluating the underlying factors which had resulted in the distressed financial position in the first place. In *Prestige Ceramics*, the Asian Financial Crisis of 1997 resulted in a severe reduction in the demand for ceramic tiles and the High Court was of the view that the financial crisis could not have been foreseen by the company. Subsequently, in the case of *Metal Industry Employees Union v Yodoshi Malleable (M) Sdn Bhd*[1] the occurrence of a fire had exacerbated the company's financial woes and for this reason the Industrial Court was of the view that it amounted to a special circumstance.

In the present case, the Hotel had been imposing a service charge of 10% on its customers for room, food and beverages. However, the Hotel argued that it was left with no alternative but to reduce the service charge imposed on its customers from 10% to 5% for the following reasons:

- It had suffered financial losses and reduced revenues for the year 2013 and 2014.
- In order to comply with the Minimum Wages (Amendment) Order 2012, the Hotel had to increase the salaries and wages for its employees with effect from 1 October 2013 and this resulted in significant increase in the overall wage bill. Not only were employees' salaries increased to meet the minimum wage of RM900, longer serving employees were given a proportionate increase based on their length of service.
- There was increased competition from other hotels in the area and occupancy rates were on the decline.

Decision

After the service charge was reduced, the Union filed a complaint of non-compliance of the collective agreement with the Industrial Court. The Industrial Court in its award held by a majority that the above factors amounted to a special circumstance for the following reasons:

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- The collective agreement between the Union and the Hotel was signed in 2010 and the Minimum Wages (Amendment Order) 2012 was not within the contemplation of the parties when the collective agreement was entered into.

- After the implementation of the minimum wage, the Hotel had experienced a significant increase in its wage bill despite a reduction in the number of employees.

- Furthermore, the Hotel continued to suffer a drop in revenue and incurred losses.

Conclusion

From the decision of the Industrial Court, it is now clear that legislation passed by Parliament can amount to a special circumstance if it directly results in a company's financial distress. In addition, in order to successfully vary a collective agreement, an employer must show the events which led to the financial distress had not been contemplated by the parties when the collective agreement was entered into and was beyond the control of either party. The decision of the Industrial Court affirms the position that financial distress can amount to a special circumstance and must not be dismissed outright by the court.

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[1] [2013] 3 MELR 431

CORPORATE LAW

The Framework of Equity Crowdfunding in Malaysia

IN THIS ARTICLE, AQILAH LOKMAN ANALYSES THE FRAMEWORK OF EQUITY CROWDFUNDING IN MALAYSIA

The Securities Commission ("SC") released the *Guidelines on Regulation of Markets under Section 34 of the Capital Markets and Services Act 2007* ("Guidelines") on 10 February 2015 to introduce the new requirements for the registration of equity crowdfunding platforms and provide governance arrangement for the operator of such platforms.

The Guidelines were issued by the SC pursuant to Section 377[1] of the *Capital Markets and Services Act 2007* ("CMSA") read together with Subdivision 4, Division 2 of Part II of the CMSA.

What is crowdfunding?

Crowdfunding is described as "*the use of small amounts of money, obtained from a large number of individuals or organisations, to fund a project, a business or personal loan, and other needs through an online web-based platform*"[2] .

There are a few types of crowdfunding activities, such as donation crowdfunding, reward crowdfunding, peer-to-peer lending and equity crowdfunding ("ECF"). ECF refers to a form of corporate fundraising that envisages start-up or other smaller companies ("issuers") obtaining seed or other capital through small equity investments from relatively large numbers of investors, with online portals publicising and facilitating such offers to crowd investors[3].

The ECF concept consists of three important roles:

i. the project initiator (the "issuer");

ii. individuals who support the idea (potential "investor"); and

iii. the platform that brings the parties together to launch the idea (the "ECF operator").

Why the need for crowdfunding?

The SC's *Public Consultation Paper No 2/2014 on Proposed Regulatory Framework For Equity Crowdfunding* ("Public Consultation Paper") explained that crowdfunding can facilitate and encourage innovation, and increase productivity, competitiveness and growth. The availability of ECF as a financing option could increase competition among suppliers of capital to start-ups and other small enterprises, resulting in a potentially lower cost of capital for the issuers[4]. This is in line with the SC's mission to promote, maintain and facilitate a fair, efficient, innovative and competitive market.

How does crowdfunding work?

ECF operator

An ECF operator will be subject to the Registered Electronic Facility ("REF") Requirements which are currently set out under Subdivision 4 of Part II of the CMSA[5]. All ECF operators must be locally incorporated[6]. Any person who operates an ECF platform in Malaysia without being registered as an REF under the CMSA commits an offence under the CMSA and, if convicted, may be fined up to RM5 million or to imprisonment up to five years, or both.

The operator plays a critical role in ensuring confidence in the ECF platform. An ECF operator must carry out proper due diligence on prospective issuers to ensure the issuers are qualified investors to participate on the platform. The ECF operator must also monitor issuers to ensure that the fundraising limits imposed are not breached and monitor investors to ensure that the investment limits are not breached[7].

The operator is also required to ensure that funds obtained from investors are safeguarded in a trust account until the targeted amount is achieved. The ECF operator is prohibited from providing any financial assistance to investors to invest in shares of an issuer hosted on its platform or compensating any finder or introducer for providing the ECF operator with information about potential investors[8].

Issuers

Only locally incorporated private companies (excluding exempt private companies) will be allowed to be hosted on the ECF platform[9]. An issuer shall not be allowed to be hosted concurrently on multiple ECF platforms.

Certain companies, such as public listed companies and their subsidiaries, companies with no business plans and companies with paid up share capital exceeding RM5 million, will not be allowed to raise funds through the ECF platforms.

Under this framework, an eligible issuer is only allowed to raise up to RM3 million within a 12-month period, and may only raise a maximum amount of RM5 million through the ECF platform.

The investor

A sophisticated investor is not subject to any restrictions as to the amount he wants to invest in a project. A retail investor, however, is only allowed to invest a maximum of RM5,000 per issuer with a total amount not exceeding RM50,000 within a 12-month period. An angel investor on the other hand may invest a total of RM500,000 in a 12-month period[10]. An angel investor is defined in the Guidelines as an investor that is accredited by the Malaysian Business Angels Network.

ECF investors are given a six-day cooling off period, within which they may withdraw the full amount of their investment. In addition, if there is any material adverse change relating to an issuer, the investors must be notified of such change. The investors will be given the option to withdraw their investment if they choose to do so within 14 days after the said notification[11].

Financial disclosure

The requirements to disclose financial information are provided as follows[12]:

i. Offerings below RM300,000: No requirement to file financial information, but the ECF operator has the discretion to request for certified financial statements/information from the issuer's management for verification purposes.

ii. Offerings between RM300,000–RM500,000: Audited financial statement where applicable. Where audited financial statements are unavailable, certified financial statements/information by the issuer's management may instead be filed with the ECF operator.

iii. Offerings above RM500,000: Audited financial statements.

Conclusion

Many countries such as the UK, US, New Zealand and Australia have long introduced equity crowdfunding as an alternative source for private companies to raise capital. However, since ECF is relatively new in Malaysia, issuers may be reluctant to accept crowdfunding as a viable source of funding. There are also concerns over the commercial viability for those who get chosen to operate the platform. On the other hand, the introduction of ECF will, hopefully, help startups and new entrepreneurs grow and expand their businesses as anticipated by the SC.

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[1] Section 377 provides the SC may issue guidelines and practice notes in respect of the CMSA or any particular provision of the CMSA.
[2] Securities Commission *Public Consultation Paper No 2/2014 Proposed Regulatory Framework For Equity Crowdfunding* dated 21 August 2014 at page 3.
[3] Securities Commission *Public Consultation Paper No 2/2014 Proposed Regulatory Framework For Equity Crowdfunding* dated 21 August 2014 at page 3.
[4] Securities Commission *Public Consultation Paper No 2/2014 Proposed Regulatory Framework For Equity Crowdfunding* dated 21 August 2014 at page 4.
[5] Registration of Electronic Facilities.
[6] Para 11.04 of the Guidelines.
[7] Para 11.05 of the Guidelines.
[8] Para 11.12 of the Guidelines.
[9] Para 11.13 of the Guidelines.
[10] Para 11.21 of the Guidelines.
[11] Para 11.07 of the Guidelines.
[12] Para 11.19 of the Guidelines.

CASE NOTE

Ishmael Lim Bin Abdullah v Pentadbir Tanah Persekutuan & Pentadbir Tanah Gombak

IN THIS ARTICLE, NIK AZILA SUHADA CONSIDERS THE CASE OF *ISHMAEL LIM BIN ABDULLAH V PENTADBIR TANAH PERSEKUTUAN & PENTADBIR TANAH GOMBAK* ON WHETHER THE REQUIREMENT FOR AN ENDORSEMENT OF THE MEMORIAL ON THE TITLE TO A LAND IS A MERE FORMALITY.

Introduction

On 18 November 2014, the Federal Court declined Mr Ishmael Lim's ("Mr Lim") application for leave as the Court found that Mr Lim had not satisfied the legal test that would warrant the Federal Court allowing his application for leave to appeal. The result? Mr Lim will now have to vacate the land which he had been occupying for 40 years. Both the High Court and the Court of Appeal decided that Mr Lim wasn't the proprietor of the land despite the fact that title searches of the land revealed Mr Lim as the proprietor.

Facts

In 1973, the Acquiring Authority[1] declared its intention to compulsorily acquire a piece of land located in Rawang, Selangor ("the Land"). The Land was needed for the construction of a military college and, therefore, it was to be compulsorily acquired pursuant to the *Land Acquisition Act 1960* ("the Act"). At that time the Land was owned by Lim Kim Cheng. As required under the Act, an inquiry was held before the Land Administrator and Lim Kim Cheng was awarded RM6,187.80 by way of compensation for the Land in October of 1973.

In March 1974, and in compliance with the requirements of the Act, the Acquiring Authority caused to be issued a statutory notice that the State Authority has taken formal possession of the land. The notice is by way of *Borang K* that serves to notify the owner that the Land has now reverted back to the State. In October of the following year the Land was transferred from Lim Cheng Kim to Lim Yew Kay, Mr Lim's father. In January 1986, the Land was re-alienated by the State Authority to the Federal Lands Commissioner ("the FLC") with a new title.

In December of 1992, presumably not knowing that the Land was now registered to the FLC, Lim Yew Kay transferred his ownership of the Land to Mr Lim. The latter than charged the Land to a bank as collateral for a loan. Mr Lim claimed that he had been diligently paying the assessments and quit rent in respect of the Land since 1993 and had made several land title searches on the Land from 1993–2005 and at all times the land searches confirmed that he was the registered proprietor of the Land.

In June of 2002, a memorial was duly endorsed on the title to the Land in respect of the acquisition of the Land. In November of that year, Mr Lim was informed by the Land Administrator of the District of Gombak ("the Land Administrator") that the Land had been compulsorily acquired under the Act in 1974. In March of 2005, Mr Lim was in receipt of a notice to vacate the Land and to demolish all structures found on the Land.

The High Court

Mr Lim commenced proceedings in the High Court against the FLC and the Land Administrator. He sought an injunction to restrain the FLC and/or the Land Administrator from entering and taking possession of the Land and a declaration that he is the lawful registered owner of the Land. The High Court dismissed his claim on 11 March 2010.

The Court of Appeal

In May 2014, the Court of Appeal dismissed Mr Lim's appeal from the High Court. The Court of Appeal affirmed the High Court's ruling that, upon the issuance of *Borang K* in 1974, the Land had vested in the state authority notwithstanding that there was an omission to endorse the memorial on the title which is a requirement under section 23 of the Act. The Court of Appeal agreed with the finding of the High Court that the requirement for an endorsement of the memorial under section 23 of the Act was a formality and the omission to do so did not invalidate the compulsory acquisition process. As such, the purported transfers of the Land in 1975 to Mr Lim's father and again in 1992 to Mr Lim were all void and ineffective. The acquisition process had been concluded in 1974.

The Federal Court

Mr Lim then sought leave from the apex court to appeal against the decision of the Court of Appeal. He postulated eight questions of law to the Federal Court. The chief question being whether, as a matter of law, the requirement for the Land Administrator to endorse the *Borang K* on the register document of title, as required by section 23 of the Act, is merely directory and not mandatory.

On 18 November 2014, the Federal Court refused to grant leave to appeal to Mr Lim. The result was that the Court of Appeal's rulings that the compulsory acquisition of the Land had been completed in 1974 when *Borang K* was issued, that the requirement for an endorsement of the memorial under section 23 of the Act was a formality and that the omission to have a memorial endorsed pursuant to section 23 of the Act did not invalidate the compulsory acquisition process, all remained good law.

In an earlier decision, the High Court in *Hong Lee Trading & Construction Sdn Bhd v Taut Ying Realty Sdn Bhd*[2] was asked to determine the actual date of acquisition under the Act. Was it when the *Borang K* was issued and/or served *or* was it after the memorial of *Borang K* was made on the register document of title as required by section 23 of the Act? Section 23 of the Act reads:

> ***"23 Entry in register***
>
> *The proper registering authority, upon receipt of the notice in Form K, or the Land Administrator of his own motion*

after completing Form K, shall, upon the register document of title or other appropriate record in his possession as specified in s9 (2) or (3), make with respect to any scheduled land [memorial]-

(a) that the whole of such land has been acquired and has vested in the [State Authority] [or, in the case of a parcel of a subdivided building, in the person or corporation on whose behalf the parcel has been acquired]; or

(b) that so much of the land as is specified in the last column of the schedule to such Form has been acquired."

(Emphasis ours)

In *Hong Lee Trading*, Lamin J, who later retired as the President of the Court of Appeal, observed that the land sought to be acquired by the State Authority would vest in the latter upon (a) *Borang K* being issued and served on the land owner and (b) a memorial of *Borang K* is entered on the register document of title either by the proper registering authority or the land administrator. Lamin J's decision in *Hong Lee Trading* was brought to the attention of the High Court. The learned judge however was not inclined to agree with Lamin J's assessment. A reading of the appellate court's grounds of judgment reveal that the Court of Appeal did not discuss Lamin J's *ratio* in *Hong Lee Trading.*

Another provision of the Act appears to have been overlooked by the Court of Appeal. Section 66 of the Act reads:

"66 Land to vest free from incumbrances

Upon the making of a memorial under s 23 in respect of any scheduled land, the land shall vest in the State Authority as State land [or, in the case of parcel of a subdivided building, in the person or corporation on whose behalf the parcel was acquired,] free from incumbrances."

(Emphasis ours)

The High Court judge whose attention was drawn to section 66 expressed that "*s. 66 of the LAA only sought to unequivocally confirm or affirm the vesting of the said Land on the State Authority as State Land free from encurambrances*" and nothing beyond.

Postscript

The Federal Court's disinclination to allow Mr Lim's application for leave deprived the apex court of Malaysia an opportunity to decide the crucial issue at hand — whether the requirement for an endorsement of the memorial on the title to the land is a mere formality or whether its omission rendered the acquisition incomplete such that the land could not be said to have vested in the State Authority. As the law now stands, section 23's requirement, despite being cast in a mandatory language, has been held by the Court of Appeal to be a mere formality — a breach of which bears no consequences to the State Authority.

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[1] State Authority
[2] [1991] 1 MLJ 250

FINANCIAL SERVICES

The Securities Commission's Guidelines on Unlisted Capital Market Products under the Lodge and Launch Framework

IN THIS ARTICLE, HONG JAYEEN LOOKS AT THE SECURITIES COMISSIONS'S NEW GUIDELINES ON UNLISTED CAPITAL MARKET PRODUCTS UNDER THE LODGE AND LAUNCH FRAMEWORK

Introduction

The Securities Commission ("SC") had on 9 March 2015 issued the new *Guidelines on Unlisted Capital Market Products under the Lodge and Launch Framework* (the "New Guidelines"). The New Guidelines set out the requirements applicable to those who wish to make available unlisted capital market products to sophisticated investors in Malaysia.

From 1 June 2015 ("Effective Date"), unlisted capital market products will no longer require the SC's authorisation or recognition under section 212(5) of the *Capital Markets Services Act 2007* ("Old Regime") provided that all the applicable requirements under the New Guidelines have been complied with[1].

Unlisted capital market products include:

- wholesale fund;

- structured products;
- private debt securities ("PDS") and *sukuk*; and
- asset-backed securities.

The New Guidelines will supersede the existing guidelines in relation to the abovementioned unlisted capital market products. Nonetheless, certain provisions of the New Guidelines, particularly those relating to continuous obligations shall be applicable to unlisted capital market products which have been approved, authorised or recognised by the SC prior to the Effective Date[2].

PDS and *sukuk*

This article shall only focus on the salient changes effected by the New Guidelines applicable to unlisted PDS and *sukuk*, as set out in Part 3 of Section B.

The offering of unlisted PDS and *sukuk* to persons outside of Malaysia is also subject to the New Guidelines.

Timing of the lodgment

Pursuant to the New Guidelines, an issuer of PDS or *sukuk* or its principal adviser is responsible for lodging all information and documents as stipulated under the New Guidelines via an online system to be made available on the SC's website on the Effective Date (the "System") either prior to the issuance (applicable for PDS or *sukuk* issued on a bullet basis) or prior to the first issuance (applicable for PDS or *sukuk* issued on a programme basis). An issuer of ringgit denominated *sukuk* has to fulfill an additional requirement to seek the endorsement of the *Shariah* Advisory Council[3] prior to the lodgment[4] and Section C of the New Guidelines.

Timing of the launch

From the Effective Date, any unlisted PDS or *sukuk* has to be issued within 60 business days from the lodgment date, which shall take effect only after all payments due have been cleared. In the case of PDS or *sukuk* issued on a programme basis, only the first issuance has to be issued within the 60-Business-Days time frame. No issuance will be allowed once the time limit has lapsed and a new lodgment has to be made (together with payment of applicable fees) via the System to the SC. A post issuance notice must be submitted to the SC via the System within seven business days from the issuance date (if issued on a bullet basis) or seven business days after every subsequent issuance date (if issued on a programme basis). Any late submission will attract a late submission fee as stipulated under the SC's fees regulations. The post issuance notice requirement is also applicable to any PDS or *sukuk* approved under the Old Regime if any of the issuance was made after the Effective Date.

Upsizing of PDS or *sukuk*

The position of the SC on the upsizing of PDS or *sukuk* issued on a one-off basis remains the same under the New Guidelines — any upsizing of such PDS or *sukuk* is not allowed once such PDS or sukuk have been issued.

Upsizing of PDS or *sukuk* on a programme basis (whether the upsizing is done before or after the issuance) is permitted under the New Guidelines by amending the total issue size of the PDS or *sukuk* and submitting all information and documents for a new lodgment with the SC. Fees will be charged only on the increased portion[5].

Revisions to the principal terms and conditions

Once the principal terms and conditions ("PTC") have been lodged under the New Regime, revisions are allowed to be made in the following manner:

- for pre-issuance revisions (or in the case of PDS or *sukuk* issued on a programme basis, prior to the first issuance), such revisions can be made by re-lodging all information and documents to the SC. A fee, which is equivalent to 10% of the relevant fees paid at the initial lodgment, will be charged[6];
- for pre-issuance revisions of PDS or *sukuk* approved under the Old Regime, such revisions would have to be made by submitting an application to the SC manually for approval[7];
- for post issuance revisions, such revisions can be made by updating the terms in the original lodgment form within 14 Business Days of the proposed revision coming into effect. An issuer also has to comply with the requirements set out in Chapter 6. No fee will be charged[8].

Further, for PDS or *sukuk* denominated in ringgit, in the event any such revisions involve any *Shariah*-related issues, the issuer (through its principal adviser) must first refer such matters to the *Shariah* Advisory Council for endorsement, prior to submitting the re-lodgment or the update to the SC[9].

Conclusion

The SC has stated in the New Guidelines that the lodge and launch framework seeks to promote process efficiency, shorten time to market and provide certainty of product offering[10]. The changes, for example, migration to an electronic system, shorter time limit to launch appear to promote the stated aims of the SC for efficiency and shorter time to market.

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[1] Paragraph 1.11 of Chapter 1

2 Paragraph 1.1 of the Frequently Asked Questions on the Requirements under the Guidelines on Unlisted Capital Market Products under the Lodge and Launch Framework ("FAQ").

3 Section 2(1) of the Capital Markets Services Act 2007:

"*Shariah* Advisory Council means Shariah Advisory Council established under section 316A

Section 316A Establishment of Shariah Advisory Council for Islamic capital market

(1) The Commission may establish a *Shariah* Advisory Council for Islamic capital market which shall be the authority for the ascertainment of the application of *Shariah* principles for the purposes of Islamic capital market business or transaction.

(2) The *Shariah* Advisory Council may determine its own procedures."

4 Paragraph 4.01 of Chapter 4.

5 Paragraph 6.12 of Chapter 6 of Part 3 and Paragraph 4.13 of the FAQ.

6 Paragraph 4.12 of the FAQ.

7 Paragraph 4.18 of the FAQ.

8 Paragraph 4.13 of the FAQ.

9 Paragraph 6.16 of Chapter 6.

10 Paragraph 1.10 of Chapter 1

INTELLECTUAL PROPERTY

Protecting Your Intellectual Property from Misappropriation and Loss by Employees and Competitors

IN THIS ARTICLE, TENG WEI REN RECOMMENDS THE IMPLEMENTATION OF A ROBUST INTELLECTUAL PROPERTY POLICY TO PROTECT INTELLECTUAL PROPERTY ASSETS FROM FALLING INTO THE HANDS OF COMPETITORS THROUGH ACTIONS OF ROGUE EMPLOYEES

Introduction

Today's knowledge-based economy has given rise to new sources of competition. The development and acquisition of new ideas and innovation have become the core competence for a successful corporation; perhaps over and above the control of markets and raw materials. Strategic management of intellectual property ("IP") will ensure market dominance and continuing profitability.

Employees are the wellspring of a corporation's IP. Inventions, trademarks, designs, technology, know-how and trade secrets are fairly obvious IP. However, even seemingly trivial work done by employees, such as compilation of databases or creation of marketing brochures, may also produce IP of significant value.

As a general rule, IP created by an employee in the course of carrying out his or her job duties will automatically belong exclusively to the employer. For example, the *Copyright Act 1987*, the *Industrial Designs Act 1996* and the *Patents Act 1983* provide that a work or industrial design or invention created by an employee in the course of employment is deemed to be owned by or otherwise assigned to the employer in the absence of any provision to the contrary in the agreement between the parties.

Be that as it may, there are areas of difficulty. For example, an employer may encounter problems in attempting to claim proprietorship over an industrial design that was created by an employee using the employer's means and materials where the creation of the design was outside the scope of the terms of the employee's employment.

Confidential information is different from copyright, industrial designs, trademarks and patents. There is no system in place for the registration of confidential information. The right of the employer to prevent the unauthorised use and disclosure of confidential information is premised upon the relationship between the employer and the employee to whom the employer had confided the confidential information. Protection can only arise by keeping the information secret. Once the information has been disclosed to the public, it loses the quality of confidentiality and other parties will be at liberty to use the information.

IP's intangible and fluid nature leaves it vulnerable to misappropriation by employees who are minded to set up a business in competition with the employer's business, or by employees who have been "poached" by a competitor. Hence, the need to protect these valuable IP assets from such rogue employees has become more critical.

Implementing an IP policy

In light of the above, it is important for a corporation to establish a corporate policy with respect to the ownership, control and management of IP that the corporation has created or acquired. The policy should define not only the responsibilities of employees but also of third parties who may have dealings with the corporation with regard to IP, such as contract employees as well as contractors and consultants employed by the corporation. A robust IP policy will typically address:

- the ownership of IP;
- the identification and recording of IP;
- the transfer of the corporation's IP;
- confidentiality arrangements;

- IP evaluation, reporting and auditing; and
- the identification of roles and responsibilities of employees and ex-employees.

These key areas are further addressed below.

The ownership of IP

IP may be created by employees so it is important that the corporation's ownership of such IP be perfected and preserved. IP created by employees of a corporation in the course of their employment vests in the corporation, as a general rule. In instances where an employee creates any IP outside his or her normal course of employment, with the use of the corporation's resources, it would be advisable for the contract of employment to stipulate that such IP is deemed to belong to the corporation and to require that the IP be assigned by the employee to the corporation. Similar arrangements should also apply to third parties engaged by the corporation as it would be advisable for a formal deed of assignment of the IP to the corporation be executed to avoid ambiguity in respect of the ownership of the IP.

Employees and third parties should be required to obtain written approval from a designated officer of the corporation if they desire to use, reproduce or distribute externally the corporation's IP, even where the use is for personal projects or in their private capacity. An employee or third party who becomes aware of any unauthorised use or dealing in the corporation's IP should be required to report the unauthorised use or dealing to the corporation.

In the creation of IP, a corporation may need to engage the services of third parties such as universities, suppliers, design houses and vendors, especially where an interdisciplinary approach is required. The ownership of the resulting IP from such a collaborative effort may not necessarily vest in the corporation by operation of law. For example, the IP created by an individual who is not an employee of the corporation may arguably be vested in his employer.

Further, authors of a joint work are co-owners of copyright in the work and joint inventors of an invention are the co-owners of the right to the patent for it unless, for instance, the authors or inventors are employees of the corporation. Thus, at the outset the agreement governing the collaboration should set out well drafted IP clauses not only pertaining to the ownership of the IP but the nature and limitations of each party to exploit the IP. Such a clause should further provide that the inventors and authors agree to assign the IP to the corporation.

The identification and recording of IP

The presence of a system to identify and record IP ensures that a corporation's IP are identified and monitored. Such a system further ensures the efficient utilisation and commercialisation of the IP. The IP should be identified by recording the assets, their ownership and if relevant their creators where the IP is created by an employee in the course of his or her duties, by contractors, by consultants or in the conduct of a research project with an external party. The corporation will generally need to actively manage its IP that are important to its operations or which contribute significantly to achieving its objectives or that is an outcome of the investment of its resources or that has been or may be included in its commercialisation activities.

While IP notices need not be published as a prerequisite for establishing IP rights, IP notices nonetheless function to put the public and trade on notice of the corporation's claims to ownership of the IP. Proprietary rights attached to the contents of documents or to a trademark may be easily indicated with the affixation of the symbol "©" (for copyright works), ® (for registered trademarks), or "TM" (for registered and unregistered trademarks). Applications should be made expeditiously to register IP for which a registration regime exists ie copyright, trademarks, industrial designs and patents. Registrations should be made in the name of the corporation.

When a new IP is identified as having potential commercial value, it must be reported to a designated officer of the corporation for the execution of protective measures. The new IP and information and know-how in relation to the IP must be kept confidential through proper use of confidentiality agreements and by marking documents containing such materials with the words "Private and Confidential". Where practicable, IP should be kept physically or electronically secure.

Transfer of the corporation's IP

A well implemented IP transfer policy will not only ensure the effective commercialisation of the IP but also encourage the production and growth of valuable inventions, ideas and other creative works. Employees who create any IP are responsible for disclosing the same to the corporation. Such disclosure should be required to be made in advance of any presentation, publication, display or disclosure to the general public as failure to do so may result in the loss of the corporation's rights to such IP. Advance disclosure will further allow strategic measures to be taken to safeguard the corporation's interest in the IP, including the need to apply for the formal registration of such interest such as in cases of patentable inventions and registrable industrial designs.

The corporation's IP should not be transferred by assignment, licence, sale or otherwise without prior approval of a designated officer/IP officer of the corporation. Employees are to be made aware that they are to use the corporation's IP solely for the purposes of performing his or her duties in the course of employment and on a non-transferable licence. Any employee's grievance in respect of the transfer, commercialisation or ownership of IP ought to be resolved using the corporation's prevailing grievance policy and procedure.

Confidentiality arrangements

Confidential information may need to be accessed by or be made available to employees and other parties in the course of the conduct of the corporation's business. A culture of secrecy concerning confidential information must be inculcated among employees. Generally, while an employee remains employed with the employer, the employee owes a duty to act in the employer's best interest. After termination of such employment, the law allows the employee to use his or her full skill and knowledge, eg know-how and show how, even if such use is for the purposes of competing with his or her former employer. The steps below may be useful to avoid situations where an ex-employee unfairly asserts that such skill and knowledge were acquired by him or her in an honest manner.

Employees must keep confidential any confidential information to which he or she has access and only use it for the purpose for which it is supplied. A "need-to-know" policy should be implemented where access to information should be confined to only the employees who need to know the information to be able to do their job.

Third parties must keep confidential any confidential information to which he or she has access and only use it for the purpose for which it was supplied, in each case as if he or she were an employee of the company. Where parties have not properly entered into a business relationship but are in an exploratory phase, a non-disclosure agreement may be executed between the corporation and the third party to safeguard confidential information from being compromised.

IP evaluation, reporting and auditing

The adoption of a culture of evaluating, reporting and auditing IP is necessary in order to identify important aspects such as the corporation's risk management, company practices and governance. This will provide constructive insight into the strengthening of the corporation's operations and commercialisation of its IP.

A general IP audit involves:

- the identification and recordation of IP required by the corporation to run its business;
- the determination of the ownership and legal status of such IP;
- the assessment of the risk of such IP being infringed or infringing the rights of third parties; and
- ascertaining the steps required to maintain the rights to the continued use of the IP.

An IP audit should ideally be carried out by or under the supervision of personnel with sufficient IP-related legal knowledge as well as understanding of the corporation's business and future plans. There should also be a system to continuously review the effectiveness of the IP management system.

The identification of roles and responsibilities of employees and ex-employees

Employees must be made aware of their respective roles and responsibilities to ensure that they are able to implement steps to safeguard the corporation's IP.

A designated personnel/IP officer may be appointed to exercise the corporation's powers and functions under the IP policy. The IP officer's role and responsibilities include:

- auditing and identifying the corporation's IP;
- authorising the acquisition of formal protection if required;
- providing final sign off for commercialisation of the IP;
- receiving reports of infringement and implementing "take down notices" for content on the electronic medium in the event that the corporation should receive such a notice; and
- providing advice, and negotiating and drafting agreements where required.

Depending on the nature of the corporation's IP, it may be necessary to appoint a committee to carry out the above mentioned responsibilities where the committee may constitute personnel with technical and marketing knowledge and experience, in addition to legal personnel. A standard procedure must be implemented when employees leave the corporation. Firstly, the departing employee's access to any of the corporation's confidential and/or sensitive information such as those residing in document management systems should be revoked or otherwise limited. An exit interview should be conducted to ensure the return of any materials constituting confidential information to the corporation and to remind the departing employee of his or her duty of confidence to the corporation. The exit interview should be conducted with the aim of:

- identifying any IP that has been developed or is in the course of development by the departing employee;
- learning of the departing employee's further plans, more specifically whether the departing employee intends to join a competitor or to start his or her own business; and
- addressing the departing employee's concerns on his or her obligations *vis-à-vis* the corporation's IP.

If there is any suspicion of misappropriation of the corporation's IP by a departing employee, full scale investigations should be conducted which may necessitate forensic analysis of electronic devices used by the departing employee, such as laptop computers. When an employee leaves the corporation, it must be ensured that all of his or her means to remotely access the corporation's data are disabled.

Conclusion

An IP Policy should be an essential part of any business plan and will go a long way to facilitate a successful business.

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TAX LAW

Direct Taxes and Indirect Taxes — a Comparison between Entities in Malaysia and Labuan

IN THIS ARTICLE, GOH KA IM HIGHLIGHTS THE DIFFERENCES IN TAX TREATMENTS FOR ENTITIES IN MALAYSIA AND LABUAN.

Introduction

Much has been written about the beneficial tax treatment currently enjoyed by Labuan entities in the Labuan International Business and Financial Centre ("Labuan IBFC"), particularly under the *Labuan Business Activity Tax Act 1990* ("LBATA").

Such beneficial tax treatment is in relation to the direct tax on profits imposed on Labuan entities. However, there are other beneficial tax treatments relating to indirect taxes that are also made available to Labuan entities which will be highlighted in this article together with a comparison of the different tax treatments for Labuan entities and Malaysian entities.

Labuan Business Activity Tax Act 1990

Under the LBATA, a Labuan entity carrying on a Labuan trading activity is charged tax at a rate of 3% on the net audited profits reflected in the audited accounts of the Labuan entity for each year of assessment. However, a Labuan entity carrying on a Labuan trading activity has the option of electing to be charged tax at a fixed rate of RM20,000 (approximately USD6,000) for each year of assessment. Once this option has been exercised, a Labuan entity would not be subject to the 3% tax charge.

In the case of a Labuan entity carrying on a Labuan non-trading activity (which would basically include all investment activities), there is no charge to tax.

Income Tax Act 1967 ("ITA")

Other Malaysian non-Labuan entities deriving income from Malaysia are subject to tax under the ITA where the usual rate of tax applicable to companies is currently 25%. However, it has been proposed that the rate be reduced to 24% from the year of assessment 2016.

For Labuan entities that prefer to enjoy benefits under a Malaysian double tax treaty rather than the tax benefits under the LBATA, they may opt to make an irrevocable election for their profits to be taxed under the ITA instead of the LBATA. With such an election, all of the Labuan entity's profits, whether arising from a Labuan trading activity or a Labuan non-trading activity, would be subject to tax at the usual rate of 25% under the ITA.

Exemption orders under the ITA

Ordinarily, payments of interest, royalties, technical fees and other gains or profits not coming within the specified classes of income, which are derived from Malaysia and paid to non-residents, would be subject to withholding tax in Malaysia.

However, Labuan entities are exempted from withholding tax on those specified payments made to non-residents.

Under the Income Tax (Exemption) (No 22) Order 2007 ("2007 Exemption Order"), due to the terminology used which refers to "offshore company" instead of "Labuan entity", Labuan companies and Labuan trusts are among the types of entities specified as being exempted from withholding tax on interest, royalties and technical fees paid to non-residents. This exemption, however, does not apply to Labuan foundations.

As such, a new exemption order known as the Income Tax (Exemption) (No 4) Order 2012, which was gazetted in 2012, used the term "Labuan entity" in relation to exemption from withholding tax on other gains or profits not coming within the specified classes of income so that where those payments are concerned, the exemption from withholding tax is made available to all Labuan entities as defined, including Labuan foundations, Labuan companies and Labuan trusts. The anomaly affecting the 2007 Exemption Order is known to the Labuan authorities and should hopefully be resolved soon.

Double tax treaties

Some countries that have entered into double tax treaties with Malaysia have specifically excluded Labuan entities from enjoying the benefits provided under their double tax treaties.

One of the latest examples is the double tax treaty between Malaysia and India known as the Double Taxation Relief (The Government of the Republic of India) Order 2012 ("India Order"). The Protocol to the India Order specifies that persons who are entitled to tax benefits under the LBATA are not entitled to benefits under the India Order but an exception is made for Labuan companies which have made an irrevocable election to be charged tax in accordance with the ITA.

In contrast, other countries which have excluded Labuan entities from enjoying the benefits under their double tax treaties do not make any exceptions for

Labuan entities which elect to be taxed under the ITA instead of the LBATA.

One such example is the double tax treaty between Malaysia and South Africa known as the Double Taxation Relief (The Government of the Republic of South Africa) Order 2005 ("South Africa Order"), which specifies that the benefits of the South Africa Order shall not be made available in relation to the carrying on of any offshore business activities (as defined in the LBATA as at 26 July 2005).

As no exception was provided in the South Africa Order, Labuan entities wishing to enjoy benefits under the South Africa Order or other similar double tax treaties without provisions for an exception should be aware that electing to be taxed under the ITA instead of the LBATA may not necessarily enable them to enjoy treaty benefits.

Inheritance tax and gift tax

There is no inheritance tax or estate duty in Malaysia, including Labuan, so any estate planning does not have to take into account such taxes.

There is also no gift tax per se in Malaysia, including Labuan, but if the gift involves real property or shares in a real property company, the *Real Property Gains Tax Act 1976* may need to be considered.

Stamp duty

Stamp duty is imposed on certain types of instruments in Malaysia as specified in the *Stamp Act 1949*. Common instruments which are subject to stamp duty would be conveyances or transfers on sale of property such as shares and real estate. For such instruments, the rate of stamp duty is imposed on the value of the property in question so the total stamp duty payable could be quite substantial depending on the value of the property.

For Labuan entities, an exemption order known as the Stamp Duty (Exemption) (No 3) Order 2012 ("Stamp Order") is in force which exempts all instruments executed by a Labuan entity in connection with a Labuan business activity from stamp duty.

In addition, under the Stamp Order, all instruments of transfer of shares in a Labuan entity, as well as the constituent documents for the establishment of a Labuan entity are exempted from stamp duty.

Customs duties

Customs duties, the most common of which are import duty and export duty, are imposed on certain goods imported into or exported from Malaysia.
However, once again there is special treatment in relation to Labuan; as stated in the *Customs Act 1967*, the "principal customs area" in Malaysia is defined to exclude Labuan so that no export duty is payable on any goods exported from Labuan and generally no import duty is payable on goods imported into Labuan.

Goods and Services Tax (GST)

GST is a new tax that came into force in Malaysia on 1 April 2015 and is levied on the supply of goods or services made in Malaysia, as prescribed, including the importation of goods into Malaysia.

However, GST shall not apply to any importation of goods or supply of imported services into Labuan unless specifically prescribed by the Minister of Finance by an order laid before Parliament. Where goods are supplied from Labuan to Malaysia or taxable services are made by a taxable person in Labuan to Malaysia, GST would be chargeable.

Conclusion

There is a comprehensive range of tax benefits both in relation to direct taxes and indirect taxes available to Labuan entities which do not apply to other Malaysian entities. Such benefits contribute to make Labuan IBFC a very attractive jurisdiction for a variety of business and financial activities[1].

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[1] An earlier version of this article was first published in CTIM's *Tax Guardian*, Q4 issue (www.ctim.org.my) October 2014".

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