



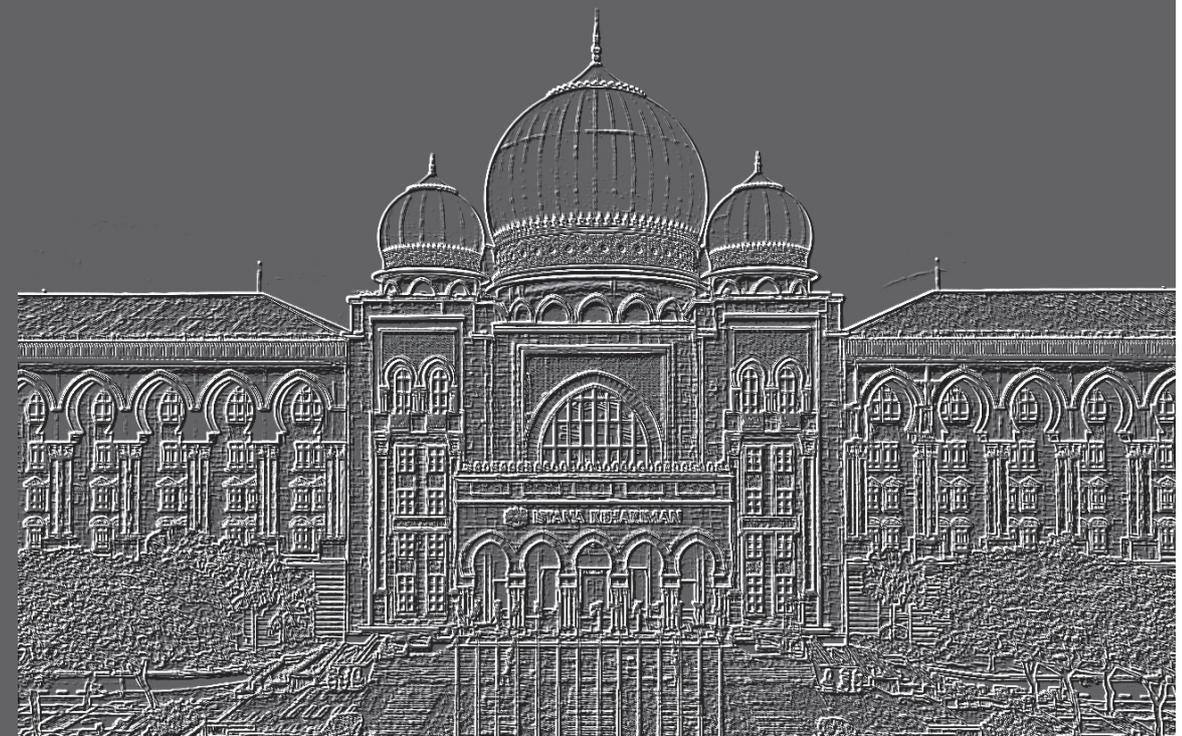
# JOURNAL OF THE MALAYSIAN JUDICIARY

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## PREFACE

We are on the cusp of an exciting time ahead, because for the first time, the JMJ invites writers from outside the small niche of judges from our Judiciary.

The depth and weight this has added to our publication is invaluable. In this, one is reminded of the remark made by Lord Cooke of Thorndon (New Zealand Court of Appeal and Lord of Appeal in the House of Lords), that we can now “enjoy the luxurious advantage of the freedom to ransack the case laws of the larger English speaking jurisdictions”, and in this we can afford to be eclectic.

We have yet another first; in that the Chief Justice, in recognising the allure of having referees to advise, influence, reform and refine the shape of our nascent publication, has invited eminent personalities to be members of the JMJ’s Panel of Referees. Their input promises to give it profundity and élan.

The thrill derived from the range of all these diverse talents is, one hopes, the appeal of our publication.

Justice Zainun Ali  
Managing Editor



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**Royal Address by His Majesty Sultan Ibrahim Ibni  
Almarhum Sultan Iskandar, the Sultan of Johor,  
at the Opening Ceremony of the Muar Court Complex  
on Thursday, January 18, 2018**

Ladies and Gentlemen,

The Federal Constitution is the supreme law of Malaysia. It is an all encompassing living instrument which has taken into account the interests of all parties as well as the historical background of this country.

Our Constitution is based upon the Westminster system of democracy with a constitutional monarchy. The Federal Constitution came into effect in 1957 and continues to be the source of governance in Malaysia.

Nevertheless, there have been amendments and improvements made to the Federal Constitution since its inception, to cater to the prevailing needs and requirements of the country at various points in time. If those amendments prove to be detrimental today, I must then suggest that the matter be rectified for the sake of the country's stability and the people's well-being.

The State of Johor was the first government in Malaysia to have a written Constitution and to practise the system of constitutional monarchy. It began when the late Sultan Abu Bakar declared the *Undang-Undang Tubuh Kerajaan Johor* on September 14, 1895. Up till today, the *Undang-Undang Tubuh Kerajaan Johor*, which provides for the manner of governance and rules on how the government should be administered, is still used without much amendment.

Ladies and Gentlemen,

To maintain the country's stability, our system of separation of powers must be protected. The three main components of Government, namely the Executive, the Legislature and the Judiciary, must be independent and each must have the right to decide on matters falling within its own jurisdiction. No component holds absolute power. If the power to administer, to enact laws and to adjudicate disputes is bestowed

on a single individual or component, it will encourage autocratic governance. There will then be no check and balance.

The jurisdiction of Parliament is only to enact laws. A law which is to be enforced must be passed by three entities, namely the *Dewan Rakyat* (House of Representatives), the *Dewan Negara* (Senate) and the *Yang di-Pertuan Agong*. These three entities must be given freedom to exercise their functions in decision-making so as to ensure a complete process in the enacting of laws.

The Executive, on the other hand, must administer in accordance with enacted laws. Whenever there is dispute in relation to administration, it must be adjudicated by the Judiciary. Thus, the administration of the Government will be carried out properly and there will be no abuse of powers.

Ladies and Gentlemen,

The Judiciary was carefully established, independent from the Executive and the Legislature, under the Federal Constitution. The power to appoint a Judge of the High Court vests in an independent institution, namely the Conference of Rulers and the King (the *Yang di-Pertuan Agong*).

I am also subject to the law and cannot interfere in the judicial process. Nevertheless, my responsibility lies in ensuring that the life of the people of my State is safe, peaceful and prosperous.

The judges and the judicial officers in the Judiciary are free from any interference by other parties. In this matter, I believe that all judges have the courage to uphold justice and are able to make fair and just decisions and be accountable for them.

I also believe that judges will perform their duty to the best of their ability and that they are not influenced by personal or political interests. All decisions made by them must be based upon the country's Constitution and laws as well as on clear facts and evidence, and should be made without fear or favour.

Therefore, I reiterate and call upon people at all levels to collectively respect and protect the principles of the independence of the Judiciary. One must not make rash and baseless allegations against a judge or a judicial officer.

In my view it is not easy to shoulder the responsibilities of a judge. They have to exercise restraint at all times and make many sacrifices. They need to be constantly circumspect in their dealings with their fellow men so as to remain objective and independent in carrying out their judicial functions.

Thus, the life of a judge is always lonely as he/she is not allowed to socialise freely. Not all invitations to functions can be accepted by judges. The places they visit or frequent should not be a place which would tarnish their image and professional reputation.

Judges are also encouraged to speak less but to listen more especially during proceedings in the courtroom. They need to focus on the cases which are on trial and make the best decisions in accordance with the facts presented in court and the law, and not based upon mere presumptions. In making their decisions, judges must adhere to the provisions of the laws which are enacted by the Legislature, and be free from any prejudice or conjecture.

Nevertheless, integrity and fairness are the most important attributes of a judge who must always be faithful to truth and justice. Every judge must be responsible in protecting the image of the Judiciary and together with other judges, strive to elevate its level of integrity.

Ladies and Gentlemen,

I have often stressed upon the importance of an amicable and proper relationship between the Federal Government and the State Government in order to form a developed and prosperous Malaysia.

I would like to take this opportunity to thank the Federal Government for building this new Muar Court Complex to replace the old Muar Court at Jalan Petrie. With this new court complex which is both spacious and comfortable, I believe the quality of the delivery of judicial services to the public will be improved, especially to those in Muar.

I would also call upon the Federal Government to speed up the construction of the new Johor Bahru Court Complex, as the current old court building can no longer accommodate the public's needs. As it is, due to lack of space, the courtrooms have to be located at several different locations. The State Government of Johor has made available a suitable area in Kota Iskandar, and in due course I will make the old Johor Bahru Court building a Heritage Museum for the State of Johor.

I would like to take this opportunity to record my sincere appreciation to all members of the Judiciary who have at all times shouldered the trust given to them with integrity in upholding justice for the people and the country.

Lastly, I would like to congratulate and thank all parties involved in organising today's opening ceremony.

# Shaping the Future of Arbitration in Malaysia\*

by

*The Rt. Hon. The Chief Justice Tun Raus Sharif<sup>\*\*</sup>*

[1] It is both an honour and a pleasure for me to address all of you at this inaugural National Arbitration Conference with the theme “*Shaping the Future of Arbitration in Malaysia*”.

[2] Let me begin by extending my heartiest congratulations to the Malaysian Institute of Arbitrators for putting together an excellent programme with a great cast of speakers for this conference.

[3] The timing of this Conference is especially welcomed in the current climate. This era is indisputably the golden age of arbitration.

[4] Once confined to construction disputes, arbitration in Malaysia has transformed to avail itself to a multitude of commercial disputes, both domestically and internationally.

[5] For those entering into cross-border transactions, arbitration is now the preferred mode of dispute resolution and Malaysia is rightly recognised as an attractive and sophisticated arbitration venue for user-friendly arbitration. A constant search for development and progress has seen Malaysia emerge as a promising destination in terms of alternative dispute resolution (“ADR”) for parties and arbitrators alike.

[6] Having served as a judge for the past 24 years, I can safely say that Malaysia has made great strides to cultivate a friendly and vibrant environment for arbitration.

[7] But arbitration in Malaysia did not have a spurt of growth overnight; it was the fruit of labour by many parties/institutions. A number of factors have contributed to this positive development.

[8] In this respect, I would like to take stock of how we got to this position. Perhaps, what I can do today is to share with you some of

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\* Keynote address at the National Arbitration Conference on February 8, 2018 at the KLRCA.

\*\* Chief Justice of Malaysia.

the factors which have led to Malaysia being the arbitration hub it is today and highlight the progress we have made in the Malaysian arbitration regime, as we chart our way forward.

[9] I attempt to cover three points. Top on the list is the comprehensive statutory framework which is in line with modern principles of international arbitration practice. Secondly, the active role played by the judiciary through its endeavours in facilitating arbitration; and thirdly, the role of our stakeholders in charting the course of arbitration in Malaysia.

### **Comprehensive statutory framework**

[10] When I speak of the comprehensive statutory framework within the arbitration regime, credit must be given to our Legislature for ensuring that strong statutory underpinning is in place for the development of both domestic and international arbitration. The Malaysian Legislature has also been perceptive to the demands of the arbitration market.

[11] Fortunately, our legislators have continuously been sensitive to the preferences of arbitration users. To its credit, the Malaysian Legislature has focused its attention on these users – whether individuals or large corporations – in understanding their essential need for speedy, cost-effective and efficient resolution to disputes that arise in the course of their business engagements.

[12] Thus, with the paramount purpose of ensuring that arbitration is made more attractive to these users, the Malaysian Parliament repealed the Arbitration Act 1952 and the Convention on the Recognition and Enforcement of Foreign Arbitral Awards Act 1985.

[13] In their place is the Arbitration Act 2005 (“AA 2005”), which came into force on March 15, 2006.

[14] The AA 2005 introduced nothing short of a revolutionary legislative framework which catapulted Malaysia’s reputation as a cutting edge, pro-arbitration jurisdiction.

[15] Modelled on the UNCITRAL Model Law on International Commercial Arbitration 1985 (with amendments as adopted in 2006) (“Model Law”) and the New Zealand Arbitration Act 1996, the AA 2005 internalised generally recognised principles of international arbitration law.

[16] Though the AA 2005 was confronted with teething problems and lacunae at the beginning, these minor drawbacks were expeditiously addressed by the Arbitration (Amendment) Act 2011.

[17] To add to the Legislature's accolades, amendments to the Legal Profession Act 1976, made by way of the Legal Profession (Amendment) Act 2013, now allow for foreign arbitrators and lawyers to participate in arbitral proceedings as both counsel and arbitrator. This is another great effort taken by Malaysia to promote a vibrant and globalised arbitration practice in Malaysia.

[18] With this amendment, our pool of arbitrators and counsel has been diversified. Now, our flourishing arbitration economy reaps the benefits of this robust statutory framework.

[19] In addition, to facilitate the mediation process, the Malaysian Parliament enacted the Mediation Act 2012 ("MA 2012") which came into force on August 1, 2012 with the main objectives to encourage and promote mediation, and to facilitate dispute settlement in an impartial as well as time and cost-effective way. The advantages of Court-Annexed Mediation are many, *inter alia*, quicker resolution of disputes, less expensive in terms of costs as compared to litigation and less formal setting as compared to court room litigation.

[20] Apart from the MA 2012, we have the Kuala Lumpur Regional Centre for Arbitration ("KLRCA") Mediation Rules (Revised 2013) which is a set of procedural rules covering all aspects of the mediation process to help parties resolve their domestic or international disputes.

### **Role of the judiciary in facilitating arbitration**

[21] On our part, the courts have always played a significant role in facilitating arbitration. The courts in Malaysia are now committed to the widely accepted core principles of arbitration as enshrined in the UNCITRAL Model Law on International Commercial Arbitration. The AA 2005 gives statutory force to the tenets embedded in the Model Law, and in cases like *The Government of India v Cairn Energy India Pty Ltd & Ors*,<sup>1</sup> the courts have recognised the importance of the application of the Model Law, thus contributing to a healthy and properly functioning arbitration regime.

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1 [2014] 1 AMCR 760; [2014] 9 MLJ 149.

[22] The dual pillars of arbitration, namely, party autonomy and minimal judicial intervention in arbitration, are reaffirmed and enhanced through the AA 2005. These fundamental pillars of arbitration are time and again protected and reinforced by decisions of the courts in Malaysia. The reason why users trust Malaysia as a seat of arbitration is not solely because of the fine quality of arbitration that Malaysia proffers, but I believe also because of the faithful non-interventionist approach of the Malaysian judiciary.

[23] Having fully understood the depth of its responsibility and the extent of its impact, the judiciary has consciously made efforts to ensure that arbitration-related cases are speedily disposed of, and on an average, cases on arbitration awards in the High Courts are generally heard within three months and disposed of within nine months from the date of registration.

[24] Previously, excessive court intervention in arbitral proceedings had greatly affected the efficacy of arbitration itself. Many a time parties came to court invoking the inherent jurisdiction of the court to stall arbitration, review the awards, etc. Such intervention was viewed by many as a hindrance to the arbitral process. Not to mention the excessive costs and uncertainty, thus converting arbitration into court room litigation. With it came the agony of the appeal process and delays therefrom.

[25] To illustrate this point further, it is a well-known fact that before the reform to clear the backlog of cases was initiated by our former Chief Justice Tun Zaki in late 2008, it took the High Court an average of three to five years to dispose of a case. The Court of Appeal disposal would require another two to three years. Likewise, another two to three years in the Federal Court for the appeal to be finally disposed of. Thus, in those days, when an arbitral award was challenged up to the Federal Court, it could take at least seven years before it could be finally concluded.

[26] Now of course, it is very much faster, i.e. nine months for the disposal of cases at the High Court, nine months at the Court of Appeal and six months at the Federal Court. Although it is still a long process, it is definitely better than before. Against this background, there were recommendations by the corporate sector for further amendments to be made to the AA 2005 to ensure certainty, clarity and finality of the arbitral process and enforcement of awards with minimal intervention from the courts.

[27] This was addressed by the Arbitration (Amendment) Act 2011. The Explanatory Note to the Amendment Bill explains:

... the purpose of this amendment is to limit court intervention to situations specifically covered by the Principal Act and to discourage the use of inherent powers by the court.

[28] The newly amended section 8 limits the instances where the court can intervene in arbitration proceedings. Section 8 of the AA 2005 provides that “no court shall intervene in matters governed by this Act, *except where so provided in this Act*” which is read to mean “*minimal intervention consistent with the policy underlying the UNCITRAL Model Law*”.<sup>2</sup>

[29] It is absolutely necessary that in balancing party autonomy and flexibility on the one hand, and strict adherence to the statutory framework of the arbitral process on the other, the coercive powers of the judiciary ought only to be invoked as a last resort, and should otherwise remain dormant. The underlying principle is this:

Courts should be slow in interfering with an arbitral award, unless it is a case of patent injustice in which event the law permits interference in clear terms.

[30] I am pleased to report that the Malaysian judiciary has consciously respected the spirit of the AA 2005, and has interpreted and applied the law with the best interest of the future of arbitration in view.

[31] The judiciary has also been vigilant in ensuring that recognised grounds for setting aside or declining to enforce an award are not easily exploited or expanded. Where judicial intervention is warranted, the judiciary has stepped to the forefront and taken over the reins, so as not to compromise the administration of justice.

[32] Take the recent Federal Court case of *Thai-Lao Lignite Co Ltd & Anor v Government of The Lao People’s Democratic Republic*.<sup>3</sup> In this case, for the first time in Malaysian history, an international arbitral award was set aside. In deciding so, the Federal Court held, at paragraph 239, that:

“Support for arbitration” is not “no disturbance”. There are always two sides to the same coin. The loser will call for “disturbance”.

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2 See *Far East Holdings Bhd & Anor v Majlis Ugama Islam dan Adat Resam Melayu Pahang (and 2 Other Appeals)* [2017] 8 AMR 313; [2018] 1 CLJ 693, FC.

3 [2017] 6 AMR 219; [2017] MLJU 1196.

If an arbitral award is a sacred cow and cannot be disturbed, that will not engender confidence in arbitration. “No disturbance” may appear, at least superficially, to support arbitrators. But in truth, “no disturbance” is anathema to arbitration. “Do not disturb” will kill confidence in arbitration. Once confidence is lost, both arbitration and arbitrators will be the [worse] for it. For arbitration to continue to be relevant, it must be accepted that arbitral awards are not sacrosanct. Arbitral awards will be reviewed by the supervisory court of the seat. Arbitration will be dead, in Malaysia and elsewhere, if a supervisory court will only ... rubber stamp arbitral awards.

[33] Inasmuch as the courts must embrace the principles of finality of awards, party autonomy and minimal court intervention in the context of the UNCITRAL Model Law legal regime, the courts cannot allow an award to stand in the face of a clear excess of jurisdiction and a breach of the equally important principle that arbitration proceedings are consensual.

[34] In *The Government of India v Cairn Energy India Pte Ltd*<sup>4</sup> the Court of Appeal elaborated on the need to maintain a restrictive approach when exploring the ground of public policy. The Court of Appeal held:

... First, that the public policy ground for setting aside or non-recognition of an award must be given a narrow and more restrictive construction and interpretation. This harks back to the fundamentals; that at the heart of the matter is an award which resolves the dispute between the parties, which dispute the contracting parties had contractually agreed shall be resolved by arbitration. I would add that the court should be slow to find such a ground; or to expand the hitherto accepted and recognised categories ...

[35] In terms of the enforcement of arbitration awards, the Convention on the Recognition and Enforcement of Foreign Arbitral Awards Act 1985 (the New York Convention Act) has been repealed by the AA 2005, and replaced with enforcement provisions which provide a uniform process for the recognition and enforcement of both domestic and foreign arbitral awards.

[36] The Malaysian judiciary, having regard to the clear statutory power and jurisdiction of arbitrators to rule on their own jurisdiction, has been steadfast in enforcing arbitration agreements. Courts, in

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4 [2014] 1 AMCR 760; [2014] 9 MLJ 149.

assessing plausible enforcements of arbitration agreements, are ready to “lean towards arbitration”. There is no doubt that the arbitration fraternity enjoys strong judicial backing with regard to the enforcement of arbitral agreements. The court in Malaysia is purely an enforcement court and must recognise a valid arbitration award save for the exceptions provided under the law.

[37] The courts have also extended support by displaying flexibility and being liberal in the construction of arbitration agreements.

[38] For instance, the Federal Court in *Ajwa for Food Industries Co (MIGOP), Egypt v Pacific Inter-Link Sdn Bhd*<sup>5</sup> held, at paragraphs 25 and 26, that:

[25] We are of the view that an arbitration agreement need not be signed ... such a written agreement to arbitrate does not necessarily mean a formal agreement executed by both parties. It would be sufficient so long as the arbitration agreement is incorporated into a written document.

...

[26] ... We are of the view that the mere fact the arbitration clause is not referred to in the contract and that there is a mere reference to standard conditions which was neither accepted nor signed, is not sufficient to exclude the existence of the valid arbitration clause. There is no requirement that the arbitration agreement contained in the document must be explicitly referred to in the reference. The reference need only be to the document and no explicit reference to the arbitration clause contained therein is required.

[39] Another noteworthy amendment to the AA 2005 is the newly amended section 10(1)(a). The newly amended section 10 has limited instances where the court may stay proceedings to just one ground. The only ground is when the High Court is satisfied that the arbitration agreement is null and void, inoperative or incapable of being performed. The new amendment also restricts the powers of the High Court in hearing the questions of law arising out of an award. The old section 42(1) of the AA 2005 allowed any party to arbitral proceedings to refer any question of law arising out of an award to the High Court. Under the new amendment, the High Court is empowered by a new

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5 [2013] 4 AMR 789; [2013] 5 MLJ 625.

subsection 42(1A) of the Act to dismiss any such reference unless the question of law substantially affects the rights of the parties.

[40] Emphasising the perimeters of this statutory framework, the Federal Court in *Press Metal Sarawak Sdn Bhd v Etiqa Takaful Bhd*<sup>6</sup> held that if a valid and binding arbitration agreement exists between the parties, and the dispute falls within the arbitration agreement, the court must grant an order to stay the court proceedings pending reference to arbitration.

[41] The Malaysian judiciary has also played an important role in facilitating arbitration through its structural and policy initiatives. One of the initiatives I would like to highlight is the Court-Annexed Mediation we started in 2010 to encourage the early settlement of disputes between parties without trial. The court-annexed mediation programme is where the judges are the mediators in assisting the disputing parties to find solutions to their predicament. We have our very own Mediation Centres operating in major centres throughout Malaysia.

[42] From what I have discussed thus far, clearly, arbitration in Malaysia enjoys a symbiotic relationship with the courts. In this regard the role of the judiciary cannot be discounted. Resultantly, the positive effect of this is the blooming confidence that users have in arbitration.

### **Role played by our stakeholders**

[43] Speaking of arbitration in Malaysia, one cannot dismiss the role played by the KLRCA. The KLRCA was just recently rebranded the Asian International Arbitration Centre (“AIAC”) on February 7, 2017 after receiving approval from key stakeholders and the relevant authorities.

[44] The KLRCA was established in 1978 under the auspices of the Asian-African Legal Consultative Organisation (“AALCO”). The KLRCA was in fact the first regional center established by AALCO in Asia to provide institutional support as a neutral and independent venue for the conduct of domestic and international arbitration proceedings in the region. The Government of Malaysia has accorded the KLRCA independence and certain privileges and immunities for

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6 [2016] 5 AMR 635; [2016] 2 AMCR 473; [2016] 5 MLJ 417.

the purpose of executing its functions as an international institution. Under the stewardship of its Director, Datuk Professor Dr Sundra Rajoo, the KLRCA has made headway in making Malaysia one of the preferred hubs for arbitration in South East Asia.

[45] The KLRCA has come a long way since its inception and this is evident from the KLRCA's Annual Report 2016 which states:

From 1978 to 2010, the Kuala Lumpur Regional Centre for Arbitration (KLRCA) recorded 22 cases. By 2016, it recorded a staggering 618 cases, a 96.4% growth since 2010.

The number of cases for arbitration translates to claims totaling to USD295,470,992.84 (for international cases) and MYR468,209,113.39 (for domestic cases). Further claims amounting to MYR1,537,979,679.80 were adjudicated. This is an all-time high for the Centre since its resurgence in 2010.

[46] With the revitalisation of the KLRCA under Datuk Professor Sundra Rajoo, user confidence has improved immensely in the use of arbitration as a method of resolving commercial disputes in Malaysia. More parties are now willing to have their contractual disputes arbitrated at the KLRCA in accordance with the KLRCA Arbitration Rules. To date, there are more than 1,000 international and local arbitrators who are empanelled on the KLRCA's Panel of Arbitrators – many of whom are Fellows or Members of the Chartered Institute of Arbitrators. The KLRCA has enacted its own set of rules to regulate arbitration proceedings under its purview. The KLRCA Arbitration Rules 2010 are a set of rules covering all aspects of the arbitration process in settling disputes.

[47] The KLRCA Arbitration Rules allow flexibility in proceedings; it gives discretion to parties pertaining to the choice of arbitrator, place of arbitration and procedure for conducting the arbitration proceedings. The KLRCA Arbitration Rules 2010 conform to the International UNCITRAL Arbitration Rules 2010. In 2013, the KLRCA also introduced the KLRCA Fast Track Arbitration Rules which was designed for parties who wish to obtain an award in the fastest way with minimal costs. The Rules provide that arbitration must be completed within a maximum period of 160 days. The streamlined new rules seek to preserve the working relationship of the parties and ensure those who negotiate their own settlements have more control over the outcome of their dispute.

[48] Equally impactful is the transition of the KLRCA to its new home, the Bangunan Sulaiman in 2014. The KLRCA's new home houses excellent state-of-the-art facilities and infrastructure, making arbitration in Malaysia all the more attractive to international users.

[49] Another body which has played a pivotal role in facilitating arbitration in Malaysia is The Chartered Institute of Arbitrators ("CIArb") (Malaysia Branch) which is a non-profit organisation working in the public interest to promote ADR as a mode to resolve commercial disputes efficiently. Presently, it has a local membership of 432.

[50] CIArb (Malaysia Branch) was established in 1993, and exists for the global promotion, facilitation and development of all forms of ADR. In addition to providing education and training for ADR practitioners, the CIArb (Malaysia Branch) acts as a centre dedicated to providing world-class quality and efficient service to ADR practitioners, policy makers, academics and others in the dispute resolution industry.

[51] The CIArb (Malaysia Branch) has for many years been working closely together with the KLRCA in the provision of high level conferences, lectures and training for arbitrators, ADR practitioners and people who aspire to be arbitrators or wish to establish their career in the practice of ADR. The CIArb (Malaysia Branch) is well known for its sterling ADR training lectures and conferences in Malaysia.

## **Conclusion**

[52] In concluding, I would like to reiterate that to maintain the arbitration industry's positive growth, we must continue to work hard on being an arbitration centre par excellence – not just in terms of the number of cases, but also by upholding the very highest standards in ethics, advocacy, quality of arbitrators and jurisprudence. This must be the hallmark of our arbitration regime, and clients experiencing arbitrations here must go away feeling that their dispute was handled fairly and professionally, irrespective of the outcome.

[53] I end my address this morning by once again thanking the organisers of this conference for having me here today. I wish this conference every success and I hope that all of you will find this conference fruitful and stimulating, and appreciate the varied perspectives and exciting discourse on offer.

Thank you.

## To Intervene or Not to Intervene

*by*

*Justice Dato' Mary Lim Thiam Suan\**

[1] The principle of minimalist intervention by the court in matters relating to arbitration is recited almost like a mantra by legal counsel in any given arbitration related proceedings in court. The court is frequently reminded to restrain its exercise of discretion when dealing with arbitration, with suggestions of dire consequences to State and industry if the courts are perceived as not supportive of arbitration. It is most unfortunate that the true meaning and purpose for that principle in the first place is generally misunderstood; and that the decision to intervene or not to intervene in arbitration and arbitration related matters is truly yet another exercise of judicial discretion.

[2] Arbitration started off as a real and viable alternative to litigation in court. The latter was perceived to be far too slow, unresponsive to the practicalities and needs of the financial and commercial world, formalistic and too rules-based, constrained by the law of evidence. The appeals process within the litigation regime, accepted as a necessary component of the rule of law, does not enjoy the same reception in arbitration. Time spent in court scrutinising the ambit of a decision to arbitrate, the issues that may or may not fall within the jurisdiction of the arbitral tribunal, and the award rendered by the arbitral tribunal, are often perceived as intrusions that undermine the very right of the parties to contract in the terms that they may mutually agree upon. Those terms extend to and include their choice of forum for resolving with finality and certainty, any disputes that may arise between them.

[3] The real attraction of arbitration is not so much in any costs saving or the cloak of confidentiality; it lies in the measure of control that the disputants have in many respects, particularly in the choice of the arbitral tribunal. Consequently, litigation over and on arbitration is said to unnecessarily prolong the process of resolution of disputes which is after all, already resolved by arbitrators selected by either

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\* Judge of the Court of Appeal of Malaysia. The views and opinions expressed in this article are those of the writer.

the disputants themselves or a respected and reliable regional or international arbitral institution, often on the strength of their expertise and neutrality.

[4] Article 4 of the UNCITRAL Model Law on International Commercial Arbitration (“UNCITRAL Model Law”) upon which section 8 of the Arbitration Act of 2005 (Act 646) (“AA 2005”) is modeled states:

In matters governed by this Law, no court shall intervene except where so provided by this Law.

The UNCITRAL Model Law was adopted by the United Nations Commission on International Trade Law (“UNCITRAL”) on June 21, 1985 at the close of the Commission’s 18th annual session. The General Assembly, in its resolution 40/72 of December 11, 1985, recommended “that all States be given due consideration to the Model Law on International Commercial Arbitration, in view of the desirability of uniformity of the law of arbitral procedures and the specific needs of international commercial arbitration practice.” This Model Law is a draft law which any country is free to introduce into their own domestic law, whether with or without amendments and modifications. This is unlike the Convention in the Recognition and Enforcement of Foreign Arbitral Awards 1985, more popularly referred to as the “New York Convention” where member States are obliged to adhere to the terms of the Convention when introducing the Convention into their domestic regimes.

[5] Using the Model Law framework for any arbitration law is intended to aid uniformity and harmony in international commercial arbitration. Parties and the courts may refer and rely on a whole treasury of deliberations and writings from other jurisdictions which have similarly adopted Model Law as well as use the *Travaux Préparatoires* of UNCITRAL Model Law, and various other reports and commentaries prepared by UNCITRAL [such as the Analytical Commentary on Draft Text of a Model Law on International Commercial Arbitration (Report of the Secretary General, UN Commission on International Trade Law), the Report of the Working Group on International Contracts Practices, and the UNCITRAL 2012 Digest of Case Law on the Model Law]. In the Explanatory Note to the Model Law prepared by the UNCITRAL Secretariat, it is stated that “The need for improvement and harmonisation is based on findings that domestic laws are often

inappropriate for international cases and that considerable disparity exists between them”.

[6] The understanding behind Article 4 and thereby section 8 of the AA 2005 required an appreciation of how Model Law interfaces in any deliberation. In aid of uniformity and harmonisation of the interpretation and application of the various provisions and principles found under the Model Law which thereby enhance international and multi-border investments, Article 4 mandates that courts intervene only in the areas which are provided under the Model Law. Although the Model Law is only a draft from which countries may frame their international arbitration laws, it would wreak havoc to practice and commerce if this provision is absent from the Model Law. Again, consistent with this object, intervention by the courts under a residual or inherent jurisdiction is also necessarily excluded.

[7] This principle of intervention according to Model Law however has since come to be acknowledged as “minimum or minimalistic intervention”. Unfortunately, there is a misconception that this means that the courts must adopt a “non-interventionist approach”, that the courts are not supposed to intervene in arbitration and arbitration related matters. From the terms of Article 4 and our section 8, it is apparent that there is a positive and supportive role to be played by the courts.

[8] It is, therefore, timely to re-evaluate this question of intervention by the courts in arbitration and arbitration related matters; what considerations ought to weigh in that exercise; and whether the pendulum of non-intervention has swung too far.

### **The options**

[9] As a forum for resolution of disputes, litigation is but one of two adjudicative options; the other is arbitration. Pitted against these two adjudicative options are options ranging from facilitative, advisory to determinative. The facilitative options include negotiation and mediation while conciliation is advisory in nature, and finally the determinative options include early neutral evaluation, mini trial and expert determination and resolution vide an ombudsman. All these options are available in any of the industries, businesses, commerce or mercantile that we see listed on the Stock Exchange. Thrown in now is what is still generally regarded as the “new kid on the block” in Malaysia, adjudication.

[10] Authors on ADR say that ADR evolved as an innovation to inflexible traditional procedures and institutions. Court processes and rules of procedure and evidence – the whole adversarial system – were often seen as slow, complicated, bewildering and intimidating, resulting in the court system being seen as inaccessible. The philosophy behind ADR is empowerment of the individual, encouraging the parties to take charge or resume charge of their problems, and to some extent, their destinies. In this way, better outcomes were believed to be possible through the informal exchanges, and business or personal relationships could then be preserved. Studies also showed that indeed, a very small percentage of cases actually go to trial (below 10%).

[11] In the opening chapter of *Arbitration in Malaysia – A Practical Guide*, published in 2016 by Sweet & Maxwell and written by the Director of the Kuala Lumpur Regional Centre for Arbitration, is the topic of “History of ADR in Malaysia”. Datuk Sundra Rajoo traces the evolution of ADR, recognising that it travelled to our shores with our forefathers from China and India, finding companionship in the local *penghulu* systems and yet more comfort from the *syariah* system which also encourages similar resolution or settlement mechanisms. Actually, there are a lot of commonalities in the *adat perpatih* system of Negeri Sembilan where parties have to *bermuafakat*, which in essence refers to agreement; and it is very much agreement within the *luak* or *perut*, that is clan, as the case may be. Everything is kept within the community with decisions of elders reigning supreme over any dispute resolution.

[12] Regardless of the resolution process, it is apparent that there is a common denominator, which is the involvement of neutral third parties who may or may not be known to the parties but who essentially are acceptable and respected by them. Regardless the dispute, be it clan, ethnic, custom, tribal or *kongsi* centric to trade associations or unions, commerce, business or industry based set ups, be it local, regional or international, or any combination of all that, the third parties are often from the community elders or the wealthy, influential leaders who are entrusted with power and authority to maintain social harmony and manage disputes. Enforceability was a given as the fear of ostracism, banishment or worse, often had the most sublime effect of dutiful compliance.

[13] The availability and thereby the choice of forum and procedure is generally driven by priorities. When considering and drafting the

best options for a dispute resolution clause, and this is particularly true of substantial contracts large in terms of economies of scale and financial costs and benefits, parties often favour an interest-based choice as opposed to one that is rights based. In the former, parties are looking at the real interests.

[14] These options are not necessarily structured or contracted as single options. It is not infrequent to see multi-tiered dispute resolution clauses in any given contract, sometimes to make the mechanism more potent or effective, a combination of any or all, say med-arb or ad-arb. In fact, the more complex, multi-partied and valuable the contract, the more likely it is to see such multi-tiered or composite ADR clauses with negotiations and conciliations being conducted many times over at various management levels, in-house and holding company levels, with time spans worked in for reflections, cooling off and other considerations. And, this is before throwing in the supranational development contracts, multi-party and multi-contract dimensions with its multi-border and multi-systems considerations. This is quite a cocktail and now, the choice for the adjudicative processes appears but a far distant glimmer, making the earlier remarks of litigation and now by association, arbitration, actually the alternative processes.

[15] Some of these alternative processes have been formalised through statute. Arbitration through firstly, the Sarawak Ordinance No. 5 of 1952 which had adopted the English Arbitration Act of 1950. That Ordinance was later adopted by the rest of Malaysia through the Revision of Laws Act 1968 (Act 1) and it became the Arbitration Act of 1952 (Act 93). In 2005, that 1952 Act was finally repealed and replaced by a completely new piece of legislation, the AA 2005 which came into force on March 15, 2006. The AA 2005 was amended in 2011 with some of the provisions better drafted to address concerns raised since its implementation. The AA 2005 substantially applies UNCITRAL Model Law with modifications, and amalgamates the law on domestic and international arbitrations under a single Act. This allows for the same application of Model Law but with a difference for domestic arbitrations, the difference being an added avenue of recourse to court through questions of law that are said to have arisen from the arbitral award. This extra power of intervention by the court under section 42 in Part III of the AA 2005 applies automatically in the case of domestic arbitrations unless parties to a domestic arbitration have opted out from its application. Parties to an international arbitration may opt

in to the application of Part III of the AA 2005 – see subsection 3(4) of the AA 2005.

[16] There are now plans afoot to further amend the AA 2005, with stakeholders frantically rushing to examine the proposals, engage in exchanges and submit appropriate and meaningful recommendations so that the future of ADR but more specifically, arbitration, may be better shaped to meet the needs of country, region and changing times.

[17] The other alternative modes or dispute resolution processes are mediation and adjudication. In 2012, the Mediation Act (Act 749) (“MA 2012”) was enacted with the aim of promoting and encouraging mediation as a method of alternative dispute resolution and facilitating the settlement of disputes in a fair, speedy and cost effective manner. In that same year, the Construction Industry Payment and Adjudication Act 2012 (Act 746) or CIPAA was also enacted although it did not come into force until 2014. CIPAA contains a provisional dispute resolution process hyped out specifically for construction and construction related matters, and more particularly, in respect of their interim or progress claims and arguably final claims. Both pieces of legislation provide that these alternative processes may be resorted to concurrently with litigation – see section 4 of the MA 2012 and section 37 of CIPAA.

[18] The position is somewhat different when dealing with arbitration. The arbitration clauses or the agreement to arbitrate is often jealously relied on to ensure that litigation is stayed and the parties are referred to arbitration as the agreed forum for dispute resolution – see section 10 of the AA 2005, and the courts have consistently given due recognition to such agreements.

[19] In a paper presented at the Denning Lectures organised by the Bar Association for Commerce Finance and Industry titled “*Law & Society 1975*”, Sir Henry Fisher put forward 12 propositions that both legislators and judges should always have in the forefront of their minds when going about their respective businesses. Although written more than 40 years ago, those propositions, in particular two of them, are apt for this paper.

[20] First, the occasions on which it becomes necessary to go to the courts for determination of legal questions should be reduced to a minimum. Second, judges should remember that their function is an ancillary one, namely to lay down the law in such a way that more

and more future disputes can be settled without recourse to the courts and to give clearer guidance to individuals and companies in the conduct of their affairs. These two propositions underscore this paper, whether the right of access to justice which is constitutionally enshrined under Article 8 of the Federal Constitution has only one recourse or seat, that is, the courts, or that indeed, there are more. And, whether in deference to the choice of forum for dispute resolution, the opportunity to develop or clarify the law is lost. In a display of healthy respect for ADR, the courts, through the pre-trial case management system, often remind and encourage parties to resolve their disputes as opposed to going to trial, or even appeal – see Order 34 rule 2(2) of the Rules of Court 2012 and Practice Direction No. 5 of 2010.

[21] But, that is not all. In their substantive decision-making, the courts have adhered to a call for minimum intervention when it comes to arbitration. Have the courts gone too far in harkening to that call, and should there be a change? It is in the context of that perspective that this paper seeks to draw some awareness to consider how at least two judiciaries have cautioned the extent of adherence to this principle.

[22] The arbitral community, and just about everyone remotely related to it, and its pitch, is that when it comes to arbitration, it is first and last, a principle of minimal intervention by the court, an absolute pillar of any successful arbitration regime anywhere in the world. This principle is twinned by the principle of respect for party's freedom of choice or party autonomy. The courts in Malaysia, without doubt, have repeatedly echoed that refrain for so long now that it is difficult to recall when we were any different. It is however, necessary that the courts examine that rationale in order that it may attend to its proper role when it comes to arbitration and ADR.

[23] In October 2013, the Right Hon. Chief Justice of Singapore spoke on "Judicial Attitudes towards Arbitration and Mediation in Singapore" at the Arbitration Conference co-hosted by the ASEAN Law Association and the Kuala Lumpur Regional Centre for Arbitration. His Lordship felt that because these two modes function primarily to resolve disputes, arbitration and mediation actually partner the courts in its first core function of resolving disputes. In this respect, the institutions which propagate this function have expanded so exponentially, and enjoyed so much success around the world, that their integrity and commitment to the cause of resolving disputes is beyond question.

[24] However, Chief Justice Sundaresh Menon recognised that there is actually a second function of the court which is equally, if not more important than the first. And, that is the function and responsibility of developing the law, both statute and common law, in any given field. The function of the law is to provide the framework for permissible conduct and activity. The courts' role is to define that framework, explain, interpret, adapt and apply the law or the principles to the real factual conditions and circumstances. In so doing, the courts are not only providing remedies to the immediate parties of the dispute before the court but are actually giving authoritative force to the law and enforcing the law; it is developing the law. The courts give legitimacy and integrity to the laws passed.

[25] So, when the courts pass arbitration and arbitration awards by offering it minimum intervention and thereby lending it support and legitimacy, despite the presence of more than 10 out of 50 provisions in the AA 2005 for intervention whether pre, during or after arbitration, can the courts be accused of abrogating from their exercise of judicial power and function? The support of the courts in Malaysia is clear and certain. The High Court, Court of Appeal and the Federal Court spell out the same refrain of minimum intervention. See for instance the decisions of the Federal Court in *Ajwa for Food Industries Co (MIGOP), Egypt v Pacific Inter-Link Sdn Bhd*;<sup>1</sup> *Press Metal Sarawak Sdn Bhd v Etiqa Takaful Bhd*;<sup>2</sup> and *Government of India v Petrocon India Ltd*.<sup>3</sup>

[26] To answer the poser, it is perhaps apt that we begin by looking at the contribution to the development of the law that arbitration disputes could otherwise offer.

[27] Lord Dyson Master of the Rolls in a paper presented at the 2015 Keating Lectures entitled "The Contribution of Construction Cases to the Development of the Law" acknowledged that much of the law of contract, tort, limitation, restitution and damages, to name a few, had in fact benefited from the disputes concerning construction contracts. Construction contracts, after all, are simply contracts, complicated by details. It is these details, both technical and financial that are often off-putting to the extent of being labelled "boring", consisting of all facts and no law. Hence, the judges who first tried these disputes

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1 [2013] 4 AMR 789; [2013] 5 MLJ 625.

2 [2016] 5 AMR 635; [2016] 2 AMCR 473; [2016] 9 CLJ 1.

3 [2016] 4 AMR 225; [2016] 3 MLJ 435.

in the United Kingdom (“UK”) were not even called judges but “Official Referees” (“ORs”) and relegated to the end of a long corridor located at the top floor of the Royal Courts of Justice. When the ORs moved to the Rolls Building at Fetters Lane into the Technology and Construction Courts, the ORs were also addressed as judges. The ORs and thereby construction cases had “come in from the cold”. Lord Dyson cited a long line of landmark cases that we often overlooked that actually emanated from construction disputes. See for example *Atomic Power Construction v Trollope and Colls*;<sup>4</sup> *RTS Flexible Systems Ltd v Molkerei Alois Muller GmbH & Co KG*<sup>5</sup> on the existence of contract; *Young & Marten v McManus Childs*<sup>6</sup> on implied terms; *Chartbrook Ltd v Persimmon Homes*<sup>7</sup> on the proper interpretation of a pricing formula in a contract to develop a mixed development consisting of commercial and residential development; *Rainy Sky SA v Kookmin Bank*<sup>8</sup> concerning a ship building contract; *Sempre Metals Ltd v Welsh Health Technical Services Organisation*<sup>9</sup> on the law of damages; *Ruxley Electronics v Forsyth*;<sup>10</sup> *Anns v Merton LBC*;<sup>11</sup> *Junior Books v Veitchi*;<sup>12</sup> and *Governors of the Peabody Donation Fund v Sir Lindsay Parkinson & Co Ltd & Ors*<sup>13</sup> on the law on duty of care.

[28] Locally, there is the recent Federal Court’s decision in *Dream Property Sdn Bhd v Atlas Housing Sdn Bhd*;<sup>14</sup> a decision which can only be described as seminal on section 71 of the Contracts Act 1950 (Act 136) from the perspective of the law on unjust enrichment and restitution, and the Court of Appeal’s decision in *Tanjung Teras Sdn Bhd v Government of Malaysia*.<sup>15</sup>

[29] In his paper mentioned earlier, Chief Justice Sundaresh Menon acknowledged that “there is some anecdotal evidence to suggest a hollowing out of cases especially in fields such as shipping,

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4 [1963] 1 WLR 333.

5 [2010] 1 WLR 753.

6 [1969] 1 AC 454.

7 [2009] 1 AC 1101.

8 [2011] 1 WLR 2900.

9 [1980] 13 BLR 1.

10 [1995] 3 WLR 118.

11 [1978] AC 728.

12 [1983] 1 AC 520.

13 [1985] AC 210.

14 [2015] 2 AMR 601; [2015] 1 AMCR 469; [2015] 2 MLJ 441.

15 [2015] 9 CLJ 1002.

international contracts, construction and energy law, where arbitration has narrowed the Court's role in building jurisprudence". To this, his Lordship said:

But even so, there will always be a volume of cases that will come before the Courts. Further, some types of disputes are, by their nature not suited to be referred to ADR.

**[30]** This would be the ones where public considerations will override or trump party autonomy. His Lordship remained confident that the judicial function to generate jurisprudence and enforce norms cannot and will not be displaced.

**[31]** There is now disquiet and rumblings which have started and gained some momentum over in the motherland of common law. The courts here must be aware and conscious of these concerns, and should not refrain from exercising discretion for intervention merely out of a pious respect for the twin pillars of arbitration. A swing completely in respect of party choice may be a swing too far in practice, and it may be timely to strike some balance. Had the earlier decisions that were mentioned previously gone the arbitration route, the courts first and the rest of commerce and industry second, would have been deprived of the best opportunity to expound on these critical areas of the law.

**[32]** In the British and Irish Legal Information Lecture or better known as the Bailii Lecture of 2016, The Right Hon. Lord Chief Justice of England and Wales, Lord Thomas of Cwmgiedd spoke on "Developing commercial law through the Courts: rebalancing the relationship between the Court and arbitration". The Lord Chief Justice ("LCJ") expressed similar concerns that arbitration is seriously impeding the development of commercial law and he called for a redressing of the balance between the two. The LCJ said that the UK took a wrong turn in 1979 and 1996 when it introduced measures to make arbitration more attractive in the international market. The measures involved limiting the number of appeals that would come before the courts so that there was more finality and certainty in arbitral awards. Lord Thomas was of the view that limiting the number of appeals reduced the potential for the courts to develop and explain the law, and this endangered the development of the common law, whose strength, vitality and agility forms the framework to underpin international markets, commerce and trade. It is the decision making in the courts that play a vital role in developing the law. When articulated publicly,

the law is developed in the light of reasoned argument that becomes refined and tested before the various tiers of the judiciary. There is also public scrutiny of the law as it develops, and this may lead to or encourage debate in the market place. The issue may then be brought back to the courts and to Parliament, if necessary: "This ensures, as a necessary underpinning to public scrutiny, that the law's development is not hidden from view". In this sense and on the basis of these publicly articulated laws and precedents, markets and their actors can then organise their affairs and business arrangements, says Lord Thomas.

[33] Like Lord Dyson, Lord Thomas reminded that appeals from arbitration awards actually provide a ready source of appellate decisions which have helped shape commercial law. For example, the House of Lords' decision in *L Schuler AG v Wickman Machine Tools Ltd*<sup>16</sup> on the rule that subsequent conduct cannot be used to construe a contract. That case emanated from an arbitration award and a special case procedure.

[34] But, it is the time-consuming process that this and other like cases underwent that contributed to the change of policy in 1979 and 1996. The arbitration in *L Schuler AG* took seven days but the time spent in court was far longer. First instance before Mocatta J was seven days, Court of Appeal presided over by Lord Denning was five days and the House of Lords, another seven days. At that time, pleadings had to be laboriously read aloud to the Bench.

[35] Taking into consideration several other factors such as high interest rates, inflation, that often many disputes arise from a single event, growth of international arbitrations which did not emanate from London and the involvement of many foreign state enterprises, and not forgetting the long delays in the special case procedure as manifested in *L Schuler AG*, there was plenty of cause for the 1979 and later 1996 change of policy. Yet, another argument was that the approach of allowing the courts to intervene to correct and develop the law was out of step with other arbitration centres. It was making London less attractive as a dispute resolution hub.

[36] This appears to have been quite a prevalent view at that time. For instance, this was also Lord Diplock's view as reflected in his Alexander Lecture in 1978, a view which he later laid down in *BTP*

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16 [1974] AC 235.

*Tioxide Ltd v Pioneer Shipping*, better known as *The Nema No. 2*.<sup>17</sup> At the Court of Appeal, Lord Denning had similarly expressed the view that a commercial arbitrator was more likely to be better placed to interpret the contract (frustration of a charterparty) in a commercial sense than a judge and more likely to be right than a judge for that matter although this mischaracterisation of the judge and the arbitrator was disproved by Lord Goff in *The Oinoussian Virtue*.<sup>18</sup> Despite that, Lord Diplock pronounced guidelines on a very restrictive approach on grant of leave for appeals. These guidelines were subsequently codified into the Nema Guidelines by a Departmental Committee chaired by Lords Mustill, Steyn and Saville. This then was implemented through section 69 which we see today in the UK Arbitration Act 1996.

[37] Lord Thomas believed that the UK had not reached the stark example that has taken place in the United States where mandatory arbitration clauses are inserted in contracts. These clauses remove whole classes of claims from the jurisdiction of the courts thereby undermining aspects of the development of the law. Various model and innovative measures have been embarked towards restoring the balance, amongst which is the establishment of a Financial List where specialist judges sit to hear disputes on finance, and a Market Test Case Scheme concerning market issues where there is no immediate relevant authoritative English law guidance. There is no present cause of action and the court is not invited to make any declaratory orders but the procedure allows resolution of any market uncertainties before damage actually accrues, almost pre-emptive in nature. Much else is also underway, including this call for restoring the balance and a revision of the criteria for appeals.

[38] Lord Thomas also addressed the principal tenets of arbitration – autonomy and confidentiality. Autonomy was really as to procedure and evidence; and with the wide array of measures available within the court system, his Lordship saw little difference in practice though there may be in theory. As for confidentiality, his Lordship doubted if there was in any case, certainly not for long and not from all. If the award requires recognition and enforcement, the details enter the public arena anyway. Any perceived advantage is more apparent than real, of interest really to lawyers and generally not newsworthy.

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17 [1982] AC 724.

18 [1981] 2 All ER 887.

[39] In expressing these concerns, his Lordship was actually hearing the cries of concern from the shipping, construction, insurance and commodities industries themselves that there was little case law on standard contracts and changes in commercial practice to guide the industries to better or best practice in real and practical terms. It was time to “re-appraise the pragmatic compromise” adopted in 1979 and 1996. Lord Thomas explained that there was significant irony that has resulted from that policy:

To promote the use of commercial law developed in London through the aim of making London a more attractive centre for dispute resolution reform was effected, the consequence of which has been to undermine the means through which a significant part of its strength – its excellence was developed. But, that undermining will, unless reversed, be to the detriment of the wider interests of the common law as developed in London and to the real interests of London as an international financial and trading centre.

[40] These were Lord Thomas’ concluding remarks that it must always be remembered that:

- (a) It is the courts that develop the law; arbitration does not.
- (b) Courts articulate and explain rights, including definitive rulings on the scope and interpretation of contractual clauses, financial instruments etc.; arbitration does not.
- (c) Open court proceedings enable people to watch, debate, develop contest, and materialise the exercise of both public and private power; arbitration does not.

[41] Lord Thomas is not alone in these thoughts. In the Master’s Lecture of 2006, Justice Coleman already spoke on “Arbitrations and Judges – how much interference should we tolerate?” In his paper, he acknowledged that section 69 is the product of a compromise between two policy objectives which were in conflict; that of party autonomy and the desirability for finality of awards; and the other objective being the need to preserve and develop English commercial law as a valuable national asset. Section 69, firstly through section 1 of the UK Arbitration Act 1979 and later the Arbitration Act 1996, was introduced on the back of a very strong belief that the position of London and English arbitration law was seriously eroded by court interference in arbitration awards through the special case procedure.

Michael O'Reilly, Professor of Law at Kingston University, also carried out some empirical research on the question of whether section 69 should be abolished, a view advocated even by Lord Saville. Professor O'Reilly found from his research encouraging responses (60%) that there should be more appeals from arbitrations to court, not less. He advocated the view that restricting appeals not only stultify the development of the common law but is also unhealthy for the development of international arbitration in the long run.

[42] In his earlier paper, where several cases of intervention by the Singapore court were examined, Chief Justice Sundaresh Menon opined that in the undertaking of intervention and oversight, the "courts should neither be unduly exacting with a view to finding that the arbitral process should not be upheld ... nor should they be too ready to yield so as to refuse relief where the grievance is fairly made out." The courts should bring a "sensible commercial perspective to bear on the issues", a task which I more than strongly believe the courts here can discharge. There is a need to maintain this delicate balance between upholding the consensual nature of the arbitral process and maintaining a degree of judicial oversight to ensure that fundamental standards of procedural fairness are abided and public policy is not contravened. His Lordship believed that the UNCITRAL Model Law has struck this balance well.

[43] It must be so for the Model Law does allow for intervention in prescribed areas. And in those respects and where there is cause to do so, the courts must intervene regardless of the party choice of dispute resolution. The inclusion of recourse to the court is clear indication under the Model Law that there is indeed recourse to the courts. The courts cannot, under cover of parties' options of passive or active intervention – a right afforded by the Model Law anyway – decline or restrict that recourse. The courts cannot, for reasons of party autonomy and minimal intervention, refuse redress when confronted with substantial questions of law under section 42, a mechanism different from the UK section 69 appeals procedure, and decline intervention in the name of those same reasons. When the Arbitration Bill was still in its infancy, the Malaysian Bar had actually proposed a similar appeals mechanism for section 42. That was rejected in favour of what we have today. The availability of recourse to the courts under section 42 has caused the arbitration community to think that there is too much interference from or by the courts. Even more so with

the most recent decision from the Federal Court in *Far East Holdings Bhd & Anor v Majlis Ugama Islam dan Adat Resam Melayu Pahang (and 2 Other Appeals)*.<sup>19</sup>

[44] This recent decision of the Federal Court may be seen as an attempt to put right that balance, that the question of law which may be examined by the courts under section 42 is really “any question of law” as envisaged under that provision. Although not an exhaustive list of the kind of questions that may fall within “the paradigm of ‘any question of law’ in section 42”, indicates an attempt to minimise any development of a parallel body of legal jurisprudence:

- (a) a question of law in relation to matters falling within stage two of Mustill J’s three-stage test;
- (b) a question as to whether the decision of the tribunal was wrong (*Vinava Shipping Co Ltd v Finelvet AG “The Chrysalis”*<sup>20</sup>);
- (c) a question as to whether there was an error of law, and not an error of fact (*Micoperi SrL v Shipowners’ Mutual Protection & Indemnity Association (Luxembourg)*<sup>21</sup>): an error of law in the sense of an erroneous application of the law;
- (d) a question as to whether the correct application of the law inevitably leads to one answer and the tribunal has given another (*MRI Trading AG v Erdenet Mining Corporation LLC*<sup>22</sup>);
- (e) a question as to the correctness of the law applied;
- (f) a question as to the correctness of the tests applied (*Canada v Southam Inc*<sup>23</sup>);
- (g) a question concerning the legal effect to be given to an undisputed set of facts (*Carrier Lumber Ltd v Joe Martin & Sons Ltd*<sup>24</sup>);
- (h) a question as to whether the tribunal has jurisdiction to determine a particular matter (*Premium Brands*): this may also come under section 37 of the AA 2005; and

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19 [2017] 8 AMR 313.

20 [1983] 2 All ER 658.

21 [2011] EWHC 2686 (Comm).

22 [2012] EWHC 1988 (Comm).

23 (1997) 144 DLR (4th) 1 (SCC).

24 [2003] BC.J No. 1602.

- (i) a question of construction of a document (*Intelek Timur Sdn Bhd v Future Heritage Sdn Bhd*<sup>25</sup>).

[45] The intentions and policy behind the 1979 and 1996 Arbitration Acts of the UK are carried in the legislation itself. In the short title, the Act is described as:

An Act to restate and improve the law relating to arbitration pursuant to an arbitration agreement; and to make other provision relating to arbitration and arbitration awards, and for connected purposes.

[46] In section 1, there is clear policy statement set out:

The provisions of this Part are founded on the following principles and shall be construed accordingly:

- (a) The object of arbitration is to obtain the fair resolution or disputes by an impartial tribunal without unnecessary delay or expense;
- (b) The parties are free to agree how their disputes are resolved, subject only to such safeguards as are necessary in the public interest;
- (c) In matters governed by this Part the Court should not intervene except as provided by this Part.

[47] The AA 2005 does not have the same philosophy. Neither does it have the backdrop of the UK experience. In the case of the AA 2005, it was a case of replacing a long overdue piece of legislation which had thrown the country out of sync with the rest of the arbitration world. Given that the AA 2005 deliberately makes no distinction in terms of international and domestic arbitrations in relation to the first two Parts of the Act where the Model Law is incorporated, and given that Malaysia has deliberately shied away from a leave mechanism that exists under section 69 of the UK Arbitration Act 1996, and more particularly given the development of the court system itself at all levels, the arguments and advantage of arbitration being faster and cheaper is fast appearing as an overaged slogan that has stayed long past its shelf life.

[48] Yet, there are still, and always be, real benefits in going to arbitration. Not for autonomy or confidentiality, saving of costs and

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25 [2004] 2 AMR 481; [2004] 1 CLJ 743.

expense, but because of the measure of control and choice over the judge, pace and conduct of the arbitration. There is already a huge availability of experts and expertise as well as local writings on the subject.

[49] When viewed from that perspective, and this is especially so for domestic arbitrations, then substantive law remains always the domain of the court. The application is overseen by the court and where the application afflicts the clear practice as understood outside arbitration, the courts must be ready to step in. There cannot be two parallel bodies of law. The decision of the Federal Court in *Far East Holdings Bhd* setting out the tests for the court's intervention under section 42, to a large extent, serves to minimise that development of a parallel body of law. No court can support such a system or construction in the name of party autonomy; no court can possibly lend integrity to such constructions which run astray of what is generally understood. Declining intervention in the name of minimal intervention would be wrong under such circumstances; any support for the sake of support will only undermine the rule of law. The clear silent choice of options of operations of Part III of the AA 2005 should be given proper regard. If parties want otherwise, then they should exercise the option of the exclusion of operation of section 42 or any or whole of Part III. Otherwise, the courts retain power and have the duty to intervene in the case where substantial rights have been breached.

[50] This is not an attempt or even a suggestion that there must be a retreat. This is a call for a more balanced approach. The courts must keep the balance as they are duty bound to do. When the court's decision to intervene or not to intervene in arbitration is exercised maturely and with confidence and certainty, is well-rationalised and current, it can only aid and support any development of ADR.

# Freedom of Contract and Legislative Intervention: Determining Common Properties in Strata Development

by

*Justice Dato' Vazeer Alam Mydin Meera\**

## **Brief historical context**

[1] The global post-World War II reconstruction and economic boom was a period of immense economic growth, starting from the end of the war until the recession of 1973–75. Post-war Malaya, in the 1950s and subsequently independent Malaysia in the 1960s, also benefitted from this global economic expansion, which brought soaring demand for its two main commodities, rubber and tin.<sup>1</sup> The rapid economic expansion during this period ushered in increased urbanisation of the population, caused in part by the urban pull and rural push phenomena that saw massive migration of rural population to urban centres. The rapid increase in urban population saw a concomitant increase in demand for urban housing and commercial properties. That demand was met in large by construction of high-rise flats (now more fashionably termed as apartments and condominiums) and commercial buildings in the mid-1960s.

[2] The law is often said to play catch-up with the pace of society's progress and to meet socio-economic developmental needs of the time. The development of strata units came with fresh legal issues. In the early 1960s, there was no legislation in existence in the States of Malaya that provided for registration of proprietorship of defined areas of high-rise buildings such as flats or apartments. The subdivision of land into strata lots and the issuance of titles thereto were unheard of at the time. There was lack of a good system of registration of titles to these "mansions in the sky" that gave the owners undisputed and

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\* Judge of the High Court of Malaya.

1 See "An economic review of Malaya: 1945–49: an account of post-war reconstruction and economic progress in Malaya and of current economic problems" by Great Britain, Central Office of Information, Reference Division, London 1950.

unchallengeable title, so that these properties could be transacted and dealt as conveniently as landed properties. Thus, to meet the demands of the populace and industry, there was urgent need to devise a safe and effective system of ownership of these strata properties, similar to the Torrens system of registration and ownership of ground level landed property. This was a challenge faced by most Commonwealth countries.

[3] However, in the interim, sans strata title laws, the legal fraternity improvised and employed various methods to secure ownership rights of purchasers of high-rise strata units. In the introductory chapter of *Rath, Grimes and Moore, Strata Titles*,<sup>2</sup> the learned authors made the following observation in respect of the mode of ownership and conveyance of strata property before the development of strata title laws in Australia:

Since the last war the trend has been towards ownership rather than rental of flats. This raises the question: What were the methods employed to achieve ownership before the Strata Title Act came into force? The answer must be that absolute ownership of flats in the sense that one may “own” a cottage, did not exist. However, a variety of schemes existed calculated to secure to flat-dwellers the nearest practical equivalent to ownership.

[4] Similarly, in Malaya, and subsequently in Malaysia, there were three common methods of ownership of strata property in use then. Professor Teo Keang Sood,<sup>3</sup> a leading authority on land law in Malaysia and Singapore, also made similar observations regarding the pre-strata titles conveyancing regime in the following terms:

As the Federated Malay States Land Code 1926 then in force did not provide for strata title ownership, various devices were resorted to in order to meet the rise in demand for such individually owned flats or units. These included the device of tenancy in common, the home unit company system and the grant of a lease of such a flat or unit.

[5] These methods of ownership were imported mainly from other Torrens system jurisdictions, such as Australia and Singapore, and modified to suit the local needs. They were:

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2 (Sydney: Law Book Co of Australasia Ltd, 1962).

3 See *Strata Title in Singapore and Malaysia*, 4th edn (Singapore: LexisNexis, 2012), p 11.

- (a) the “private leasehold” method;
- (b) the “tenancy-in-common” method; and
- (c) the concept of a home unit company or “company title” method.<sup>4</sup>

These common methods and their shortcomings have been well documented and described by several learned authors in their seminal works on the subject matter.<sup>5</sup> Professor Jamila Hussain also discusses them in her pioneering work on the subject.<sup>6</sup>

[6] These methods were primarily legal devices improvised by law practitioners using existing laws to overcome a lacuna in the law, i.e. to fill the void until such time when strata title laws were enacted and implemented.

[7] Among the three methods, the “private leasehold” method was the most popular device used by conveyancers. The use and prevalence of the private leasehold method as a method of conveying strata property was confirmed by a senior conveyancing practitioner from the 1960s in the course of his testimony in *Tai Aik Tong Sdn Bhd v Embassy Sdn Bhd*.<sup>7</sup>

[8] This sale method of a strata parcel involves the granting to the purchaser by the developer/proprietor a private lease of the strata unit for a term of usually not more than 30 years at a purchase price or “rental” that reflects the actual market value of the property, with a clause for renewal. The sale and purchase agreement and the annexed lease would contain a covenant that expressly allows the use and enjoyment of the common areas by the purchaser/lessee in conjunction with the other lessees in the development. Such agreements would also usually contain a series of covenants to regulate the management of the building block, for example, the common areas or facilities such as stairwells, lifts, pumps, water pipes, water tanks, sewerage

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4 See Su Geok Yam, “Titles in Mid-Air in West Malaysia” (LLB Project Paper, 1976) (unpublished) Faculty of Laws, University of Malaya, Kuala Lumpur for an in depth discussion and detail account of these methods.

5 See for example, Sackville and Neave, *Property Law: Cases and Materials*, 6th edn (Sydney: Butterworths, 1999), para [6.3.197].

6 Jamila Hussain, *Strata Title in Malaysia* (Kuala Lumpur: Pelanduk Publications, 1999).

7 [2013] 5 AMR 279 at 290.

pipes, car parks and service roads within the development. These areas containing the common facilities of the development would be found within areas demarcated as common property, which would usually be held and maintained by the developer or proprietor of the master title. The contracting parties were free to negotiate the terms of the agreement, and when the obligations arising out of contract were consensual, the courts were loath to interfere.<sup>8</sup> This was in keeping with the doctrine of “freedom of contract”<sup>9</sup> and maintaining the sanctity of contract<sup>10</sup> freely entered into by parties.

[9] Whilst much may be said about the freedom of contract, problems, anomalies and aberrations have arisen from time to time in such contractual relationships, and as a result of that, Parliament had seen it fit to intervene and address the undesirable state of affairs.<sup>11</sup> Even though the common law of contract developed as the embodiment of agreements made by the free consent of parties competent to contract, for a lawful consideration and with a lawful object, a concept which now finds statutory force in the Contracts Act 1950 (Act 136),<sup>12</sup> Parliament has on various occasions interfered with the doctrine of freedom of contract to further its legislative purpose of protecting often times the weaker party, particularly consumers at large who might not have much of a bargaining power and be at the mercy of the

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8 See Siti Aliza Alias and Zuhairah Ariff Abdul Ghadas, “Inequality of Bargaining Power and the Doctrine of Unconscionability: Towards Substantive Fairness in Commercial Contracts” (2012) 6(11) *Australian Journal of Basic and Applied Sciences* 331–341.

9 Lord Denning MR in *George Mitchell (Chesterhall) Ltd v Finney Lock Seeds Ltd* [1983] QB 284 at 297; [1983] All ER 108 at 115, referred to the doctrine of “freedom of contract” an “idol” which according to him was shattered by the UK Unfair Contract Terms Act 1977.

10 “... if there is one thing which more than another public policy requires it is that men of full age and competent understanding shall have the utmost liberty of contracting, and that their contracts when entered freely and voluntarily shall be held sacred and shall be enforced by courts of justice. Therefore, you have this paramount public policy to consider – that you are not lightly to interfere with this freedom of contract.”: per Sir George Jessel MR in *Printing and Numerical Registering Co v Sampson* [1875] LR 19 Eq 462.

11 The Hire-Purchase Act 1967 (Act 212); Consumer Protection Act 1999 (Act 599); Housing Development (Control and Licensing) Act 1966 (Act 118) are classic examples of statutes that impose restriction on the freedom of contract.

12 See Contracts Act 1950 (Act 136), ss 10(1), 13, 14, 15, 16, 19 and 20.

stronger party.<sup>13</sup> Parliament has also intervened to correct anomalies that result from a prevailing state of affairs.

### Legislative intervention

[10] There were various shortcomings and problems associated with the then prevailing contractual mechanisms of ownership and conveyance of strata properties, which became the catalyst for legislative intervention. Thus, on January 1, 1966, Parliament via the National Land Code 1965 (Act 56) (“NLC”)<sup>14</sup> introduced for the first time in Malaysia a wholly new concept of property ownership, wherein ownership of strata parcels were evidenced by the issuance of subsidiary titles. However, despite this well-intentioned legislative intervention, these statutory provisions were far from adequate to address the issues at hand. Even though there were provisions in the NLC for the issuance of subsidiary titles to strata units, these provisions were found unworkable as there was no statutory mechanism provided therein for the issuance of subsidiary titles. This state of affairs prevailed well into the 1980s. There is case authority confirming that even as late as in May 1980, strata titles were not issued in Malaysia, nor was there a register of strata titles in existence then. This was observed by the Federal Court in *Faber Merlin (M) Sdn Bhd & Ors v Lye Thai Sang & Anor, Tan Kim Chua Realty (M) Sdn Bhd v Lye Thai Sang & Anor*<sup>15</sup> where Wan Suleiman FCJ speaking for the court observed that:

... strata titles have as yet never been issued in this country, and that no register of strata title exists. The importance of this fact is that the provisions of the National Land Code are irrelevant for the purpose of construing this agreement so that we would have to confine ourselves to the agreement itself to determine the rights of the parties.

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13 See Nurretina and Z Amin, “Unconscionable Contracts: The Courts’ Approach Towards Substantive Fairness” [2003] 4 MLJ clxv; Adnan Trakic, “Statutory Protection of Malaysian Consumers Against Unfair Contract Terms: Has Enough Been Done?” [2015] CLWR 44 3 (203); Cheong May Fong, “A Malaysian Doctrine of Inequality of Bargaining Power and Unconscionability After *Saad Marwi*?” [2005] 4 MLJ i.

14 (Act 56 of 1965), ss 151–157, 161–163 and 355–374. Act 56 repealed and replaced the Federated Malay States Land Code 1926.

15 [1985] 2 MLJ 380, FC.

[11] These inadequacies led to various amendments to the NLC in regards to the provisions relating to subdivision of buildings with a view to enhancing their effectiveness.<sup>16</sup> By way of historical reference, it would be worth noting that these unworkable subsidiary titles provisions in the NLC were repealed and replaced by the Strata Titles Act 1985 (Act 318) (“STA”).<sup>17</sup> It was only then that a proper and workable strata titles regime became operational in Peninsula Malaysia. The STA also underwent changes over the years to address provisions that needed amendments in order to further enhance the strata ownership regime with a view to protecting the interest of parcel owners.

[12] In the series of amendments to the strata properties regime, a separate Act, the Building and Common Property (Maintenance and Management) Act 2007 (Act 663) (“BCPA”), was enacted primarily for the purposes of providing a proper legal framework for the maintenance and management of high-rise strata development, both residential and commercial. There was a recognised need to ensure that the amenities and facilities shared in common were properly managed and maintained. This was, in part, to safeguard strata developments from falling into a state of disrepair and prevent them from turning into decrepit urban slums. The added advantage to parcel owners in such a statutory scheme was obvious in that a properly managed and maintained strata development would enhance value to the parcel owners, both in terms of convenience and property value. The BCPA allowed for the creation of a statutorily mandated joint management body (“JMB”) pending the formation of a management corporation (“MC”) under the STA.<sup>18</sup> Prior to the coming into force of the BCPA, the general practice was for developers and parcel

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16 One such amendment was National Land Code (Amendment) Act 1977 (Act A386), which allowed the State Authority to appoint a designated officer to carry out the functions of and duties of the management corporation in the event that the latter fails to perform any of the duties imposed on it.

17 Act 318 which came into force on June 1, 1985 comprises the old provisions relating to subsidiary titles in the NLC and fresh concepts based on the New South Wales and Singapore strata titles legislation to meet current developments and socio-economic needs. See the Explanatory Statement to the Strata Titles Bill 1985 and also Malaysia Parliamentary Debates (1985) Dewan Rakyat, Sixth Parliament, 3rd Session, Vol III, No 14 at 2261–2264; and Dewan Negara, Sixth Parliament, 3rd Session, Vol III, No 6 at 970–974.

18 The JMB comes into being by operation of law pursuant to the provisions of s 4 of the BCPA. The MC is a statutory body established under s 17 of the STA.

owners to enter into contractual arrangements to provide for the proper maintenance of common areas until the formation of the MC. However, these contractual arrangements were often fraught with problems as there was no statutory backing for such arrangements, and the success of these contractual arrangements were contingent upon the developer and the parcel owners being committed to discharge their respective duties and obligations for the effective management of the strata development. Mismanagement by developers and the lack of participation by parcel owners in the management of strata development led to many high rise developments falling into a state of disrepair. This was often exacerbated by the lack of interest on the part of developers to apply for the issuance of strata titles, which would be the prelude to the formation of the MC. Hence, Parliament enacted the BCPA with the primary objective of providing the necessary legal framework and statutory force for the proper and effective maintenance and management of buildings and common property within a strata development prior to the formation of the MC. Thus, pending the establishment of the MC, the JMB was intended as an interim stopgap measure to address problems plaguing strata schemes, particularly the never-ending disputes between developers/vendors and purchasers/owners of strata parcels.

### **Interaction between contractual provisions and statutory rights**

[13] The statutory definition of common property as provided in the STA and the BCPA, and the contractual concept of common property in the agreements between the developer and parcel owners, may not necessarily be the same. In some cases, areas which had been specifically designated as common property in the contractual documents were excluded from the statutory definition in the STA and the BCPA. This often gave rise to disputes. The responsibility to manage and maintain the common property in the strata development fell on the developer initially, and post-BCPA, on the JMB, until the MC is formed. When the JMB was formed, the developer/proprietor had a legal obligation to hand over the common property within the strata development to the JMB for it was the statutory duty of the JMB to properly maintain the common property and keep it in a state of good and serviceable repair.<sup>19</sup> Therefore, it became important to determine where the boundary lies between the privately owned parcels and common property as

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<sup>19</sup> See BCPA, s 8(1)(a).

often the developer/proprietor chose to retain that which is common property as their own private property. Thus, in *Golden Connection Sdn Bhd v CSH Enterprise Sdn Bhd*,<sup>20</sup> the High Court applied the statutory definition in section 2 of the STA to determine the issue of whether a void area in between a ground level parcel unit sold to the plaintiff and a mezzanine level parcel unit sold to another purchaser came within the definition of “common property” as defined in the STA. The term “common property” in the STA is defined to mean so much of the lot as is not comprised in any parcel (including any accessory parcel) or any provisional block shown in an approved strata plan. The High Court held that it was evident from the relevant plans that the void area is common property as defined in section 4 of the STA, as it was capable of being used in connection with the enjoyment of more than one parcel owner, namely, by both the mezzanine floor unit owner and the ground level unit owner.

[14] Similarly, in *I & P Inderawasih Sdn Bhd lwn Binariang Communications Sdn Bhd*,<sup>21</sup> the dispute was whether the roof, the public stairway to the roof and certain other portions of the building were “common property”. The plaintiff was the developer and registered land owner upon which a strata development was constructed. The plaintiff had sold subdivided lots in the strata development to purchasers. The defendant, after securing the consent of the purchasers of several lots in the building, but without the plaintiff’s authorisation, had constructed a telecommunications transmission station on the rooftop of the building and also prevented access to the roof. The question was whether the areas in question were “common property” under the purview of the plaintiff as developer. Again, the High Court applied the definition in section 4 of the STA and construed that these areas had not been sold together with the lots, and were capable of being enjoyed by more than one parcel owner. Thus, the court held that they were “common property” which came under the plaintiff’s custody as developer since strata titles had not been issued and the MC had not yet been formed. Hence, the court concluded that without the plaintiff’s authorisation, the defendant had trespassed upon the “common property” by constructing a cabin together with telecommunications transmission equipment on the roof and had

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20 [1995] 3 MLJ 731.

21 [1998] 6 MLJ 667; affirmed in [2000] 3 AMR 3198; [2000] 3 MLJ 321, CA.

prevented access to the common stairway. The court found the consent obtained from the parcel owners inoperative and inapplicable in law. In the circumstance, it was the consent of the plaintiff that was material, and not that of the individual purchasers, as these areas were common property within the statutory meaning ascribed in the STA, and further, the management and maintenance of the common property contractually vested with the plaintiff. Therefore, the plaintiff was entitled to the mandatory injunction applied for.

### **Some common issues relating to common properties**

[15] The coming into force of the BCPA further exacerbated and heightened tensions between developers, parcel owners and JMBs. These conflicts often centered on the issues of common property, and its control and management. The disputes were particularly focused on section 44 of the BCPA which states that upon the coming into operation of the Act, the provisions of any written law, contracts or deeds relating to the maintenance and management of buildings and common property in so far as they are contrary to the provisions of that Act shall cease to have effect.<sup>22</sup> This provision often brought about conflicts between developers and parcel owners, particularly in respect of their respective contractual and statutory rights as regards that which is common property and that which is not.<sup>23</sup>

[16] One such dispute arose in *JMC - Kelana Square v Perantara Properties Sdn Bhd*<sup>24</sup> ("Kelana Square"). In that case, following the formation of the plaintiff as the JMB, the defendant who was the developer of the strata development, handed over possession of the common property in the development to the plaintiff. However, the defendant refused to hand over any of the car parks on grounds that the car parks were excluded from the definition of common property under the sale and purchase agreements entered into in 1995 between the purchasers of the strata units and the defendant. The defendant considered the car parks to be its own property and had rented them out to owners

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22 See *Wisma MPL JMB v Malaysia Pacific Corp Bhd* [2012] 6 AMR 553; [2013] 1 CLJ 420; and *Nadia Management Corp v Yap Kuee Hong* [2014] 1 LNS 1539.

23 See *Perbadanan Pengurusan Seri Cendekia v Chee Keng Properties Sdn Bhd & Anor* [2013] 1 LNS 236; *JMB Silverpark Sdn Bhd v Silverpark Sdn Bhd & Anor* [2013] 9 MLJ 714; *Badan Pengurusan Tiara Duta v Timeout Resources Sdn Bhd* [2014] AMEJ 0739; [2015] 1 MLJ 110.

24 [2014] 1 LNS 1085.

and occupiers of the strata units on a daily and/or monthly basis. The plaintiff, as JMB, considered the car parks to be common property by virtue of the provisions of the BCPA, particularly the definition of "common property" in section 4 thereof, and instituted proceedings to claim the same as rightful owners. The plaintiff's arguments were essentially that the building and its maintenance and management are governed by the STA and the BCPA, and as strata titles had not been issued and the MC had not been formed, the plaintiff statutorily came into being to take control of and manage the common property in the development.<sup>25</sup> The plaintiff's powers and duties as a JMB are spelt out in the BCPA,<sup>26</sup> which includes the power and duty:

- (a) to properly maintain the common property and keep it in a good and serviceable repair;
- (b) to determine and impose charges that are necessary for repair and proper maintenance of the common property;
- (c) to order repairs to be done in respect of the common property; and
- (d) to impose and collect from unit owners, maintenance and management charges in proportion to the allocated share units of their respective parcels.

[17] The plaintiff argued in reliance of section 2 of the BCPA, that, since car parks are defined as common property under the BCPA, and common property is to be maintained and managed by the plaintiff as the lawful JMB, the car parks must be handed over to the plaintiff. Now, section 2 of BCPA provides that:

"common property", in relation to a development area, means so much of the development area as is not comprised in any parcel, such as the structural elements of the building, stairs, stairways, fire escapes, entrances and exits, corridors, lobbies, fixtures, and fittings, lifts, refuse chutes, refuse bins, compound drains, water tanks, sewers, pipes, wires, cables and ducts that serve more than one parcel, the exterior of all common parts of the building, playing fields and recreational area, driveways, *car parks, and parking areas*, open spaces, landscape areas, walls and fences, and all other facilities

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<sup>25</sup> See BCPA, s 4.

<sup>26</sup> See BCPA, s 8.

and installations and any part of the land used or capable of being used or enjoyed in common by all the occupiers of the building. (Emphasis added.)

So, obviously, by statutory definition in the BCPA, car parks and parking areas are deemed common property.

[18] However, the defendant applied to strike out the plaintiff's claim by reliance on the provisions of the sale and purchase agreements entered into by the defendant and the purchasers which specifically excluded the car parks as common property. The learned High Court judge accepted the defendant's argument and struck out the plaintiff's claim, on grounds the plaintiff's claim was obviously unsustainable as the purchasers had by contract, i.e. the sale and purchase agreements, agreed to contract out the car parks as common property. However, this decision was reversed by the Court of Appeal and the matter was set down for trial.

[19] At trial the plaintiff submitted that the definition of the common property in the sale and purchase agreements was inconsistent with the statutory definition of common property under the BCPA, and as such, contended that the definition under the statute ought to prevail. Thus, the plaintiff argued that the car parks ought to be surrendered to the plaintiff together with all income that the defendant has generated from renting out the car park since the incorporation of the plaintiff.

[20] The defendant, on the other hand, argued that all the purchasers/owners of parcel units in Kelana Square had contractually agreed with the defendant via provisions in the sales and purchase agreements ("SPA") that the common property in Kelana Square excluded the car parks found in basements 1, 2 and 3 and on the ground level surface area of Kelana Square, and therefore the plaintiff could not have rights over the car parks. In this regard, the defendant relied on the contractual definition of "common property" in the SPA, which read as follows:

"Common Property" means, in relation to the Shop office Project, so much of the area in the Shop office Project as is not comprised in any Unit (including Any accessory Unit) or any provisional blocks as shown in the approved Building Plans, including but not limited to such facilities and services stipulated in the Fifth Schedule hereto

which are reserved for the use and enjoyment of the purchasers of the Units comprised in the Shop office Project, but excluding:

- (a) all surface car parks demarcated or constructed in or about the Shop office Project and all covered car parks (including the basement car parks and any other car parks); and
- (b) the food court and deli which are situated on the ground level and Plaza level; In the Shop office Project.

Further, Clause 5.08 of the SPA also provides that the purchasers had agreed with the defendant that the said car parks are not included in any sale of parcel units of Kelana Square, whether as common property or as an accessory unit. Clause 5.08 reads as follows:

5.08. Retention of Car Park, Food Court and Deli

Notwithstanding the sale of the Unit to the Purchaser and the sale of the parcels of office and/or retail units comprised in the Shop office Project, the Purchaser agrees and confirms that all surface car parks and covered car parks (including the basement parking and any other parking) in the Shop office Project and the food court and deli situated on the ground level and plaza level respectively shall belong to the vendor and shall not be included into the sale of the Unit whether as an accessory unit or common property.

[21] In addition to that, the Kelana Square House Rules, which governs the use of the building, the shop and office units and common property of Kelana Square, and which is enforced by the plaintiff, specifically excludes the car parks in Kelana Square from the definition of common property. Thus, the defendant contended that the plaintiff has tacitly agreed via the said House Rules, which is a contract *inter se* between the parcel owners and the JMB, that the car parks in Kelana Square are excluded as common property. Finally, the defendants argued that the plaintiff's claim that the car parks are common property of Kelana Square under the BCPA is misconceived because the BCPA does not have retrospective effect or application as the Kelana Square SPAs were entered into sometime beginning from 1995, i.e. well before the coming into effect of the BCPA. This final point was grounded on the pronouncement of the Federal Court in *Badan Pengurusan Bersama Paradesa Rustika v Sri Damansara Sdn Bhd*<sup>27</sup> that the BCPA does not have retrospective effect.

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27 [2013] 6 AMR 517; [2014] 1 MLJ 14; [2013] 9 CLJ 813.

[22] The High Court in *Kelana Square* found for the plaintiff and declared the car parks in the strata development were common property, despite the contractual stipulations to the contrary. In coming to that finding, the High Court had placed emphasis on the definition of “common property” as in section 2 of the BCPA, and had also relied on the provisions of sections 44 and 45 of the BCPA. The following parts of the judgment of the High Court is apposite for our current purpose:

BCPA 2007 has very clearly provided that car parks are part of common property. Although the defendant’s argument is that BCPA 2007 does not have retrospective effect, in my considered opinion section 44 of BCPA 2007 provides saving clause which says as follows:

“On the coming into operation of this Act, in a local authority area or part of a local authority area or in any other area, the provisions of any written law, contracts and deeds relating to the maintenance and management of buildings and common property in as far as they are contrary to the provisions of this Act shall cease to have effect within the local authority area or that other area.”

Section 44 must be read together with section 45(1) of the BCPA 2007 which provides as follows:

“The provisions of this Act shall have effect notwithstanding any stipulation to the contrary in any agreement, contract or arrangement entered into after the commencement of this Act.”

It is my considered opinion that by virtue of the saving clause in section 44 read with section 45(1), it is very clear to me the definition of “Common Property” in the SPA at page 4 of Agreed Bundle B6, as far as provisions excluding all surface car parks demarcated or constructed in or about the Shop office Project and all covered car parks (including the basement car parks and any other car parks) are contrary to the provisions of this BCPA 2007 and the provisions shall cease to have effect.

[23] The decision in *Kelana Square* mirrored an earlier decision of the High Court in *Ideal Advantage Sdn Bhd v Palm Spring Joint Management Body & Anor*<sup>28</sup> (“*Ideal Advantage*”) wherein the court held that the transfer of car parks in the strata development by the developer

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28 [2014] 1 AMR 49; [2014] 1 CLJ 598.

to the plaintiff was in contravention of the provisions of the BCPA and declared that the car parks were common property within the meaning ascribed in the BCPA. In effect, the High Court in both these cases were of the view that section 44 of the BCPA would supersede the contractual bargain freely entered into by the parties. Since the definition of common property in section 2 of the BCPA included car parks, therefore, the court held that the sale and purchase agreements that excluded car parks from common property were contrary to statute and accordingly held them to be void to that extent.<sup>29</sup>

[24] The judgments of the High Court in *Kelana Square* and *Ideal Advantage*<sup>30</sup> were a departure from an earlier decision of another High Court, wherein it was held that prior to the coming into force of the BCPA, the position as regards the rights of parties in a strata development would be governed by the agreements freely entered into by the parties.<sup>31</sup> However, it must be noted that both the decisions in *Kelana Square* and *Ideal Advantage* were keeping in line with the general judicial trend in that most disputes as regards ownership of car parks and other areas housing common facilities were being resolved in favour of parcel owners, primarily because of statutory provisions in the BCPA read together with the provisions in the STA.

[25] The *Kelana Square* decision was, however short lived and overruled in part by the Court of Appeal. In *Perantara Properties Sdn Bhd v JMC - Kelana Square & Another Appeal*,<sup>32</sup> the Court of Appeal acknowledged the fact that in section 2 of the BCPA, Parliament had seen it fit to make car parks in any development with common facilities as common

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29 See also *Perbadanan Pengurusan Palm Spring @ Damansara v Muafakat Kekal Sdn Bhd & Ors (No 2)* [2015] MLJU 279 where by reference to the definition of common property in section 2 of the BCPA, the High Court found the car parks in dispute to be common property and accordingly ordered the cancellation of strata titles for the car parks issued in the name of the developer.

30 The judgment in *Ideal Advantage* (supra) was however subsequently set aside by the Court of Appeal on the basis that in an entirely separate proceeding, the formation of the JMB was declared void *ab initio*.

31 See *Sharon Lobo v AAB Avenue 1 Sdn Bhd & 3 Ors* [2010] AMEJ 0105 where Dr Prasad Sandosham Abraham J (as he then was) held at p 39: "... The question is what is the position prior to the coming into force of BCPA? It is my judgment that reading sections 44 and 45(1) of the BCPA, it is clear that prior to 2007, it is governed by agreements entered into before the parties ...".

32 [2016] 5 CLJ 367.

property. However, the Court of Appeal disagreed with the High Court to the extent that the enactment had retrospective effect to alter the contractual relationship of the parties and their respective contractual rights flowing therefrom and held that:

The effect of the learned judge's construction of s 44 read with the definition of "common properties" in s 2 of the BCPA 2007 is a blatant amendment to the terms and conditions of the 1995 sales and purchase agreements. That said, his Lordship's view on face value can be said to have merit as s 44 of the BCPA 2007 does contain the words "shall cease to have effect", giving rise to a reasonable inference that BCPA 2007 is a retrospective legislation to eradicate the practice of developers like the appellant from retaining car parks as common properties.

The Court of Appeal further observed that:

... it is significant that the 1995 sales and purchase agreements at that particular time were perfectly legal agreements. There were no common law or statute law which prohibited the same. Hence when the purchasers and the appellant entered into those agreements they were exercising their rights pursuant to the concept of "freedom of contract" as submitted by learned counsel. These rights are fundamental rights and the courts must presume that Parliament would not invade such rights unless clear words are used. We find no such clear words in BCPA 2007. The parties knew exactly what the bargains were when they entered into the 1995 sales and purchase agreements and it is trite law the courts cannot rewrite contracts when they are freely entered into.

[26] The Court of Appeal seems to have placed great emphasis on the sanctity of contract entered into by the parties prior to the coming into force of the BCPA and was of the opinion that the contractual rights flowing from the contract must be upheld.<sup>33</sup> "The fundamental principle of the sanctity of contract is meant to be honoured by contracting parties, and must therefore be upheld."<sup>34</sup> The Court of Appeal in

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33 The time honoured principle of sanctity of contract envisages that a party to a contract cannot unilaterally impose a new term to the existing agreement, nor vary, subtract from or add to the prevailing terms.

34 See *HSBC Bank Malaysia Berhad v Dato' Seri Mohamad Khir bin Toyo & Anor* [2016] MLJU 1370.

*Pernec Ebiz Sdn Bhd v CCI Technology Sdn Bhd & Ors*<sup>35</sup> alluded to “the principle that contracting parties are obliged to uphold the sanctity of contract and honour the bargain they have entered into, as embodied in s 38(1) of the Contracts Act 1950:

The parties to a contract must either perform, or offer to perform, their respective promises, unless the performance is dispensed with or excused under this Act, or of any other law.

[27] Similarly, the Federal Court in *Merita Merchant Bank Singapore Ltd v Dewan Bahasa Dan Pustaka*<sup>36</sup> said that it “... was a well-established principle sanctioned by the doctrine of sanctity of contract that parties who make agreement must adhere to their terms.” The Federal Court, once again, in the recent case of *Thai-Lao Lignite Co Ltd & Anor v Government of the Lao People’s Democratic Republic*<sup>37</sup> reiterated that our courts must uphold the sanctity of the principle of party autonomy and freedom of contract.<sup>38</sup> And that has been the prevalent judicial view for some time now. The freedom of contract doctrine is the cornerstone of our law of contracts and the Malaysian courts have consistently refrained from interfering and rewriting contracts freely entered into by parties.<sup>39</sup>

[28] The importance of the Court of Appeal’s decision in *Kelana Square* is that, firstly, the court recognised the sanctity of contract entered into by the parties, and secondly, the court held that the BCPA cannot be applied retrospectively to contracts entered prior to the coming into effect of the statute. This means that the court was of the view that once the BCPA was in force any prospective attempt to demarcate car parks in a strata development and carve them out as private property would be contrary to the provisions of the BCPA, particularly the definition of common property in section 2 of the BCPA, and as such

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35 [2014] AMEJ 0836; [2015] 2 MLJ 117.

36 [2015] 1 AMR 575; [2014] MLJU 1807.

37 [2017] 6 AMR 219; [2017] 9 CLJ 273.

38 For instances where the courts have strictly upheld the doctrine of freedom of contract, see *Sri Kajang Rock Products Sdn Bhd v Mayban Finance Bhd & Ors* [1992] 3 CLJ Rep 611; *NFC Labuan Shipleasing I Ltd v Sumatec Resources Bhd* [2017] 1 LNS 1172; *Wisma Perkasa Sdn Bhd v Weatherford (M) Sdn Bhd & Anor* [2017] 2 AMR 92; [2017] 5 CLJ 219.

39 There is a new-found tendency by the courts to intervene in appropriate cases in the guise of unconscionability. See *Saad bin Marwi v Chan Hwan Hua* [2001] 2 AMR; [2001] 3 CLJ 98.

it would be struck down. This view would be consonant with settled law and in accordance with the provisions of section 45 of the BCPA which prohibits contracting out of the statute. The prohibition against contracting out of statute was reaffirmed by the Supreme Court in *Gimstern Corp (M) Sdn Bhd v Global Insurance Co Sdn Bhd*<sup>40</sup> where it was held that “parties cannot contract out of an Act of Parliament, that is to say they cannot include in their contract terms and conditions which are contrary to the Act. If they do so, such terms and conditions are void.”<sup>41</sup> However, in *Kelana Square*, the Court of Appeal found that the developer was not attempting to contract out of any statutory provision, for the statute was not in force at the material time in 1995 when the SPAs were entered into. The Court of Appeal further held that the BCPA does have retrospective application for the statute does not provide for such retrospective application. That the BCPA does not operate retrospectively was made clear by the Federal Court in *Badan Pengurusan Bersama Paradesa Rustika v Sri Damansara Sdn Bhd*<sup>42</sup> (“*Paradesa Rustika*”). Zulkefli Makinudin CJM (as he then was) in delivering the judgment of the court said:<sup>43</sup>

It is therefore clear that the provisions of the Act do not have retrospective effect. The requirement in relation to the opening and maintenance of the building maintenance account in our view did not apply to the respondent as the condominium had long been completed, and possession of the individual units had been handed over to the purchasers more than seven years earlier. On this point the question of giving the provision of the Act a purposive interpretation as suggested by learned counsel for the appellant does not arise as the provision of the law is very clear. It is a trite proposition that an Act of Parliament only comes into operation from the date the Act provides for the same. Section 19 of the Interpretation Acts 1948 and 1967 provides that:

- (1) The commencement of an Act or subsidiary legislation shall be the date provided in or under the Act or subsidiary legislation or, where no date is provided, the date immediately following the date of its publication in pursuance of section 18.

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40 [1987] 1 MLJ 302.

41 See also the Federal Court’s decision in *SEA Housing Corp Sdn Bhd v Lee Poh Choo* [1982] 2 MLJ 31.

42 [2013] 6 AMR 517; [2014] 1 MLJ 14.

43 *Ibid*, at 524 (AMR); 24-25 (MLJ).

- (2) Acts and subsidiary legislation shall come into operation immediately on the expiration of the day preceding their commencement.

There is therefore no basis or no room for an argument that the Act has retrospective application as there is no indication to the contrary within its four corners.

[29] The determination of the Federal Court on the point of retrospective application was very much a part of the *ratio decidendi* of the decision.<sup>44</sup> The Federal Court had unequivocally concluded that the provisions of the BCPA do not have retrospective effect. In supporting its said conclusion, the Federal Court had noted that there “is no indication to the contrary within its four corners” to say otherwise. This observation is important for, as a matter of law, it is presumed that a statute is not intended to have retrospective operation, save where a contrary intention appears.<sup>45</sup> If the legislature intends that an Act or enactment is to have retrospective application, “it must expressly and clearly say so”.<sup>46</sup> In *Paradesa Rustika*, the Federal Court reiterated the principle that a statute comes into force only from the date stipulated therein.

[30] The *dicta* of the Federal Court in *Paradesa Rustika* was applied by the Court of Appeal in *Kelana Jaya*<sup>47</sup> in coming to the conclusion that section 2 of the BCPA does not in any way indicate that the definition of “common property” is intended to apply retrospectively. Further, it must be gainsaid that a retrospective operation should not be given to a statute to impair an existing right. When there is doubt as to

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44 The Supreme Court of Victoria in *Melbourne Cricket Club v Clohesy* [2005] 14 VR 206 noted that *ratio decidendi* refers to the proposition of law expressed or necessarily implied by a court as providing the legal justification for deciding a case, or a particular issue in a case, in a particular way. See para 100 of the said decision.

45 *National Land Finance Co-Operative Society Ltd v Director General of Inland Revenue* [1993] 2 AMR 3581, SC at 3590; [1994] 1 MLJ 99, SC at 106.

46 *Tenaga Nasional Bhd v Kamarstone Sdn Bhd* [2014] 1 AMR 522, FC at 527; [2014] 2 MLJ 749, FC at 756; *Puncakdana Sdn Bhd v Tribunal for Housebuyers Claims & Another Application* [2003] 5 AMR 570; [2003] 4 MLJ 9.

47 The Court of Appeal was bound to apply the *dicta* by virtue of the doctrine of *stare decisis*. See the Federal Court judgments in *Co-Operative Central Bank Ltd (In Receivership) v Feyen Development Sdn Bhd (Feyen No. 2)* [1997] 3 AMR 2673 at 2682; [1997] 2 MLJ 829 at 836–837; and *Lembaga Tata tertib Perkhidmatan Awam Hospital Besar Pulau Pinang & Anor v Utra Badi all K Perumal* [2001] 2 AMR 1905 at 1951–1952; [2001] 2 MLJ 417 at 449 for an application of this doctrine.

whether the legislature had intended to impair the existing rights of the subjects, such doubt must be construed in favour of the subject.<sup>48</sup> In the House of Lords judgment of *Colonial Sugar Refining Co Ltd v Melbourne Harbour Trust Commissioners*,<sup>49</sup> Lord Warrington of Clyffe noted:

In considering the construction and effect of this Act, the Board is guided by the well known principle that a statute should not be held to take away private rights of property without compensation unless the intention to do so is expressed in clear and unambiguous terms.

[31] That private right of property ownership is of course a basic constitutional right embodied in Article 13 of the Federal Constitution that reads:

- (1) No person shall be deprived of property save in accordance with law.
- (2) No law shall provide for the compulsory acquisition or use of property without adequate compensation.

[32] It is trite law that private property can only be compulsorily acquired or used by the State and not otherwise. The rationale of compulsory acquisition by the State is that private interests may in some circumstances be subordinated to the higher interests of the public. Patanjali Sastri, CJ in delivering the judgment of the Indian Supreme Court in *State of Bihar v Kameshwar Singh*,<sup>50</sup> said:

It is true that under the common law of eminent domain as recognized in the jurisprudence of all civilized countries, the State cannot take the property of its subject unless such property is required for a public purpose and without compensating the owner for its loss.

[33] However, it must be noted that such laws, if at all, must be stated in clear and unambiguous terms. Further, such laws must afford adequate compensation. Viscount Dilhorne in delivering the judgment of the Privy Council in *Government of Malaysia & Anor v Selangor Pilot Association*<sup>51</sup> observed:

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48 *National Land Finance Co-Operative Society Ltd v Director General of Inland Revenue* [1993] 2 AMR 3581, SC at 3590-3591; [1994] 1 MLJ 99, SC at 106-107.

49 [1927] AC 343 at 359.

50 AIR 1952 SC 252 at 264.

51 [1977] 1 MLJ 133 at 137.

Article 13(2) places a restriction on the powers of the Legislature. It is not within its power to pass a law providing for the compulsory acquisition or use of someone else's property without providing for the payment of compensation.

[34] In this regard, the Court of Appeal in *Kelana Square* made this pointed observation:

There is no doubt that should we sustain the respondent's contention, we would be taking away the proprietary rights in the car parks of the appellant. Could this be done by an Act of Parliament? It must not be forgotten that we have a democratic system where the Federal Constitution is supreme as opposed to Parliamentary democracy where Parliament is supreme. Hence in construing provisions of statute regard must be given to the Federal Constitution. The relevant presumption here is simply that Parliament did not intend to invade the rights accorded in the Federal Constitution.

[35] The Court of Appeal took a similar approach in *Prestaharta Sdn Bhd v Ahmad Kamal Md Alif & Ors*<sup>52</sup> ("*Prestaharta*"), where the core issue that arose for determination was the question of what is common property under the relevant and applicable laws in the context of a housing development, and in particular the rights enshrined in the contract entered into freely by the parties. The Court of Appeal in *Prestaharta* held that:

The answer to the issue is simple and straight forward, taking into consideration the time the sales and purchase agreement was concluded. At that time there was no statutory control as to how the common property is to be used or divided or reserved by the developer. It was all based on contractual terms. The Housing and Development Act 1966 and/or the Housing Development (Development & Licensing) Regulations 1989 only required a S&P to be signed as per the Statutory Form. The issue of common property, etc. was done through a DMC. There was no law prohibiting DMC or any case laws to say DMC is illegal, bad in law or against the Housing and Development Act 1966, Housing Development (Control & Licensing) Regulation 1989 or Strata Titles Act 1985 at the time of the S&P was entered into.

In Clause 4.1 of the *Prestaharta* Deed of Mutual Covenant ("*DMC*"), it is provided that:

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52 [2016] AMEJ 1448; [2016] 1 LNS 255.

The Purchaser hereby agrees, covenants and undertakes that Vendor may provide at its discretion the Additional Facilities for the use and enjoyment of the Purchaser and other invitees of the Vendor as set out in the Second Schedule hereto. For the avoidance of doubt it is hereby declared that “Additional Facilities including the car park shall not under any circumstances form part of the Common Property and the ownership of the Additional Facilities shall remain solely with the Vendor.

[36] The respondents in *Prestaharta*, who were parcel owners, argued on the strength of the provisions of the BCPA that the disputed areas were common property despite the categorical covenant in the DMC that the ownership of these areas were reserved to the vendor. The Court of Appeal rejected that argument and upheld the contractual provisions in the sale and purchase agreement as well as the DMC. The relevant part of the judgment reads:

Under the S&P, the plaintiffs were fully apprised of the fact that the common property or facilities of the Riviera Bay Resort Condominium (the RBRC) only consisted of the facilities specified in the Second Schedule thereto. These facilities were being enjoyed by the plaintiffs. An important point to note is that these common facilities do not form part of the subject property comprising 22 facilities with an area of 78,943 sq ft acquired by the defendant together with 149 parcels from Pengurusan Danaharta Nasional Berhad (Danaharta). The subject property in fact, relates to the “Additional Facilities”, 22 altogether, set out in the Second Schedule to the DMC being facilities for the resort. These Additional Facilities were excluded from the common property defined in the S&P.

[37] Once again the Court of Appeal upheld the sanctity of the contract, which was a perfectly valid and enforceable agreement at the time it was entered into. The Court of Appeal found for the appellant and observed that the “... terms of the DMC provide an unequivocal and clear indication that the Additional Facilities are expressly excluded from the common property and the ownership thereof remain solely with the developer”.

[38] Therefore, when there are clear and unambiguous contractual provisions, the courts have generally given regard to them and upheld the bargain struck between the parties. In such circumstance, the courts have refrained from altering the contractual rights of parties by applying statutory provisions found in subsequent legislation that

would have the effect of taking away proprietary rights of one or more of the contracting parties, as that would be clearly unconstitutional.

[39] When the agreements in *Kelana Square* and *Prestaharta* were made, they were not governed by the BCPA, and in situations such as that, the role of the court is to give effect to the contract and interpret the contract by applying a commercially sensible construction. This was the advice of the Federal Court in *Berjaya Times Square Sdn Bhd v M-Concept Sdn Bhd*<sup>53</sup> where Gopal Sri Ram FCJ in delivering the majority judgment of the court held:

The agreement in the present case is one that is not regulated by statute. In short, it is not a contract governed by the Housing Developers legislation. The appellant and respondent were therefore at complete liberty, in accordance with the doctrine of freedom of contract to agree on any terms they thought fit. The role of the court is to interpret the contract in a sensible fashion. See, *Loh Wai Lian v SEA Housing Corporation Sdn Bhd* [1987] 2 MLJ 1.

[40] The Court of Appeal in both *Kelana Jaya* and *Prestaharta* has done precisely that. However, in contrast to the decisions in *Kelana Square* and *Prestaharta*, the Court of Appeal in *Ken Property Sdn Bhd v Badan Pengurusan Bersama Ken Damansara II Condominium*<sup>54</sup> in construing the question of whether the car parks and several other commercial lots in the strata development were common property, found for the defendant, JMB, on grounds that the plaintiff/developer had failed to prove its alleged ownership over the car park bays and shop lots. The Court of Appeal in *Ken Property* had in the course of its judgment also referred to the House Rules attached to the statutory sale and purchase agreement entered into between the plaintiff/developer and the purchasers which clearly showed that the common facilities to be provided by the plaintiff/developer shall include, *inter alia*, nursery, games room, gymnasium, squash court and multipurpose hall ("the common facilities") and at trial the plaintiff/developer's own witness testified, *inter alia*, that the shop lots, now claimed by the plaintiff/developer, were in fact intended to be used for the purpose of providing the common facilities to the residents. Thus, the contractual stipulations were indicative of the disputed areas being construed as common property.

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53 [2010] 2 AMR 205; [2010] 1 MLJ 597.

54 [2016] AMEJ 1166.

**[41]** A similar issue was also decided by the Court of Appeal in *Malaysia Land Properties Sdn Bhd v Waldorf & Windsor Joint Management Body*<sup>55</sup> where the court found that the disputed areas on the seventh floor of the strata development were common property and held that:

... the entire 7th floor had been initially designated as common property, the appellant is not at liberty to invoke clause 43.1(f) of the sale and purchase agreement to de-designate the disputed area and convert it to its own use. The appellant is bound by the sales brochure read with the sale and purchase agreement and the law to uphold what had been originally planned and approved namely, that the disputed area is common property. Once the purchasers had been given vacant possession of their respective parcels the performance of the sale and purchase agreements was complete. The appellant cannot be seen to be allowed to have any reservation of rights to be exercised “from time to time” subsequently for its own benefit.

**[42]** A common thread in all the above Court of Appeal decisions is that the sanctity of the contract entered into by the parties must be upheld, and where any subsequent legislation seems to interfere in the contractual rights of parties, especially where such contractual rights are in respect of proprietary interest in land, the application of such statutory provisions must be done with circumspection. After all, when the contractual rights are sought to be altered based on the definition sections of a statute that has no contextual relationship with the contract terms, the courts are reluctant to do so. In this regard, the Federal Court in *Metramac Corp Sdn Bhd (formerly known as Syarikat Teratai KG Sdn Bhd) v Fawziah Holdings Sdn Bhd*<sup>56</sup> reconfirmed the principle that a definition clause is always subject to the context and must be read with the scheme of the statute and what the enactment intended to remedy. The scope of the BCPA is confined to the maintenance and management of buildings and common property. The preamble to the BCPA states that it is:

An Act to provide for the proper maintenance and management of buildings and common property, and for matters incidental thereto.

**[43]** The Minister who presented the BCP Bill in the House of Representatives on December 12, 2006 had repeatedly stressed that

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55 [2014] 3 AMR 591; [2014] 3 MLJ 467.

56 [2006] 3 AMR 725; [2006] 4 MLJ 113.

the application of the BCPA extended only to the maintenance and management of buildings and common property. Thus, the definition of common property in section 2 of the BCPA cannot be understood as divesting any party of its ownership in property. The definition of common property in the BCPA does not provide as such. It is well settled that a definition section cannot be construed so as to enlarge the scope of the statute containing it.<sup>57</sup> Thus, the courts do not have the power to enlarge the scope of the BCPA to include ownership rights over property, when any extension of the meaning would be to confer benefits on persons not intended to be benefited by the legislature and at the expense of another's proprietary interest arising from a valid and enforceable contract. To allow such a reading of the law would mean that Parliament had enacted the BCPA to allow for the compulsory acquisition of property for and on behalf of purchasers/JMB's without the payment of any compensation. That would be a clear violation of Article 13 of the Federal Constitution and would never be the intention of Parliament.

[44] The problems created by the definition of common property in the BCPA seems to have caught the attention of Parliament and in 2013 the legislature enacted the Strata Management Act 2013 (Act 757) ("SMA")<sup>58</sup> as an Act to repeal and replace the BCPA. In the SMA, the definition of "common property" is different from the BCPA, and in particular car parks are not specifically stated as common property. Section 2 of the SMA provides:

In this Act, unless the context otherwise requires –

"common property" –

- (a) in relation to a building or land intended for subdivision into parcels, means so much of the development area –
  - (i) as is not comprised in any parcel or proposed parcel;  
and

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57 See the judgment of Ramachandra Iyer CJ in the Indian High Court case of *Pappathi Ammal v Nallu Pillai* AIR 1964 Mad 173 at 176.

58 Act 757 that came into force on June 1, 2015, PU(B) 231/2015 – States of Johore, Kedah, Kelantan, Malacca, Negeri Sembilan, Pahang, Terengganu, Perak, Perlis and Selangor; June 1, 2015, PU(B) 237/2015 – Federal Territory of Kuala Lumpur, the Federal Territory of Labuan and the Federal Territory of Putrajaya; June 12, 2015, PU(B) 248/2015 – State of Penang.

- (ii) used or capable of being used or enjoyed by occupiers of two or more parcels or proposed parcels; or
- (b) in relation to a subdivided building or land, means so much of the lot –
  - (i) as is not comprised in any parcel, including any accessory parcel, or any provisional block as shown in a certified strata plan; and
  - (ii) used or capable of being used or enjoyed by occupiers of two or more parcels.

**[45]** This definition is more in tandem with the definition of common property provided in section 4 of the STA, which is expressed in general rather than specific terms. This definition also corresponds to the definition of common property in the Singapore Building Maintenance and Strata Management Act. From the above definition in the new Act, in order to constitute common property, two requirements must be satisfied, namely, that such part of the development is not comprised in any parcel or accessory parcel or proposed parcel and that part must be used or capable of being used or enjoyed by occupiers of two or more parcels or proposed parcels. Hence, whilst it may still be possible to argue that car parks could be common property if they are not comprised in any parcel or accessory parcel, the new statutory definition of common property does not make a definitive statement of their inclusion as common property, as was the case in section 2 of the BCPA. This may to some extent alleviate the earlier problems associated with the definition of common property in the BCPA.

# Lifting of the Corporate Veil

by

Justice S Nantha Balan\*

[1] This article looks at the law as it presently stands, in relation to lifting or piercing of the corporate veil in Malaysia, the United Kingdom, Hong Kong, Singapore and Australia. In particular, it examines the seminal decisions of the Supreme Court of the United Kingdom in *VTB Capital plc v Nutritek International Corp & Ors* (“VTB”)<sup>1</sup> and *Prest v Petrodel Resources Ltd & Ors* (“Prest”).<sup>2</sup>

## Separate legal entity

[2] An incorporated company is a distinct and separate legal entity which can sue and be sued in its own name. The company is a juristic entity which is separate from its shareholders, directors, servants, agents and managers. That has always been the position in Malaysia. It still is. In Malaysia, the position of the company as a separate legal entity is statutorily encapsulated in section 20 of the Companies Act 2016 (Act 777) (“CA 2016”) (formerly section 16(5) of the Companies Act 1965 (Act 125) (“CA 1965”). Section 16(5) of the CA 1965 states that from the date of incorporation, “... the company shall be a body corporate by the name contained in the memorandum capable forthwith of exercising all the functions of an incorporated company and of suing and being sued ...”. But, section 16(5) of the CA 1965 makes no mention of the company being a separate legal entity. However, notwithstanding the absence of any specific reference to the separate legal entity principle in the language of the statute, the Malaysian courts have always recognised the separate legal entity principle in so far as companies incorporated under the CA 1965 are concerned. In *Lee Eng Eow v Mary Lee & Anor*,<sup>3</sup> NH Chan JCA remarked that “... The

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\* Judge of the High Court of Malaya.

1 [2013] UKSC 5; [2013] 1 All ER 1296; [2013] BCC 514; [2013] 1 CLC 153; [2013] 1 Lloyd’s Rep 466; [2013] 2 AC 337; [2013] 1 BCLC 179; [2013] 1 All ER (Comm) 1009; [2013] 2 WLR 398.

2 [2013] UKSC 34; [2013] 4 All ER 673; [2013] Fam Law 953; [2013] 2 FLR 732; [2013] BCC 571; [2013] 2 AC 415; [2013] 3 WLR 1.

3 [1999] 3 AMR 2885 at 2893; [1999] 3 MLJ 481 at 486.

separate legal personality of a company is not specifically provided for in the Companies Act. Nevertheless, the whole scheme of the Act is predicated upon the company's separate existence ...".

[3] Interestingly, section 20 of the CA 2016 (which permits a private company to be formed by a single shareholder and having a single director) has now underscored the separate legal entity principle by expressly stating that upon incorporation, the company is a body corporate and shall "have legal personality separate from that of its members". It would appear that section 20 of the CA 2016 is somewhat of a statutory codification of the established principle in *Salomon v A Salomon & Co Ltd* ("*Salomon*")<sup>4</sup> that a limited liability company established by statute has a legal existence and juristic personality separate from its shareholders. The obvious starting point in this discussion is therefore the landmark decision of the House of Lords in *Salomon*.

[4] The *Salomon* principle was comprehensively examined by Munby J in *Ben Hashem v Al Shayif & Anor*<sup>5</sup> where he referred to the opinions of the Law Lords in *Salomon* and (helpfully) distilled the salient parts of their judgment and said:

[101] The need to adopt a principled approach makes it convenient at this point to draw attention to those elementary principles of company law forever to be associated with the fundamentally important decision of the House of Lords in *Salomon v A Salomon and Company Limited* [1897] AC 22, the case which established once and for all that a "one man company" is a legal entity distinct from its owner and controller and that that individual is not liable on the company's obligations.

[102] For present purposes there is no need for me to rehearse the facts of the case. It suffices to identify the important point of principle it established. The general point was spelt out by Lord Halsbury LC at page 30:

*"it seems to me impossible to dispute that once the company is legally incorporated it must be treated like any other independent person with its rights and liabilities appropriate to itself, and that the motives of*

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4 [1897] AC 22.

5 [2008] EWHC 2380 (Fam); [2008] Fam Law 1179; [2009] 1 FLR 115.

*those who took part in the promotion of the company are absolutely irrelevant in discussing what those rights and liabilities are."*

[103] Does it make any difference that the company is a "one man company", the other shareholders being mere dummies or nominees? The answer given was a resounding "No". I go first to what Lord Herschell said at page 45:

"It was said that in the present case the six shareholders other than the appellant were mere dummies, his nominees, and held their shares in trust for him. I will assume that this was so. In my opinion, it makes no difference. The statute forbids the entry in the register of any trust; and it certainly contains no enactment that each of the seven persons subscribing the memorandum must be beneficially entitled to the share or shares for which he subscribes. The persons who subscribe the memorandum, or who have agreed to become members of the company and whose names are on the register, are alone regarded as, and in fact are, the shareholders ... Whether they are beneficial owners or bare trustees is a matter with which neither the company nor creditors have anything to do: it concerns only them and their *cestuis que trust* if they have any."

[104] Lord Macnaghten said this at page 53:

*"It has become the fashion to call companies of this class "one man companies." That is a taking nickname, but it does not help one much in the way of argument. If it is intended to convey the meaning that a company which is under the absolute control of one person is not a company legally incorporated, although the requirements of the Act of 1862 may have been complied with, it is inaccurate and misleading: if it merely means that there is a predominant partner possessing an overwhelming influence and entitled practically to the whole of the profits, there is nothing in that that I can see contrary to the true intention of the Act of 1862, or against public policy, or detrimental to the interests of creditors."*

[105] Finally, I go to what Lord Davey said at page 54:

"I do not see my way to holding that if there are seven registered members the association is not a company formed in compliance with the provisions of the Act and capable of carrying on business with limited liability, either because the bulk of the shares are held by some only, or even one of the members, and the others

are what is called “dummies,” holding, it may be, only one share of 1l. each, or because there are less than seven persons who are beneficially entitled to the shares.”

The result followed even though, as Lord Davey put it (at page 55) “any jury, if asked the question, would say the business was Aron Salomon’s and no one else’s.”

[106] The applications of the principle in *Salomon’s case* are legion. Two of the most striking, perhaps, and they might well have surprised Lord Davey’s jurymen, are to be found in the decisions of the Judicial Committee of the Privy Council in *Lee v Lee’s Air Farming Ltd* [1961] AC 12 and of the House of Lords in *Williams v Natural Life Health Foods Ltd* [1998] 1 WLR 830.

[107] In *Macaura v Northern Assurance Company Limited* [1925] AC 619 at page 626 Lord Buckmaster spelt out some of the implications of the principle of a company’s separate legal persona:

“no shareholder has any right to any item of property owned by the company, for he has no legal or equitable interest therein. He is entitled to a share in the profits while the company continues to carry on business and a share in the distribution of the surplus assets when the company is wound up.”

As Lord Wrenbury put it at page 633:

“the incorporator even if he holds all the shares is not the corporation, and ... neither he nor any creditor of the company has any property legal or equitable in the assets of the corporation.”

(Emphasis added.)

[5] Thus, it is trite law that a company is a separate legal entity and on incorporation, protects the owners and agents of the company by insulating them from the liabilities of the company. The insulative capability of the company is metaphorically called the veil (shield or mask) of incorporation. However, in certain limited and exceptional circumstances the veil may be (metaphorically) penetrated, lifted or pierced, with the consequence that the separate legal entity principle will not apply. It does not really matter which metaphor is used and the veil of incorporation is either “lifted”, “pierced” or “penetrated”. Ultimately, the lifting, piercing or penetrating of the veil, mask or shield results in a disregard of the separate legal entity principle. The

lifting of the corporate veil occurs only in exceptional circumstances where the courts will decline to uphold the separate entity principle, so that the shareholders (including perhaps directors, managers or agents) may be held personally responsible for the actions (or liabilities or debts) of the company. Once the veil of incorporation is lifted, the shareholders, directors or managers or agents cannot claim the protection of the separate company entity or the limited liability of a shareholder. It may thus be stated as a general proposition that lifting of the veil takes place where the courts are convinced that the company as a separate legal entity has been misused in some way; particularly by shareholders who have improperly used the company entity to shield themselves from potential third-party claims.

[6] Quite obviously the lifting of the corporate veil results in the emasculation of the *raison d'être* for the formation of a company, which is to shield the owner (shareholder) from liability incurred by the company. In light of *Salomon*, the courts are naturally and instinctively slow to lift the corporate veil, save in exceptional and well-defined circumstances.

### Malaysian company law

[7] The principle of separate legal entity or separate corporate personality of a company and its shareholders is the bedrock of Malaysian company law. In this regard, the then Federal Court of Malaysia endorsed *Salomon* in *Sunrise Sdn Bhd v First Profile (M) Sdn Bhd*,<sup>6</sup> holding that:

We are in complete agreement with the basic principle of the fundamental attribute of corporate personality, i.e. that the corporation is a legal entity distinct from its members, be they individuals or corporate bodies – a principle firmly established since *Aron Salomon v A Salomon & Co Ltd* [1897] AC 22.

However, since then, the development of the law has seen numerous deviations from the strict rule of the separate legal entity of the company through cases where the courts, on the particular facts and circumstances of those cases, found it appropriate and necessary to depart.

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6 [1997] 1 AMR 1 at 11; [1996] 3 MLJ 533 at 543.

Thus, in cases where there are signs of separate personalities of companies being used to enable persons to evade their contractual obligations or duties, the court would disregard the notional separateness of the companies.

[8] Thus, it is obvious enough that the lifting of the corporate veil and the imposition of liabilities against a holding company or the individual shareholder or the “controller” of the company inherently violates the sanctity of that principle of great antiquity. At any rate, it is correct to state that *Salomon* remains the foundation of company law in Malaysia. But it is imperative to note that the principle of lifting of the corporate veil does not of itself give rise to or confer a cause of action on the claimant. It cannot be used to impose liability on its own. The claimant who is seeking to lift the corporate veil must have an existing cause of action against the party that is trying to rely upon the concept of separate legal entity in order to avoid liability. Hence, there must be a pre-existing legal obligation giving rise to a cause of action in contract (or quasi-contract), tort, equity (or trust) or under statute.<sup>7</sup>

### Disregarding the separate legal entity

[9] The modern starting point when considering the circumstances in which it is permissible to lift the corporate veil is the salutary statement of principle by Lord Keith of Kinkel in *Woolfson v Strathclyde Regional Council* (“*Woolfson*”):<sup>8</sup>

it is appropriate to pierce the corporate veil only where special circumstances exist indicating that it is *a mere façade concealing the true facts*.

[10] The question sometimes arises whether in a group of companies, the holding company may be held liable for the debts or liability of the subsidiary. In law, the general position of holding companies and its subsidiaries is as stated in the case of *People’s Insurance Co (M) Sdn Bhd v People’s Insurance Co Ltd & Ors*<sup>9</sup> wherein it was held that:

The plaintiff company is a legal entity by itself. Although it is a subsidiary of the first defendant company, the plaintiff company maintains its own separate entity. In *Ebbw Vale Urban District Council*

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7 See *China Ocean Shipping Co v Mitsui Bussan Kaisha Ltd* [1995] 3 HKC 123.

8 1978 SC (HL) 90 at 96.

9 [1986] 1 MLJ 68 at 69.

*v South Wales Traffic Area Licensing Authority*, Cohen LJ said: Under the ordinary rules of law, a parent company and subsidiary company, even a 100 percent subsidiary company, are distinct legal entities ...

[11] It is trite therefore that the mere fact that a company is a subsidiary of the parent company cannot of itself be a ground to lift the corporate veil. The same principle applies to companies within a group. But the courts have in certain circumstances ignored the strict legal demarcation between these companies which are separate legal entities.

### ***DHN Food Distributors Ltd***

[12] In this regard, the argument that is not infrequently taken, especially when the subsidiary is insolvent or has no assets, is that the holding company and its subsidiary were conducting business as one unit or a single economic unit. Such an argument is plainly a reiteration of the “single economic unit” argument which was espoused by Lord Denning MR in *DHN Food Distributors Ltd v Tower Hamlets London Borough Council* (“DHN”).<sup>10</sup> It is pertinent to note that *DHN* was a case of “self-piercing” where the veil of incorporation was sought to be lifted in order that the companies within the group were treated (for the purposes of the claim for compensation) as one single economic entity. In that case, the companies within a group lodged claims for compensation for loss of business under a compulsory acquisition order and maintained that the group should be recognised as a single economic entity. This was a case of lifting of the veil of incorporation of a company so that the companies in the group would be able to receive compensation pursuant to the compulsory acquisition of property belonging to one of the companies in the group.

[13] Lord Denning MR said that the court should not ignore the reality of the corporate structure and the way the business was done. He said:

We all know that in many respects a group of companies are treated together for the purpose of general accounts, balance sheet, and profit and loss account. They are treated as one concern. Professor Gower in *Modern Company Law*, 3rd edn (1969), p 216 says:

“there is evidence of a general tendency to ignore the separate legal entities of various companies within a group, and to look instead at the economic entity of the whole group.”

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<sup>10</sup> [1976] 1 WLR 852 at 860, CA.

This is especially the case when a parent company owns all the shares of the subsidiaries – so much so that it can control every movement of the subsidiaries.

These subsidiaries are bound hand and foot to the parent company and must do just what the parent company says. A striking instance is the decision of the House of Lords in *Harold Holdsworth & Co (Wakefield) Ltd v Caddies* [1955] 1 WLR 352. So here. This group is virtually the same as a partnership in which all the three companies are partners. They should not be treated separately so as to be defeated on a technical point. They should not be deprived of the compensation which should justly be payable for disturbance. The three companies should, for present purposes, be treated as one, and the parent company DHN should be treated as that one. So DHN are entitled to claim compensation accordingly. It was not necessary for them to go through a conveyancing device to get it.”

### *Adams v Cape*

[14] However, it is significant to note that Lord Denning’s “single economic entity” approach in *DHN* was roundly rejected in the case of *Adams v Cape Industries plc (“Adams v Cape”)*.<sup>11</sup> In considering the relationship between a parent company and the subsidiary, Slade LJ stated that:<sup>12</sup>

There is no general principle that all companies in a group of companies are to be regarded as one. On the contrary, the fundamental principle is that “each company in a group of companies (a relatively modern concept) is a separate legal entity possessed of separate legal rights and liabilities.” *The Albazero* [1977] AC 774, 807, per Roskill LJ.

[15] He also said that:<sup>13</sup>

If a company chooses to arrange the affairs of its group in such a way that the business carried on in a particular foreign country is the business of its subsidiary and not its own, it is, in our judgment, entitled to do so. Neither in this class of case nor in any other class of case is it open to this court to disregard the principle of *Salomon v A Salomon & Co Ltd* [1897] AC 22 merely because it considers it just to do.

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11 [1990] Ch 433, CA.

12 *Ibid*, at p 532.

13 *Ibid*, at p 537.

[16] Slade LJ quoted Goff LJ in *Bank of Tokyo Ltd v Karoon* and said<sup>14</sup> that the relationship between members within a group of companies gives rise to economic and legal questions and that the court should confine itself to the law and not the economics of the relationship. According to Slade LJ, the court has no discretion to reject the distinction between members within a group of companies:

In the light of the set up and operations of the Cape group and of the relationship between Cape/Capasco and NAAC we see the attraction of the approach adopted by Lord Denning MR in the *DHN case* [1976] 1 WLR 852, 860c, which Mr Morison urged us to adopt: "This group is virtually the same as a partnership in which all the three companies are partners." In our judgment, however, *we have no discretion to reject the distinction between the members of the group as a technical point*. We agree with Scott J that the observations of Robert Goff LJ in *Bank of Tokyo Ltd v Karoon (Note)* [1987] AC 45, 64, are apposite:

"[Counsel] suggested beguilingly that it would be technical for us to distinguish between parent and subsidiary company in this context; economically, he said, they were one. *But we are concerned not with economics but with law. The distinction between the two is, in law, fundamental and cannot here be bridged.*"

(Emphasis added.)

[17] Slade LJ<sup>15</sup> quoted Lord Keith of Kinkel in *Woolfson* who unambiguously doubted the correctness of the approach that was taken by Lord Denning in *DHN*. He said:

Quite apart from cases where statute or contract permits a broad interpretation to be given to references to members of a group of companies, there is one well-recognised exception to the rule prohibiting the piercing of "the corporate veil." Lord Keith of Kinkel referred to this principle in *Woolfson v Strathclyde Regional Council* 1978 SLT 159 in the course of a speech with which Lord Wilberforce, Lord Fraser of Tullybelton and Lord Russell of Killowen agreed. With reference to the *DHN* decision [1976] 1 WLR 852, he said, at p 161:

"I have some doubts whether in this respect the Court of Appeal properly applied the principle that it is appropriate to pierce the corporate veil only where special circumstances exist indicating that it is a mere façade concealing the true facts."

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<sup>14</sup> Ibid, at p 538.

<sup>15</sup> Ibid, at p 539.

[18] Continuing, Slade LJ said<sup>16</sup> that there was nothing illegal in a company arranging its affairs and business in such a way that the liability should fall on one of its subsidiaries rather than another company within the group and that it was the companies' inherent right within the realm of company jurisprudence to structure its business in such a manner as to expose one company and insulate the rest of the companies in the group from liability:

... Whether or not such a course deserves moral approval, there was nothing illegal as such in Cape arranging its affairs (whether by the use of subsidiaries or otherwise) so as to attract the minimum publicity to its involvement in the sale of Cape asbestos in the United States.

As to condition (iii), we do not accept as a matter of law that the court is entitled to lift the corporate veil as against a defendant company which is the member of a corporate group merely because the corporate structure has been used so as to ensure that the legal liability (if any) in respect of particular future activities of the group (and correspondingly the risk of enforcement of that liability) will fall on another member of the group rather than the defendant company. Whether or not this is desirable, *the right to use a corporate structure in this manner is inherent in our corporate law ...*

(Emphasis added.)

### *Hotel Jayapuri*

[19] In the Malaysian context, the term "functional integrality" (which is in essence the "single economic unit" test) had on some occasions formed the basis for lifting the corporate veil. The term "functional integrality" and "unity of establishment" may well have been borrowed from the case of *Hotel Jaya Puri Berhad v National Union of Hotel, Bar & Restaurants Workers & Anor* ("Hotel Jayapuri").<sup>17</sup> In *Hotel Jayapuri*, the application in the High Court was in the nature of judicial review proceedings against the decision of the Industrial Court. In the Industrial Court, the parties were both the wholly-owned subsidiary and the parent company, i.e. the restaurant and the hotel. The area of law that the High Court dealt with was industrial jurisprudence

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<sup>16</sup> Ibid, at p 544.

<sup>17</sup> [1980] 1 MLJ 109.

in regard to a dispute arising under the Industrial Relations Act 1967 (Act 177) which is a statute which specifically enjoins the High Court not to have regard to a strict legal test. The factual evidence as related in the High Court judgment showed that the employees in question could have entered into the contracts of employment with the hotel itself (and not the restaurant), i.e. the parent. Ultimately in *Hotel Jayapuri*, the court held that there was functional integrality and unity of establishment between the hotel and the restaurant. In other words, functionally the hotel and the restaurant are in fact one integral whole and constitute one single unit. After quoting the passage from the 3rd edn of Gower's *Principles of Modern Company Law*, Salleh Abas FJ laid down the test in industrial relations law when he said the following:<sup>18</sup>

It is true that while the principle that a company is an entity separate from its shareholders and that a subsidiary and its parent or holding company are separate entities having separate existence is well established in company law, in recent years the court has, in a number of cases, by-passed this principle if not made an inroad into it. The court seems quite willing to lift "the veil of incorporation" (so the expression goes) when the justice of the case so demands.

Thus the facts of the case may well justify the court to hold that despite separate existence a subsidiary company is an agent of the parent company or vice versa as was decided in *Smith, Stone and Knight v Birmingham Corporation*; *Re FG (Films) Limited*; and *Firestone Tyre & Rubber Co v Llewelyn*. Professor Gower in his *Principles of Modern Company Law*, 3rd edition, page 213, said that the courts

"are coming to recognize the essential unity of a group enterprise rather than the separate legal entity of each company within the group. Other examples of this can be found.

In *The Roberta* (1937) 58 Ll LR 159, a parent company was held liable on a bill of lading signed on behalf of its wholly owned subsidiary, the court saying that the subsidiary was 'a separate entity ... in name alone and probably for the purposes of taxation'. In another case, *Spittle v Thames Grit & Aggregates Ltd* [1937] 4 All ER 101, the court found no difficulty in treating a subsidiary as 'to all intents and purposes' the same as the parent company which held 90 per cent of its shares. A licensing authority in

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18 Ibid, at p 112.

exercise of its discretion has been held entitled to have regard to the fact that a parent and subsidiary company, though technically separate legal persons, in fact constituted a single commercial unit (*Merchandise Transport Ltd v British Transport Commission* [1962] 2 QB 173, Devlin LJ at page 202) ... A good example of this is *Bird & Co v Thos Cook & Son* [1937] 2 All ER 227, in which an indorsement of a cheque to 'Thos. Cook & Son Ltd.' was treated as an indorsement to the allied but separate company of Thos. Cook & Son (Bankers) Ltd. by regarding it as a mere misdescription to be ignored under the principle *falsa demonstratio non nocet*."

It is clear therefore that the approach taken by the President of Industrial Court is not without any legal support when he placed an emphasis on the essential unity of group enterprise which in this case consists of the Hotel and the Restaurant, especially when Datuk NA Kularajah who is the Managing Director of the Hotel was also the Managing Director and later a Director of the Restaurant and had the ultimate authority over the employees. Thus, the practice of treating the employees of the Restaurant as being separate from the employees of the Hotel such as the Union having been told that they were so, their salaries, their EPF and SOCSO contributions being paid by the Restaurant, does not detract from the fact that the employees in question were in fact working in one group enterprise.

In my judgment, by giving recognition to this fact, the President did not cause any violence to the sanctity of the principle of separate entity established in *Salomon v Salomon & Co* but rather gave effect to the reality of the Hotel and the Restaurant as being in one enterprise. I find nothing unreasonable in the finding of the President by bypassing this principle. He did no more than to comply with the wishes of the Legislature that in the making of an award substantial merits of the case, the public interest and any matters which are necessary or expedient for the purpose of settling the dispute are among the factors which should be taken into consideration by the court. In my view, the finding by the President is in no way against the principle of separate entity and I am therefore not prepared to interfere with the award on this account.

### ***Law Kam Loy v Boltex Sdn Bhd***

[20] The decision in the case of *Adams v Cape* was adopted by the Malaysian Court of Appeal in the case of *Law Kam Loy v Boltex Sdn*

*Bhd* (“the *Boltex* case”)<sup>19</sup> in which Gopal Sri Ram JCA had repudiated the single economic unit theory by stating:

However, a careful look at the contemporary cases shows that, the view expressed by Salleh Abas FJ in the High Court and by Professor Gower no longer prevails. Indeed, the 7th edition of Gower’s work no longer canvasses the earlier opinion quoted by Salleh Abas FJ. But that is not to say that the court in the *Hotel Jayapuri* case was wrong in lifting the veil of incorporation on the facts of that case. The *Hotel Jayapuri* case was concerned with the Industrial Relations Act 1967 which requires the Industrial Court to disregard technicalities and to have regard to equity, good conscience and the substantial merits of a case. Accordingly, in industrial law, where the interests of justice so demand, it may, in particular cases be appropriate for the Industrial Court to pierce or to disregard the doctrine of corporate personality. That is what happened in the *Hotel Jayapuri* case and no criticism of that case on its facts may be justified.

[21] Gopal Sri Ram JCA then quoted Gower’s *Principles of Modern Company Law* (7th edition) to state the following:<sup>20</sup>

... Moreover the court declared that it did not accept that:

“as a matter of law the court is entitled to lift the corporate veil as against a defendant company which is the member of a corporate group, merely because the corporate structure has been used so as to ensure that the legal liability (if any) in respect of particular future activities of the group (and correspondingly the risk of enforcement of that liability) will fall on another member of the group rather than the defendant company. Whether or not this is desirable, the right to use a corporate structure in this manner is inherent in our corporate law ...”

[22] Hence, it is questionable whether *Hotel Jayapuri* can be relied upon as a binding and authoritative precedent beyond the peculiar fact pattern in that case. This is because of the reliance by Salleh Abas FJ in *Hotel Jayapuri* to that passage from the 3rd edn of Gower. In the *Boltex* case, the Court of Appeal referred to the 7th edn of Gower’s textbook and pointed out that the current authors of that eminent

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19 [2005] 4 AMR 525 at 530; [2005] 3 CLJ 355 at 360.

20 At p 531 (AMR); p 361 (CLJ).

text no longer hold that view in line with the decision of the Court of Appeal in *Adams v Cape*.

[23] As such, on that premise, it may be possible to argue that the “functional integrality” test in *Hotel Jayapuri* cannot be relied upon beyond the very limited area that it purported to cover. The ramifications of applying *Hotel Jayapuri* across the board would necessarily mean in effect that the doctrine of separate legal personality is cast obsolete. It is also crucial to observe that the functional integrality principle as espoused in the *Hotel Jayapuri* case is the same as that of the single economic test which in turn has been well and truly discarded by the Malaysian courts as seen in the *Boltex* case as well as by the English courts in the cases of *Wolfson* and *Adams v Cape*. But, it is imperative to note that the case was an industrial relations case and the pronouncement should be confined to the realm of industrial relations where statutes are given benevolent interpretations in order to achieve social justice so that the workmen are not adversely affected by strict interpretations of legislation and principles of law. *Hotel Jayapuri* itself recognises the need for this benevolent interpretation. In any event, it bears repeating that the principle of “functional integrality” as arrived at in the *Hotel Jayapuri* case was jettisoned by the Court of Appeal in the *Boltex* case. The justice of the case principle has also been firmly repudiated in the *Boltex* case.

### *Ben Hashem*

[24] The next case to be considered is *Ben Hashem v Al Shayif* (“*Ben Hashem*”).<sup>21</sup> That was a claim for ancillary relief in relation to a matrimonial dispute. In the course of the proceedings, the court was required to determine whether certain properties registered in the name of “shelf companies”, the shares of which companies were held in the name of the husband and the children, belonged in equity to the husband. In the course of his judgment, Munby J reviewed the authorities on piercing/lifting the corporate veil. According to Munby J, control, although an essential ingredient, is not of itself enough to warrant lifting the corporate veil. As Munby J recognised,<sup>22</sup> the starting point when considering the circumstances in which it is

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21 [2008] EWHC 2380 (Fam); [2008] Fam Law 1179; [2009] 1 FLR 115.

22 *Ibid*, at [151].

permissible to pierce the corporate veil is the statement of principle by Lord Keith of Kinkel in *Woolfsong* at page 96:

... it is appropriate to pierce the corporate veil only where special circumstances exist indicating that it is a mere façade concealing the true facts.

[25] That statement, as Munby J noted, was treated by the Court of Appeal in *Adams v Cape*<sup>23</sup> as stating a “well-recognised exception” to the rule prohibiting the piercing of the corporate veil.

[26] Having reviewed the authorities,<sup>24</sup> Munby J extracted the following principles to be applied in determining whether the corporate veil should be lifted/pierced:

- Ownership and control of a company are not of themselves sufficient to justify piercing the veil;
- The court cannot pierce the corporate veil, even where there is no unconnected third party involved, merely because it is thought to be necessary in the interests of justice;
- The corporate veil can be pierced only if there is some “impropriety”;
- The court cannot, on the other hand, pierce the corporate veil merely because the company is involved in some impropriety. The impropriety must be linked to the use of the company structure to avoid or conceal liability;

As Sir Andrew Morritt VC said in *Trustor* at para [22]:

“Companies are often involved in improprieties. Indeed there was some suggestion to that effect in (*Salomon*). But it would make undue inroads into the principle of *Salomon’s* case if an impropriety not linked to the use of the company structure to avoid or conceal liability for that impropriety was enough.”

- If the court is to pierce the veil, it is necessary to show both control of the company by the wrongdoer(s) and impropriety,

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23 [1990] Ch 433 at 539.

24 [2008] EWHC 2380 (Fam); [2008] Fam Law 1179; [2009] 1 FLR 115 at [159]-[164].

that is, (mis)use of the company structure by them as a device or façade to conceal their wrongdoing;

As the Vice Chancellor said in *Trustor* at para [23]:

“the court is entitled to ‘pierce the corporate veil’ and recognise the receipt of the company as that of the individual(s) in control of it if the company was used as a device or façade to conceal the true facts thereby avoiding or concealing any liability of those individual(s).”

- A company can be a façade even though it was not originally incorporated with any deceptive intent. The question is whether it is being used as a façade at the time of the relevant transaction(s); and
- The court will pierce the veil only so far as is necessary to provide a remedy for the particular wrong which those controlling the company have done. In other words, the fact that the court pierces the veil for one purpose does not mean that it will necessarily be pierced for all purposes.

### *Ord v Bellhaven Pubs Ltd*

[27] Munby J also referred to *Ord v Bellhaven Pubs Ltd*.<sup>25</sup> In that case Mr and Mrs Ord (“the Ords”) took a lease of a pub from Bellhaven Pubs Ltd (“Bellhaven”).

[28] The Ords commenced proceedings for misrepresentation concerning the turnover and profitability of the pub. Bellhaven counterclaimed for unpaid rent. Upon discovering that Bellhaven no longer had substantial assets, the Ords sought to join Bellhaven’s parent company to the action. The application failed as there was *no evidence of any concealed impropriety in the reorganisation of the group’s affairs*. In this case, Balcombe LJ said the following:<sup>26</sup>

If there had been any substance in the allegations that there had been some impropriety in the handling of the group restructuring, insolvency law (and in particular I have in mind section 423 of the Insolvency Act 1986) makes adequate provision for dealing with that eventuality.

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25 [1998] 2 BCLC 447.

26 *Ibid*, at p 458.

[29] It can be readily appreciated from the aforesaid case laws that lifting of the corporate veil will only be available in exceptional circumstances, and almost certainly not where there exists statutory provisions or common law principles designed or developed to provide a remedy for the real wrong that has been done. In the present context, it is imperative to consider some of the more recent decisions in the English courts regarding the doctrine of the lifting of the veil of incorporation as the principles that have been developed, refined, restated and elucidated in these cases.

[30] A perusal of judicial authorities from other Commonwealth jurisdictions regarding the doctrine of lifting the corporate veil clearly indicates that the principles upon which the courts are guided are largely similar to that in the English cases which have been set out above.

### Hong Kong

[31] The strict approach adopted by the courts in England and Wales is similarly espoused by the courts in Hong Kong. In *China Ocean Shipping Co v Mitsui Bussan Kaisha Ltd*,<sup>27</sup> the owners of a vessel were unable to obtain satisfaction of an arbitral award from the Panamanian charterer and sought to have the corporate veil of the charterer lifted. The owners of the vessel alleged that the charterer was a façade for a Hong Kong company so as to enable the Hong Kong company to evade its legal obligations to the owners. Bokhary JA (with whom the other members of the court agreed) held:<sup>28</sup>

Using a corporate structure to *evade* legal obligations is objectionable. The courts' power to lift the corporate veil may be exercised to overcome such evasion so as to preserve legal obligations. But using a corporate structure to *avoid* the incurring of any legal obligation in the first place is not objectionable. *And the courts' power to lift the corporate veil does not exist for the purpose of reversing such avoidance so as to create legal obligations.*

(Emphasis added.)

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27 [1995] 3 HKC 123.

28 Ibid, at p 127.

[32] Bokhary JA's findings are particularly insightful. He said this:

In the present case, there was no evasion of any obligation or liability by the defendants. There was no liability or obligation on the defendants' part to evade. No liability or obligation on anybody's part existed until the charterparties were entered into. And it was Martrans Panama who entered onto the charterparties and who assumed liabilities or obligations to the plaintiffs thereunder. The plaintiffs chose to deal with Mitrans Panama without insisting on a guarantee.

[33] Nazareth VP in turn rejected the interests of justice argument for lifting the corporate veil and cited with approval an extract from Gower's *Principles of Modern Company Law* (5th edn) in which it was, *inter alia*, stated<sup>29</sup> that "The court cannot lift the veil merely because it considers that justice so requires".

[34] In *Horace Yao Yee Cheong v Pearl Oriental Innovation Ltd* ("*Pearl Oriental*"),<sup>30</sup> the court was concerned with whether the corporate veil should be lifted so as to make the defendant company (Pearl Oriental) liable to the plaintiffs in sums for which another company (DHL) had been adjudged liable. In his judgment,<sup>31</sup> Suffiad J, at first instance, set out the basis upon which the plaintiffs alleged that the corporate veil should be pierced. He said:

The plaintiffs' claim in this case is that it would be just for the court to lift the corporate veil between DHL and the defendant on the basis that during the time when DHL was a wholly owned subsidiary of the defendant, the defendant had by improper means stripped DHL of its valuable assets with a view to evading the liabilities owed by DHL to its creditors including the plaintiffs, which liabilities were already in existence before the Scheme of Arrangement was effected.

[35] Suffiad J found that in order to pierce the corporate veil "there must be some impropriety, wrongdoing, concealment, sham or fraud involved".<sup>32</sup> The judge found that there had been such conduct, that

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29 *Ibid*, at p 133.

30 [2009] HKCFI 2137.

31 *Ibid*, at [19].

32 *Horace Yao Yee Cheong v Pearl Oriental Innovation Ltd* [2009] HKCFI 2137 at [114].

Pearl Oriental had sought to evade the existing liabilities of DHL by stripping DHL of its assets to other companies within the group, thereby putting them out of reach of DHL's creditors.<sup>33</sup>

***Pearl Oriental (Hong Kong Court of Appeal)***

[36] The Court of Appeal<sup>34</sup> took a different view. The judgment of the court was given by Rogers VP.

[37] He said:<sup>35</sup>

For the reasons already indicated, I consider that the plaintiffs' case has not been made out on the facts. But even if it could be shown that the defendant had stripped the assets of DHL to detriment of DHL's creditors that would not, in my view, give rise to the plaintiffs being able to gain judgment against the defendant.

[38] He continued:<sup>36</sup>

34. The fact that the defendant had "stripped" DHL of its assets and had acted improperly does not, of itself, give rise to a cause of action that may be brought by the plaintiffs. The wrongs, if they be wrongs, were done to DHL.

...

37. When taxed as to what was the façade or sham in this case Mr Neoh was hard pushed to settle on anything that could said to have been a sham. In the end, one can only consider what the judge said, namely, that the defendant had to be treated as the same entity as DHL. If that be the case then DHL itself would have been the sham or façade. That, on the plaintiffs' case, it clearly was not. On the plaintiffs' case it was the party wronged.

[39] The Court of Appeal's approach to lifting the corporate veil, in cases of alleged "asset stripping", is instructive. Rogers VP said:

38. It has to be observed that *lifting or piercing the corporate veil does not give rise to a cause of action in itself. It is a relief or remedy which can*

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33 Ibid, at [95] and [123].

34 [2010] HKCA 101; CACV146/2009 (April 13, 2010).

35 Ibid, at [38].

36 Ibid, at [39].

*be granted when there is an underlying cause of action. It is, therefore, important to determine what the underlying cause of action is.*

39. In the second place the device of lifting the corporate veil has been said to be a blunt instrument. Whatever a blunt instrument might mean in the context, I consider it more appropriate to regard the device of lifting the corporate veil as arbitrary. It is something that must be carefully applied and, in the context of circumstances said to warrant it in this case, *it must be clearly established that the whatever liabilities were incurred the party said to be liable to discharge those liabilities on the basis of lifting the veil had used the party nominally incurring the liability as a façade. That was not the case here.*

(Emphasis added.)

[40] In *Winland Enterprises Group Inc v Wex Pharmaceuticals Inc & Anor*,<sup>37</sup> the principles on which the corporate veil will be pierced were summarised by To J. He stated that:

In summary, the court will lift the corporate veil of a company if it is a façade or a puppet of the parent company used to perpetrate fraud or evade legal obligation and liability. Fraud and concealment which may have such effect are valid grounds for lifting the corporate veil. That a company is a façade or a puppet of its parent company by itself is neither here nor there. It is just some evidence from which the inference of illegitimate purpose may be drawn or on which to support a finding of the illegitimate purpose behind the façade. Unless the use of a corporate veil for such illegitimate purpose is proved, the use of a façade or that a company is a puppet of its parent company without more does not justify lifting of the corporate veil.

## Singapore

[41] In *Thode Gerd Walter v Mintwell Industry Pte Ltd*,<sup>38</sup> the facts were as follows. The first defendant (Mintwell) was the owner of certain leasehold property. It mortgaged its interest in the property and covenanted, amongst other things, not to let any part of the property without the consent in writing of the mortgagee bank. Mintwell fell into arrears with its mortgage repayments and the mortgagee bank (or its successor) (“the mortgagee bank”) obtained judgment in default

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37 [2012] 5 HKC 494.

38 [2009] SGHC 44.

of appearance against Mintwell. Subsequently, the mortgagee bank obtained an order for possession of the property, but did not seek immediately to enforce the order. In the interim, Mintwell granted to the plaintiff a tenancy of one of the vacant units on the property.

[42] Subsequently, the mortgagee bank enforced the order for possession and a notice of eviction was served on the plaintiff. The plaintiff claimed damages for breach of contract, misrepresentation and breach of duty against Mintwell, and against the second and third defendants, claiming that the court should hold them personally liable for Mintwell's breaches by lifting the corporate veil on the ground that the interests of justice so required. The second defendant was alleged to be the person who controlled Mintwell, being, allegedly, the main decision-maker and the person who negotiated and/or concluded the transactions with its bankers and tenants. He was also, allegedly, the person in accordance with whose directions the management of Mintwell was accustomed to act. Similarly, the third defendant was a director of Mintwell. He was authorised to act and did negotiate and/or conclude transactions on behalf of Mintwell. It was said that he too was a person in accordance with whose directions the management of Mintwell was accustomed to act. Mintwell admitted liability for breach of the tenancy agreements and a consent judgment was entered against it on the first day of trial. As to the other two defendants, the court found that there was, on the evidence, no basis for the corporate veil to be lifted.

[43] Whilst recognising that the courts have on occasions looked behind the legal personality of a company to the real controllers, the judge found that the courts do not disregard the corporate personality of a limited company save in exceptional circumstances. There was no suggestion that Mintwell was in some way used to create a sham or façade. The plaintiff had accepted that Mintwell was a genuine company, at one time involved in a manufacturing and assembly business, and the plaintiff had been Mintwell's tenant for over a year.

### **Australia**

[44] In *Commissioner for Fair Trading v TLC Consulting Services Pty Ltd & Ors*,<sup>39</sup> the case was concerned with whether an individual respondent

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39 [2011] QSC 233.

who had been enjoined from performing certain introduction services was guilty of contempt of court by being involved in a company which thereafter performed those introduction services. Philippides J, having reviewed the authorities, including English authorities, on piercing the corporate veil concluded that:<sup>40</sup>

I am satisfied to the requisite standard on the material before the court that the sole purpose of the company Love Network Qld Pty Ltd was to conceal the respondent's engagement in the conduct which was proscribed by the Order and to evade the legal obligations stemming from the Order. I conclude that the incorporation and the conduct of the business by the company Love Network Qld Pty Ltd was a sham or device used by the respondent to avoid the obligations of the Order.

### **Full control by the parent company**

[45] The next point to be considered is whether the fact that the parent company had full control of its wholly-owned subsidiary, through provision of funds, premises and personnel, and through legal structures put in place whereby ultimate control resided in the parent company. The issue of control is fairly important because it is quite common for plaintiffs to seek the lifting of the corporate veil on the basis that the targeted individual or corporation (holding company) "controlled" the company whose corporate veil is to be lifted or pierced. And so the question is whether "control" per se is sufficient to lift the corporate veil. In this regard, a finding that there was full control in and of itself cannot form the basis of the veil of incorporation being lifted. Pursuant to principles propounded by the case of *Ben Hashem* as discussed above, the corporate veil can be pierced only if control is coupled with some impropriety. The following cases are instructive on this point.

[46] In *Trustor AB v Smallbone (No. 2)*,<sup>41</sup> Sir Andrew Morritt VC held that:

Companies are often involved in improprieties. Indeed there was some suggestion to that effect in (*Salomon*). But it would make undue inroads into the principle of *Salomon's* case if an impropriety

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40 *Ibid*, at [56].

41 [2001] 1 WLR 1177.

not linked to the use of the company structure to avoid or conceal liability for that impropriety was enough.

[47] In *Linsen International v Humpuss Sea Transport & Ors*,<sup>42</sup> Flaux J was concerned with the issue as to whether to continue a freezing order made by HHJ Mackie QC. HHJ Mackie QC had granted the freezing injunction on the basis that the corporate veil within the Humpuss group could be pierced, so as to render the third to thirteenth defendants liable under the original charterparties and guarantees concluded with the first and second defendants respectively.<sup>43</sup> Flaux J cited with approval the review of authorities which Munby J had undertaken in *Ben Hashem*, and referred to the decision of Burton J in *Antonio Gramsci Shipping v Stepanovs*<sup>44</sup> where, at paragraph 15, Burton J had said:

The only apparent limitation that has been placed on the doctrine, given the necessary requirement that the trigger for it is not simply fraudulent dealing by a company but the fraudulent misuse of the company structure, as Morritt VC made clear, is that, using the gallicised words of Munby J in *Ben Hashem* at 199 (referred to by Flaux J in *Lindsay v O'Laughlaine* [2010] EWHC 529 QB at 134) the wrong-doing must not be “dehors the company”, i.e. something outside the ordinary business of the company. Whether the phrase “dehors the company” is ever a very helpful or meaningful expression, I do not know, but consideration of it is clearly inappropriate on the facts of this case, when the Corporate Defendants had, on the Claimants’ case, no independent or non-fraudulent existence. The fraud was plainly “dedans” the company, but that was because the company was set up for that very purpose, in order to abuse the company’s structure.

[48] Flaux J continued:

It seems to me, on reflection that, at least in a case (of which *Gramsci* was an egregious example) where the whole purpose of the corporate structure is to perpetrate fraud, it cannot be correct that the ability to pierce the corporate veil is limited by the need that the wrongdoing is dehors the company. However the point does not matter in the present case since, on analysis, the relevant wrongdoing here (for reasons I

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42 [2011] EWHC (Comm) 2339.

43 *Ibid*, at [14].

44 [2012] 1 BCLC 561.

will come to) was the transfer of assets from the first defendant to the third defendant with a view to frustrating enforcement against the first defendant. Thus the relevant wrongdoing was dehors the companies in respect of which the claimants seek to pierce the corporate veil.

... The claimant who wishes to pierce the corporate veil must show not only control but also impropriety, in the sense of misuse of the company or the corporate structure to conceal wrongdoing.

[49] Flaux J concluded on this issue:<sup>45</sup>

Clearly the basis of that reasoning (in *Gramsci*) was that the contract (the charterparty) was in reality one made by the puppeteer using the puppet to disguise the fact that the contract was part of a fraud being perpetrated on the claimants. The critical difference in the present case is that, as I have already held above, there was nothing untoward about either the charterparties or the guarantees when they were made. The charterparties were all genuine contracts made with the first defendant, performance by which was guaranteed by the second defendant. There was and is no basis for piercing the corporate veil at the time the contracts were made. Nothing in *Gramsci* is dealing with such a case and there is nothing in Burton J's reasoning to support the claimants' proposition that abuse of the corporate structure, long after the relevant contracts were made, can lead to the corporate veil being pierced to make companies in the group or Mr Tommy Suharto liable as if they had been or had become parties to those charterparties and guarantees.

### *Epic Quest*

[50] The case of *Epic Quest Sdn Bhd & Anor v Sheila Eleanor De Costa (suing under the name and style of De Costa & Co)*<sup>46</sup> decided by the Malaysian Court of Appeal is interesting. The veil of incorporation was lifted, apparently because the companies had disregarded the separate legal entity status of each of the companies within the group. Thus, instructions were given by company A for a matter involving company B. Similarly, payment of legal charges were paid by company A for legal work done for company B. In that case, Sheila, a lawyer exercised a lien over documents that belonged to her clients,

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45 Ibid, at [141]-[142].

46 [2011] 8 CLJ 517.

Epic Quest. Epic Quest was part of the Titijaya Group of companies and Sheila had rendered services to the group, in particular Titijaya (M) Sdn Bhd, Prestine Valley Sdn Bhd and Titijaya Hotel Sdn Bhd. There were unpaid bills in respect of the three companies and Sheila proceeded to obtain judgment against the three companies. She then exercised her lien over the documents of Epic Quest on which she did not have a judgment. The court held that it was not open to the courts to disregard the corporate veil purely on the ground that it was in the interest of justice to do so. Something more must be shown such as special circumstances which would include cases where there was either actual fraud at common law or some inequitable or unconscionable conduct amounting to fraud in equity.

[51] Based on the evidence, the court held that the plaintiff had laid sufficient evidential foundation to support the contention that special circumstances had existed for lifting the corporate veil of the appellant and the three companies within the Titijaya Group of companies. The Court of Appeal held that having themselves ignored the fact that they operated as one group enterprise when dealing with the respondent, the appellant could not be allowed to insist on their separate corporate personality to defeat the respondent's general lien whereby it would be inequitable or unconscionable to do so. The Court of Appeal opined that the corporate veil could not be used as an instrument to evade a contractual obligation. According to the Court of Appeal, unconscionable or inequitable conduct amounts to fraud in equity. In that case, the evidential trail revealed that the deponents of all affidavits were filed by one Bay Nut Soo as the "Setiausaha Syarikat Titijaya Group of companies". It also revealed that one SP Lim was a director of almost every one of them or through companies controlled by him or by close family of business associates. Further, instructions from one company came from another. Letterheads by Titijaya were used in respect of bills issued to Epic Quest. There was also a letter from Titijaya (M) Sdn Bhd stating that Titijaya had made payment for bills issued to Logic Marine.

[52] According to the evidence, the payment of legal charges for Sheila was being made by the group of companies. It was in that context that the Court of Appeal held that:

[9] From what is set out above it was evident to us that when dealing with the respondent, the Titijaya Group of Companies including the appellants and SP Lim had deliberately ignored the separate corporate

personalities of the companies, and operated as one group enterprise. The payment of the respondent's legal charges also reflected this where it can be seen that when the respondent rendered her charges to a company within the group, the respondent's charges would be paid by any one of the Titijaya Group of Companies even though the paying company did not directly receive the respondent's services. Having themselves ignored it when dealing with her, the appellants cannot now be allowed to insist on their separate corporate personality to defeat the respondent's general lien. In *Sunrise Sdn Bhd v First Profile (M) Sdn Bhd & Anor* [1997] 1 CLJ 529 Chong Siew Fai (CJ Sabah & Sarawak) said that the corporate veil cannot be used as an instrument to evade a contractual obligation.

[53] The Court of Appeal determined that having themselves ignored it when dealing with the respondent, the appellants could not be allowed to insist on their separate corporate personality to defeat the lien placed by the respondent on their documents. The basis upon which the Court of Appeal justified the lifting of the corporate veil is redolent of the single economic unit theory which was in the *DHN* case. But as explained earlier, this theory had been somewhat repudiated via the *Boltex* case.

[54] It remains to be seen whether the commingling of activities or functions per se between separate legal entities within a group of companies such as the use of common staff, letterheads, emails, facsimiles or payments for services rendered (sans any allegation of fraud, deception, evasion or concealment) can be a standalone ground for the lifting of the corporate veil, i.e. on the basis of the single economic unit (*DHN*) theory.

#### **VTB**

[55] In *VTB*, the issue of lifting of the corporate veil arose in this way. In that case, the plaintiff (*VTB*) had sought to make two companies and one individual ("the new defendants") jointly liable, with the existing defendant, a Russian entity known as *RAP*, on a contract to which the new defendants were not parties. The basis for the claim was that contrary to a dishonest representation that was made, *RAP* was in fact controlled by the new defendants which had used *RAP* as the vehicle to enter into the agreements. This involved the fraudulent use of the company structure of *RAP* which was employed as a façade to conceal the wrongdoing of the new defendants. Accordingly, *VTB*

asserted that the court should pierce the corporate veil, and that the new defendants would also be liable as original contracting parties. The Court of Appeal<sup>47</sup> found that:

- The starting point is *Salomon*,<sup>48</sup>
- *Woolfson* and *Adams v Cape* make it plain that there is only one special case for justifying the court looking behind a company's corporate façade, and that is where the company is a mere façade concealing the true facts;<sup>49</sup>
- The real issue for the court in *VTB* was as to the consequences of a judicial determination that the veil of incorporation ought to be pierced;<sup>50</sup>
- The principles set out by Munby J in *Ben Hashem* as to the circumstances in which the court would pierce the corporate veil were correct;<sup>51</sup> and
- When circumstances exist for the corporate veil to be pierced the applicant does not need to establish that it is *necessary* to do so in order to provide the claimant with an effective remedy.<sup>52</sup>

[56] The court refused to find that the effect of piercing the corporate veil would be that the new defendants would also be liable as original contracting parties.<sup>53</sup>

### **VTB (Supreme Court)**

[57] In *VTB*,<sup>54</sup> there were two issues before the Supreme Court:

1. Whether permission granted *ex parte* to VTB to serve proceedings out of the jurisdiction, on the basis of alleged torts of deceit and conspiracy, should be set aside; and

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47 [2012] 2 BCLC 437; [2012] EWCA Civ 80.

48 *Ibid.*, at [47].

49 *Ibid.*, at [48]–[49].

50 *Ibid.*, at [51].

51 *Ibid.*, at [79].

52 *Ibid.*, at [82].

53 *Ibid.*, at [96].

54 [2013] UKSC 5; [2013] 1 All ER 1296; [2013] BCC 514; [2013] 1 CLC 153; [2013] 1 Lloyd's Rep 466; [2013] 2 AC 337; [2013] 1 BCLC 179; [2013] 1 All ER (Comm) 1009; [2013] 2 WLR 398.

2. Whether VTB should be allowed to raise an additional claim, by way of amendment, based on piercing the corporate veil.

[58] As to the first issue:

- Both the judge at first instance and the Court of Appeal answered that issue in the affirmative;<sup>55</sup>
- Lords Mance,<sup>56</sup> Neuberger,<sup>57</sup> and Wilson<sup>58</sup> dismissed the appeal; and
- Lords Clarke<sup>59</sup> and Reed<sup>60</sup> disagreed.

[59] As to the second issue, the Supreme Court unanimously upheld the decision of the Court of Appeal.<sup>61</sup> Lord Neuberger, President of the Supreme Court, gave the only substantive speech. He said:<sup>62</sup>

In answer to the contention that the approach of the courts to the issue of piercing the veil is unprincipled, there is real force, at least on the face of it, in the fact that it cannot be invoked merely where there has been impropriety. As Munby J put it in (*Hashem*), paras 163-164, “it is necessary to show both control of the company by the wrongdoer(s) and impropriety, that is, (mis)use of the company by them as a device or façade to conceal their wrongdoing ... at the time of the relevant transaction(s)”.

[60] Lord Neuberger found it unnecessary and inappropriate to resolve the issue of whether the Supreme Court, in that case, should decide that, unless any statute relied on in the particular case expressly or impliedly provides otherwise, the court cannot pierce the veil of incorporation, because he was persuaded that VTB could not succeed on the pleaded facts even if proven at trial.<sup>63</sup>

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55 Ibid, at [76].

56 Ibid, at [71].

57 Ibid, at [113].

58 Ibid, at [151].

59 Ibid, at [236].

60 Ibid, at [240].

61 Ibid, at [72]; [148]; [158]; [238]; and [243].

62 Ibid, at [128].

63 Ibid, at [130] and [148].

### *Prest*

[61] In *Prest*, the dispute arose out of matrimonial proceedings. Mr Prest wholly owned and controlled (directly or indirectly, through intermediate entities) a number of non-UK resident companies which, between them, owned seven residential properties in the UK. The issue was whether Mr Prest was the beneficial owner of a vast number of assets that were legally owned by the companies which he owned and controlled. The matrimonial home was also legally owned by one of the companies. Mr Prest declared that he was not of financial means. He and the companies failed to make full disclosure and give details as to the funding and other particulars of and concerning these assets. The first instance judge<sup>64</sup> found that two properties belonged to two companies, which were owned and controlled effectively by the husband.

[62] The question was whether the properties were nevertheless properties to which the husband was “entitled, either in possession or reversion” within the meaning of section 24(1) of the Matrimonial Causes Act 1973. If they were, the court was able to make orders in relation to those properties for the benefit of the wife.<sup>65</sup> He found that unless and until that issue was answered unambiguously affirmatively, “the ordinary principle ... that the shareholders of a company (including shareholder with 100% control) have no interest in the company’s assets” applies. At first instance, the judge had acquitted the husband of any impropriety as he found:

- (a) The company structure had been set up and used for conventional reasons including wealth protection and tax avoidance;
- (b) The company was effectively being used as the husband’s money box which he used at will; and
- (c) Whilst that might have been contrary to accounting or company law, it did not mean that the structure was being used to avoid or conceal liability.

[63] Having found an absence of “relevant” impropriety, the judge at first instance nevertheless found that the husband was entitled to

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64 [2011] EWHC 2956.

65 *Ibid*, at [81].

the relevant properties within the meaning of section 24(1)(a) of the Matrimonial Causes Act 1973.

[64] However, the Court of Appeal held that:<sup>66</sup>

... once the Judge had rejected the submission that he could pierce the corporate veils of the companies in the Petrodel group, he had no choice but to find that assets of PRL and Vermont, including the London properties the subject of the appeals, belonged beneficially to PRL and/or Vermont respectively, and that none of such assets belonged beneficially to the husband.

[65] In the course of his judgment in the Court of Appeal, Rimer LJ referred to *Salomon*, and stated that it has long been recognised that there may be circumstances in which it will be legitimate for the court to pierce the corporate veil of a company. In regards to the Court of Appeal decision in *VTB*, Rimer LJ stated that:<sup>67</sup>

... the importance of the judgment in *VTB* is that it recognised and affirmed the strict limitations identified in prior authority as to the only factual circumstances in which it will be open to the court to “pierce the veil”.

[66] In rejecting the alleged “interests of justice” exception to the *Salomon* principle, the Court of Appeal expressly affirmed that:<sup>68</sup>

... *the court cannot disregard the Salomon case “merely because it considers that justice so requires.”* The husband and his company are separate legal persons and each owns his and its separate assets. Those differences must be respected and cannot be ignored merely because it is perceived as convenient to do so. *A condition of the accepted basis for a piercing of the corporate veil is that the controller of the company has misused the fact of its separate corporate identity for the purpose of hiding facts or concealing wrongdoing.*

*The rationale is that a wrongdoer cannot benefit from his dishonest misuse of a corporate structure for improper purposes.*

(Emphasis added.)

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66 [2013] 2 WLR 557 at 582, [97].

67 *Ibid*, at p 591, [123].

68 *Ibid*, at p 595, [132].

[67] This demonstrates that piercing of the corporate veil will only be available in exceptional circumstances, and almost certainly not where there exists statutory provisions or common law principles designed or developed to provide a remedy for the real wrong that has been done. In rejecting the alleged “interests of justice” exception to the *Salomon* principle, the Court of Appeal expressly affirmed<sup>69</sup> the *obiter dicta* in *Woolfson*, which *dicta* had been expressly adopted, as part of the *ratio decidendi*, in *Adams v Cape*, and the first three principles identified by Munby J in *Ben Hashem*, which the Court of Appeal in *VTB* had accepted as correct, as the preconditions for piercing the corporate veil.

[68] The Court of Appeal held that there was no jurisdiction under section 24 of the Matrimonial Causes Act 1973 to treat the assets of the parties as available for distribution to the wife. Thus, Mr Prest and his companies won in the Court of Appeal. In the Supreme Court, the critical question was whether it could order the properties to be transferred to the wife as part of the financial settlement on divorce, given that they legally belonged to the companies and not Mr Prest. The Supreme Court held that on the particular facts of this case, the UK residential properties held by the offshore companies were held on bare trust for the husband. The properties were beneficially owned by the husband and so an order could be made for the transfer of the properties to the wife. The Supreme Court held that the court can only “lift the corporate veil” – that is, disregard the separate legal personality of a company – if there is some impropriety. This will be the case where a person is under an existing legal obligation or liability, or subject to an existing legal restriction, which he deliberately evades, or whose enforcement he deliberately frustrates by interposing a company which is under his control. In this case, the available evidence was “incomplete and in critical respects obscure”. The husband and the relevant companies persistently failed to cooperate with the proceedings or comply with orders to produce documents.

[69] The Supreme Court, therefore, had to consider “what presumptions may properly be made against the husband given that the defective character of the material is almost entirely due to his persistent obstruction and mendacity”. The court inferred from the husband’s conduct that he was covering up evidence that would

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69 Ibid, at pp 594-594, [131].

reveal that the properties were indeed held beneficially for him. According to the Supreme Court, this demonstrates the importance of full disclosure to avoid a court making adverse inferences.

[70] The Supreme Court unanimously overturned the Court of Appeal and held that Mr Prest beneficially owned the assets of the Petrodel Resources Ltd companies under a resulting trust because he contributed to their purchase price. There was accordingly no need to lift the corporate veil, which could only be done in limited situations. However, because Mr Prest had been “entitled” to the assets of his companies under a resulting trust, under section 24 of the Matrimonial Causes Act 1973, the court had jurisdiction to transfer half the value of the properties to Mrs Prest. Lord Sumption gave the first judgment. He said there was only a limited power to lift the corporate veil, namely when people were under an existing legal obligation which is deliberately evaded. According to the Supreme Court, a corporate veil could be lifted only for the purpose of depriving the company or its controller of the advantage they would otherwise obtain from the company’s separate legal personality. There had been no evidence that Mr Prest had set up the companies to avoid any obligations in these divorce proceedings, so there was no ground for lifting the corporate veil. The following passages from Lord Sumption’s erudite judgment are instructive and illuminating:

[16] I should first of all draw attention to the limited sense in which this issue arises at all. “Piercing the corporate veil” is an expression rather indiscriminately used to describe a number of different things. Properly speaking, it means disregarding the separate personality of the company. There is a range of situations in which the law attributes the acts or property of a company to those who control it, without disregarding its separate legal personality. The controller may be personally liable, generally in addition to the company, for something that he has done as its agent or as a joint actor. Property legally vested in a company may belong beneficially to the controller, if the arrangements in relation to the property are such as to make the company its controller’s nominee or trustee for that purpose. For specific statutory purposes, a company’s legal responsibility may be engaged by the acts or business of an associated company. Examples are the provisions of the Companies Acts governing group accounts or the rules governing infringements of competition law by “firms”, which may include groups of companies conducting the relevant business as an economic unit. Equitable remedies, such as

an injunction or specific performance may be available to compel the controller whose personal legal responsibility is engaged to exercise his control in a particular way. But when we speak of piercing the corporate veil, we are not (or should not be) speaking of any of these situations, but only of those cases which are true exceptions to the rule in *Salomon v A Salomon & Co Ltd* [1897] AC 22, i.e. where a person who owns and controls a company is said in certain circumstances to be identified with it in law by virtue of that ownership and control.

[17] Most advanced legal systems recognise corporate legal personality while acknowledging some limits to its logical implications. In civil law jurisdictions, the juridical basis of the exceptions is generally the concept of abuse of rights, to which the International Court of Justice was referring in *In re Barcelona Traction, Light and Power Co Ltd* [1970] ICJ Rep 3 when it derived from municipal law a limited principle permitting the piercing of the corporate veil in cases of misuse, fraud, malfeasance or evasion of legal obligations. These examples illustrate the breadth, at least as a matter of legal theory, of the concept of abuse of rights, which extends not just to the illegal and improper invocation of a right but to its use for some purpose collateral to that for which it exists.

[18] English law has no general doctrine of this kind. But it has a variety of specific principles which achieve the same result in some cases. One of these principles is that the law defines the incidents of most legal relationships between persons (natural or artificial) on the fundamental assumption that their dealings are honest. The same legal incidents will not necessarily apply if they are not. The principle was stated in its most absolute form by Denning LJ in a famous dictum in *Lazarus Estates Ltd v Beasley* [1956] 1 QB 702, 712:

“No court in this land will allow a person to keep an advantage which he has obtained by fraud. No judgment of a court, no order of a Minister, can be allowed to stand if it has been obtained by fraud. Fraud unravels everything. The court is careful not to find fraud unless it is distinctly pleaded and proved; but once it is proved, it vitiates judgments, contracts and all transactions whatsoever ...”

The principle is mainly familiar in the context of contracts and other consensual arrangements, in which the effect of fraud is to vitiate consent so that the transaction becomes voidable *ab initio*. But it has been applied altogether more generally, in cases which

can be rationalised only on grounds of public policy, for example to justify setting aside a public act such as a judgment, which is in no sense consensual, a jurisdiction which has existed since at least 1775 *Duchess of Kingstons Case* (1776) 2 Smiths LC (13th ed) 644, 646, 651. Or to abrogate a right derived from a legal status, such as marriage: *R v Secretary of State for the Home Department, Ex p Puttick* [1981] QB 767. Or to disapply a statutory time bar which on the face of the statute applies: *Welwyn Hateld Borough Council v Secretary of State for Communities and Local Government* [2011] 2 AC 304. These decisions (and there are others) illustrate a broader principle governing cases in which the benefit of some apparently absolute legal principle has been obtained by dishonesty. The authorities show that there are limited circumstances in which the law treats the use of a company as a means of evading the law as dishonest for this purpose.

...

[34] These considerations reflect the broader principle that the corporate veil may be pierced only to prevent the abuse of corporate legal personality. It may be an abuse of the separate legal personality of a company to use it to evade the law or to frustrate its enforcement. It is not an abuse to cause a legal liability to be incurred by the company in the first place. It is not an abuse to rely upon the fact (if it is a fact) that a liability is not the controller's because it is the company's. On the contrary, that is what incorporation is all about ...

[35] I conclude that there is a limited principle of English law which applies when a person is under an existing legal obligation or liability or subject to an existing legal restriction which he deliberately evades or whose enforcement he deliberately frustrates by interposing a company under his control. The court may then pierce the corporate veil for the purpose, and only for the purpose, of depriving the company or its controller of the advantage that they would otherwise have obtained by the company's separate legal personality. The principle is properly described as a limited one, because in almost every case where the test is satisfied, the facts will in practice disclose a legal relationship between the company and its controller which will make it unnecessary to pierce the corporate veil.

### *Gurbachan Singh*

[71] In the Malaysian context, the starting point (post *Prest*) is the judgment of the Federal Court (per Richard Malanjum CJSS) in

*Gurbachan Singh s/o Bagawan Singh & Ors v Vellasamy s/o Pennusamy & Ors (on their behalf and for the 213 sub-purchasers of plots of land known as PN35553, Lot 9108, Mukim Hutan Melintang, Hilir Perak) and Other Appeals.*<sup>70</sup> In that case, the Federal Court rendered its opinion in a serious case involving the breach of fiduciary duties by an advocate and solicitor. The Federal Court referred to the decision of the Supreme Court in *Prest* and said:

[96] But in the event that we should, we are of the view that it is now a settled law in Malaysia that the court would lift the corporate veil of a corporation if such corporation was set up for fraudulent purposes, or where it was established to avoid an existing obligation or even to prevent the abuse of a corporate legal personality (see *Prest v Petrodel Resources Limited & Ors* [2013] UKSC 34).

[97] As to what constitutes fraudulent purposes it has been described as to include actual fraud or fraud in equity (see *Law Kam Loy & Anor v Boltex Sdn Bhd & Ors*). And fraud in equity occurred in "... cases where there are signs of separate personalities of companies being used to enable persons to evade their contractual obligations or duties, the court would disregard the notional separateness of the companies ..." (see *Sunrise Sdn Bhd v First Profile (M) Sdn Bhd & Anor* [1997] 1 AMR 1; [1996] 3 MLJ 533 per Chong Siew Fai FCJ (as he then was)).

[98] Quite recently this court also discussed on the issue of lifting a corporate veil. It said this:

"... As for principle, the starting point is no doubt the doctrine of corporate personality. The general rule is that a company has an existence that is separate and distinct from its shareholders. It finds expression in the seminal case on the subject, *Salomon v A Salomon & Co Ltd* [1897] AC 22. Lord Halsbury LC there stated the rule thus:

'... once the company is legally incorporated it must be treated like any other independent person with its rights and liabilities appropriate to itself, and that the motives of those who took part in the promotion of the company are absolutely irrelevant in discussing what those rights and liabilities are.'

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70 [2015] 2 AMR 1; [2015] 1 MLJ 773, FC.

The Lord Chancellor however provided for cases in which the veil of incorporation may be lifted. He said:

'If there was no fraud and no agency, and if the company was a real one and not a fiction or a myth, every one of the grounds upon which it is sought to support the judgment is disposed of.'

The proposition when inverted states that if there is fraud or an agency relationship or if the company is a myth or fiction, the doctrine of corporate personality does not insulate the shareholders or directors from being assailed directly."

[22] A more recent statement of the doctrine of corporate personality is to be found in the case of *Woolfson v Strathclyde Regional Council* 1978 SLT 159 which is authority for the proposition that a litigant who seeks the court's intervention to pierce the corporate veil must establish special circumstances showing that the company in question is a mere façade concealing the true facts (see *Takako Sakao (f) v Ng Pek Yuan (f) & Anor*).

[99] The phrase "a mere façade concealing the true facts" was recently elaborated by the Supreme Court of the United Kingdom in the case of *Prest v Petrodel Resources Limited and others* [2013] UKSC 34. The leading judgment of the court said this:

"The concealment principle is legally banal and does not involve piercing the corporate veil at all. *It is the imposition of a company or perhaps several companies so as to conceal the identity of the real actors will not deter the courts from identifying them, assuming that their identity is legally relevant.* In these cases the court is not disregarding the "façade" but only looking behind it to discover the facts which the corporate structure is concealing. The evasion principle is different. It is that *the court may disregard the corporate veil if there is a legal right against the person in control of it which exists independently of the company's involvement, and a company is interposed so that the separate legal personality of the company will defeat the right or frustrate its enforcement.* Many cases will fall into both categories, but in some circumstances the difference between them may be critical. This may be illustrated by reference to those cases in which the court has been thought, rightly or wrongly, to have pierced the corporate veil."

(Emphasis added.)

[72] In the *Gurbachan Singh* case, the intended purchasers of the estate land were the clients of the first appellant (the solicitor), who proceeded to set up the fourth appellant (the company) with him, his wife and a friend by the name of Manjeet as the directors. The first appellant then transferred the ownership of the estate land to the fourth appellant on October 15, 1994. The first appellant had since transferred his shares in the fourth appellant to two companies, namely, Lien Hoe Xing Sdn Bhd and Jugra Palm Oil Mill Sdn Bhd. The Court of Appeal held that the transfer of the estate land to the fourth appellant did not extinguish the equity of the purchasers because the fourth appellant through the first appellant had full knowledge of the equitable rights of the purchasers on the estate land. The fourth appellant was the alter ego of the first appellant. Thus, it justified the lifting of the corporate veil of the fourth appellant. The Federal Court endorsed *Prest* and held that it would lift the corporate veil of a corporation which was set up for fraudulent purposes, or where it was established to avoid an existing obligation or even to prevent the abuse of a corporate legal personality.

### ***Mackt Logistics***

[73] In *Mackt Logistics (M) Sdn Bhd v Malaysian Airline System Berhad*,<sup>71</sup> the issue of separate legal entity came up for consideration before the Court of Appeal. In that case, the Court of Appeal applied the principles that were enunciated and restated by the Supreme Court of the United Kingdom in *Prest*. The plaintiff (“ML”) carried on the business of air cargo transportation and handling of consignment and dealt with various airlines, including the defendant (“MAS”). In order to facilitate the dealing, ML entered into a sales agency agreement with MAS which required ML to provide a bank guarantee by way of a security, which ML did.

[74] The bank guarantee was a conditional guarantee and was valid for a period of one year. Before the expiry of the bank guarantee, MAS issued a letter of demand to the bank to call on the guarantee. The letter of demand alleged that ML did not honour its obligations to MAS, without any reference to the sales agency agreement. MAS informed ML that the call was made because there were arrears of rent due to MAS from another company known as Mackt HWT Freight

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71 [2014] 2 AMCR 185; [2014] 5 CLJ 851; [2013] 1 LNS 1097, CA.

Sdn Bhd (“Mackt HWT”) under a tenancy agreement relating to the rental of Masgo VDU and the Kuala Lumpur International Airport premises. The other reason cited for the call on the guarantee was for electricity charges that were due from Mackt HWT. The High Court dismissed ML’s claim after having pierced the corporate veil of Mackt HWT and found that the same individual was responsible for ML as well as Mackt HWT. ML appealed to the Court of Appeal. The Court of Appeal allowed the appeal. The following synopsis encapsulates the salient parts of the judgment. The first point enunciated was that once a company is incorporated, a veil is cast over the true controllers of the company, through which the law will not usually penetrate. There was no standard principle to guide the courts in piercing the corporate veil. The Court of Appeal opined that there are statutory as well as common law exceptions to the principle enunciated in *Salomon*, and once a case comes within one of the exceptions, the courts may lift the veil of incorporation.

[75] The Court of Appeal enunciated that in piercing the corporate veil, the facts of the case must be examined and it must be clearly pleaded that the veil should be lifted.<sup>72</sup> The Court of Appeal went on to hold that the plaintiff and Mackt HWT were different companies and were separate legal entities. The fact that both companies had common directors or shareholders did not negate the fact that both companies were separate legal entities. The High Court judge, having found that ML and Mackt HWT were two different legal entities, erred in law and in fact in lifting the veil of incorporation when there was no legal justification or any special circumstances required by law to do so. Further, the Court of Appeal took the view that the failure by MAS to plead the requirements to pierce the veil of incorporation must be construed against the defendant. It was, according to the Court of Appeal, fatal.<sup>73</sup>

### *Tenaga Nasional Bhd v Irham Niaga Sdn Bhd*

[76] The next case that is relevant for the present discussion is the decision of the Court of Appeal in *Tenaga Nasional Bhd v Irham Niaga Sdn Bhd & Anor* (“TNB”).<sup>74</sup>

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72 Ibid, at [19], [34], [35] and [39].

73 Ibid, at [33], [42], [44] and [60].

74 [2017] 5 CLJ 488; [2015] 1 LNS 1486; [2015] MLJU 2165, CA.

[77] The issue in *TNB* was whether the holding company could be held liable for the judgment debt of a wholly-owned subsidiary, TNB Transmission Network Sdn Bhd (“TNBT”) which was controlled and funded by the holding company. The judgment debt arose out of an arbitration award that was obtained by the plaintiff against TNBT. The facts of *TNB* are as follows. TNB operated a single business unit and performed its functions through its various divisions. TNB decided to decentralise its various functions and incorporated several subsidiaries which included TNBT. TNBT entered into five lease and warehouse management agreements (“the agreements”) between 2001 and 2002 with the plaintiffs. In 2004, TNBT decided to terminate the agreements. The dispute was then referred to arbitration. After the final award was given by the arbitrator, the plaintiffs found out that TNB had declared that its financial performance would not be affected by the award as TNBT was a dormant company. TNB then proceeded to “collapse back” the functions of several of its subsidiaries, which included TNBT, to itself. The plaintiffs then commenced proceedings against TNB in the High Court for the payment of the arbitration award. The plaintiffs sought to lift the corporate veil of TNBT on the grounds that TNB:

- (i) was the entity having total control, direction and management of TNBT such that TNB and TNBT were one and the same; and
- (ii) had committed fraud against the plaintiffs through the use of TNBT as the contracting vehicle for the agreements.

[78] The High Court judge found that this was a case of:

- (i) special circumstances where there existed “inequitable or unconscionable conduct amounting to fraud in equity”, although not actual fraud; and
- (ii) it was inequitable and unconscionable for TNB to have collapsed back the business of TNBT.

[79] The High Court judge thus lifted the corporate veil. TNB appealed to the Court of Appeal. The appeal was allowed. The main issue that was canvassed was the allegation that TNB had total control and management of TNBT or, alternatively, there was functional integrity between TNB and TNBT such that TNB and TNBT are one and the same. It was alleged by the plaintiff as an alternative that there was evidence to show or infer that TNB had committed fraud against the

plaintiff through the use of TNBT as the contracting vehicle for the agreements. TNBT was under the full control of TNB through the provision of funds, premises and personnel and the legal structures put in place by TNB. The managing director of TNBT was the Vice-President of the Transmission Division of TNB and he sat at the same desk and in the same premises. Essentially, the plaintiff argued that TNBT and TNB were operating as basically one entity. The plaintiff made it clear that it was not its case that the corporate veil should be lifted “in the interests of justice or based on economic entity”. Rather, the plaintiff’s position was that TNBT and TNB were one and the same entity. Thus, it was argued that it was unconscionable for TNB to hide behind the corporate veil.

[80] The Court of Appeal held at paragraph 49 that the “evidence was crystal clear that TNBT, which was formed long before the agreements were entered into, was not formed as a means to conceal the true facts in order to avoid contractual liability”. The plaintiff knew very well the true nature of TNBT and its mode of operations. And the Court of Appeal held that,<sup>75</sup> “even if there was no “collapsing back, there was always a danger that TNBT could be wound up and, being a company with no assets of its own, TNBT would be in no position to make any payments to the plaintiffs or any other creditor. The plaintiffs knew this full well.

[81] In so far as the issue of fraud is concerned, the Court of Appeal held that there was no actual fraud involved in the present case. The court observed that the plaintiff’s pleaded case was clearly one of actual fraud. As such, the Court of Appeal opined that *the High Court judge had erred in lifting the corporate veil on the ground of “inequitable or unconscionable conduct amounting to fraud” when that was not the pleaded case of the plaintiffs*. After analysing the evidence, the Court of Appeal concluded that there was no basis for the corporate veil to be lifted.

### **Pleadings**

[82] Premised upon the above, it is clear that, over and above control, there must be some “relevant impropriety” linked to the use of the company structure to avoid or conceal liability for that impropriety. If fraud is being asserted, then the plaintiff must be crystal clear

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75 Ibid, at [50].

about the particular type of fraud that is being relied upon. Hence, the pleadings become crucial. The plaintiff must plead whether the defendant's conduct was unconscionable and/or that the fraud in question is that of actual or equitable fraud. This is important because of the trite rule that a party is bound by the four corners of its pleadings and as such, is not entitled to rely upon facts and/or issues which have not been specifically pleaded. Thus, in cases where it is sought to lift the veil of incorporation, it is vital that there be proper and specific pleading for the lifting of the corporate veil and an identification of the type of fraud (common law fraud or equitable fraud) that is being relied upon by the plaintiff. The emphasis on pleadings is because of the demarcation between actual fraud or common law fraud and equitable fraud. In this regard, the failure to make a proper plea can be decisive, if not fatal. There are crucial distinctions which exist in law between equitable fraud and actual fraud.

[83] These differences have been elucidated at length in the case of *Takako Sakao (f) v Ng Pek Yuen (f) & Anor*<sup>76</sup> in which Gopal Sri Ram FCJ (delivering judgment of the court) had stated that:

The fraud of which Lord Halsbury spoke in *Salomon v A Salomon & Co Ltd* includes equitable fraud. In the recent Australian case of the *The Bell Group Ltd (In Liquidation) v Westpac Banking Corporation (No. 9)* [2008] WASC 239; 70 ACSR 1, Owen J discussed the distinction between equitable fraud and fraud at common law. His Honour said:

“One of the leading Australian texts on equitable principles ... *Meagher, Gummow and Lehane's Equity Doctrines and Remedies* ... At [12-050] the authors set out a non-exhaustive list of factual and legal situations that have traditionally been treated as species of equitable fraud. They include:

- (a) Misrepresentation by persons under an obligation to exercise skill and discharge reliance and trust ... and inducements to contract or otherwise for the representee to act to his detriment in reliance on the representation;
- (b) The use of power to power to procure a bargain or gift, resulting in disadvantage to the other party;

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76 [2010] 2 AMR 609; [2009] 6 MLJ 751.

- (c) Conflict of interest against a duty arising from a fiduciary relationship; and
- (d) Agreements which are bona fide between the parties but in fraud of third persons.’

...

The term common law fraud is often used to describe the tort of deceit, or the making of fraudulent misrepresentations. The tort of deceit is said to encompass cases where the defendant knowingly or recklessly makes a false statement, with the intention that another will rely on it to his or her detriment.

...

This then marks out a significant difference between common law fraud and equitable fraud. The latter does not require proof of an actual intention to deceive.

To summarise, a plea of fraud at common law will not succeed absent proof of an actual intention to deceive. Such an intention is not an ingredient of equitable fraud which is, essentially speaking, unconscionable conduct in circumstances where there exists or is implied or imposed a relationship of trust or confidence.”

[84] Quite clearly, there are two types of fraud which are recognised in law. One being common law fraud and the other equitable fraud. Legally, there are differences in terms of the elements needed to prove their existence. Hence, where two types of fraud are possible, the opposite party is entitled to know which type of fraud is levelled against it. Thus, if it is equitable fraud that is invoked, then particulars of the circumstances of the relationship between the parties giving rise to unconscionable conduct complained of should be pleaded. Moreover, since one type of fraud involves dishonesty and the other may not, the opposite party must surely be given notice if dishonesty is alleged against it and how the dishonesty was allegedly practiced.

[85] As was pointed out in Munby J in the case of *Ben Hashem*, merely taking advantage of an existing corporate structure is simply taking advantage of the principle in *Salomon*.<sup>77</sup> There has to be impropriety

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77 [2008] EWHC 2380 (Fam); [2008] Fam Law 1179; [2009] 1 FLR 115 at [199].

and the misuse of the company structure to conceal it. It is axiomatic that the impropriety must be pleaded. The importance of pleading in the context of lifting of the corporate veil can be gleaned from the following cases.

[86] In *Gurbachan Singh*, lifting of the corporate veil was not pleaded. But the relevant evidence on this issue was adduced, apparently without objection by the opposite side. The Federal Court (per Richard Malanjum CJSS) said:

[89] It is trite law that the parties are bound by their pleadings and the trial of a suit must confine to the pleadings. The court is not entitled to decide a suit on a matter that has not been pleaded (see *Yew Wan Leong v Lai Kok Chye* [1990] 1 CLJ (Rep) 330).

[90] However, in some instances, evidence adduced during the hearing can overcome the defects in pleadings as long as the other party is not taken by surprise. More so if “Such evidence when given without any objection by the opposing party will further have the effect of curing the absence of such plea in the relevant pleading, in other words, the effect of overcoming such defect in such pleading” (see *Superintendent of Lands and Surveys (4th Div) & Anor v Hamit bin Matusin & Ors* [1994] 3 AMR 1882; [1994] 3 CLJ 567).

[91] In this case the respondents while conceding that issue on lifting the corporate veil of the companies was not pleaded argued that the evidence relating to the issue was adduced. As such the learned trial judge had erred in dismissing the issue on the ground that it was not pleaded.

[92] We find the majority has dealt with the point quite succinctly. Having considered the evidence adduced by the respondents as highlighted by the majority, we are satisfied that evidence relating to the issue of whether the third appellant and SPPKB were one and same entity and whether the first appellant was the alter ego of the fourth appellant had been given without any objection from the appellants.

[93] For instance, it was not a disputed fact and indeed evidence was adduced that the directors of SPPKB replaced the directors of Nam Bee as the directors of the third appellant. That occurred soon after the estate land was transferred to the third appellant. and in respect of the fourth appellant there was no denial and in fact the first appellant admitted that he was its director for a while.

[94] Hence, having considered the case for the respondents as a whole it could not be said that such evidence had departed radically from their pleaded case. Such evidence, in our view, had cured the absence of a specific plea of the aforementioned parties being one and same entities in the respondents' statement of claim. With respect we are therefore of the view that the learned trial judge should not have dismissed the issue on account of it being not pleaded.

[87] In *Alcatel-Lucent (M) Sdn Bhd (formerly known as Alcatel Network Systems (M) Sdn Bhd) v Solid Investments Ltd and Another Appeal*,<sup>78</sup> Ramly Ali JCA (as he then was) said:

[10] The respondent's pleaded case was the existence of a collateral agreement, separate from the consultancy agreements under which it was suing. Learned judge went beyond the pleaded case when he decided to lift the corporate veil to find that the appellant was bound by the consultancy agreements (which the appellant was not a party).

[11] It is trite that parties are bound by their pleadings. *For the court to lift the corporate veil, the said issue must be specifically pleaded by a litigant* (see *Vellasamy Ponnusamy v Gurbachan Singh* [2006] 2 MLJ 715; [2006] 1 CLJ 805). Therefore, the judgment of the learned judge ought to be set aside on this ground alone.

(Emphasis added.)

[88] The matter went up to the Federal Court and the decision is reported as *Solid Investments Ltd v Alcatel-Lucent (M) Sdn Bhd (previously known as Alcatel Network Systems (M) Sdn Bhd)*.<sup>79</sup> However, the appeal before the Federal Court focused on the substantive issue of the fiduciary relationship and whether there was a duty to account. The pleadings point was not dealt with by the Federal Court.

[89] In *Giga Engineering & Construction Sdn Bhd v Yip Chee Seng & Sons Sdn Bhd & Anor*,<sup>80</sup> Richard Malanjum CJSS emphasised the importance of pleading fraud for purposes of the lifting of the corporate veil. The Federal Court said:

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78 [2012] 4 MLJ 72, CA at 80.

79 [2014] 1 AMR 348; [2014] 1 AMCR 230; [2014] 3 MLJ 785; [2014] 3 CLJ 73.

80 [2015] 6 AMR 765; [2015] 2 AMCR 855; [2015] 6 MLJ 449; [2015] 9 CLJ 537.

[34] While it was pleaded that the defendants were “part of a group of companies managed and/or controlled by the Yip family with common/connected officers and shareholders”, there is no further assertion or claim arising therefrom in the way as submitted before us by learned counsel for the plaintiff.

[35] Indeed there was *no allegation in the amended statement of claim that the plaintiff was not awarded the sub-sub contract works as a result of manipulation or the abuse of the “single” entity of the defendants.*

[36] It is also *not pleaded that in the scheme of things the defendants and the third defendant were under the dominant control of Yip Kok Weng. There was also no allegation in the amended statement of claim of fraud or equitable fraud or misrepresentation practised by the defendants upon the plaintiff during the discussion in the preparation of quotation or tender documents for the project.*

[37] Yet in his submission learned counsel for the plaintiff urged us, inter alia, to consider lifting the corporate veil of the defendants. Unfortunately, *we find nothing in the amended statement of claim that alleged the defendants committed fraud, actual or equitable fraud upon the plaintiff. There was also no allegation that the defendants misled the plaintiff.*

[38] At best the plaintiff merely pleaded that the first and second defendants:

- “a. are ... part of a group of companies managed and or controlled by the Yip family with common and or connected officers and shareholders’; and
- b. that ‘having regard to the relationship inter-se the parties arising from the joint venture and further upon the defendants having, with knowledge and encouragement, obtained the benefits of the plaintiff’s input and efforts as set out above, the defendants, in particular the first and second defendants, were under the following implied obligations towards the plaintiff in relation to the plaintiff’s portion:
  - i. not to act in any manner inconsistent with the agreement on the plaintiff’s portion;
  - ii. to, inter alia, cooperate and take all necessary steps to ensure that the plaintiff be awarded the plaintiff’s portion pursuant to the agreement on the plaintiff’s portion.”

[39] With respect, *we do not think the foregoing allegations as pleaded are sufficient as a plea for fraud or equitable fraud or to indicate special circumstances upon which on evidence adduced would justify the lifting of corporate veil of the defendants.*

...

[45] It is settled law that “there must be evidence either of actual fraud or some conduct amounting to fraud in equity to justify the lifting of corporate veil” (see *Solid Investments Ltd v Alcatel-Lucent (Malaysia) Sdn Bhd (dahulu dikenali sebagai Alcatel Network Systems (Malaysia) Sdn Bhd)* [2014] 1 AMR 348; [2014] 1 AMCR 230; [2014] 3 CLJ 73). Further, *in a plea of fraud mere allegations is not sufficient. There must be particulars given.* (see *Lee Kim Luang v Lee Shiah Yee* [1988] 1 MLJ 193).

(Emphasis added.)

## Conclusion

[90] To recapitulate, the guiding principles for purposes of the lifting of the corporate veil (per *Ben Hashem, VTB, Prest, TNB and Gurbachan Singh*) are:

- Merely taking advantage of an existing corporate structure to allocate risk or liability on a particular entity within a group of companies is simply taking advantage of the principle in *Salomon*. There has to be impropriety and the misuse of the company structure to conceal the company’s liability if the veil is to be lifted.
- Ownership and control of a company are not of themselves sufficient to justify lifting the veil.
- The court cannot lift the corporate veil, even where there is no unconnected third party involved, merely because it is thought to be necessary in the interests of justice.
- The corporate veil can be lifted only if there is some “impropriety”.
- Inequitable or unconscionable conduct per se would not be fraud in equity. It must be of such a degree that it amounted to fraud in equity and thereby justifying the lifting of the corporate veil.
- The court would lift the corporate veil of a corporation if it was set up for fraudulent purposes, or where it was established to

avoid an existing obligation or even to prevent the abuse of a corporate legal personality.

- The court cannot, on the other hand, lift the corporate veil merely because the company is involved in some impropriety. The impropriety must be linked to the use of the company structure to avoid or conceal liability.
- If the court is to lift the veil, it is necessary to show both control of the company by the wrongdoer(s) and impropriety, that is, misuse of the company structure by them as a device or façade to conceal their wrongdoing.
- A company can be a façade even though it was not originally incorporated with any deceptive intent. The question is whether it is being used as a façade at the time of the relevant transaction(s).
- The court will lift the veil only so far as is necessary to provide a remedy for the particular wrong which those controlling the company have done. In other words, the fact that the court lifts the veil for one purpose does not mean that it will necessarily be lifted for all purposes.

[91] In every case where there is a plea for the lifting of the corporate veil, it is necessary that the facts be thoroughly examined so as to detect any fraud or impropriety linked to the use of the company structure, whether by way of concealment or evasion of liability or otherwise. If the evidence shows that the company was not used as a front or a façade or a sham from the outset or during the currency of the relevant transaction or dealing, then plainly there will be no justification for lifting of the corporate veil. It is doubtful whether in view of *Boltex*, the single economic unit theory (per *DHN*) is still relevant. Thus, whether a group of companies operating or behaving as a single unit or entity *per se*, without any fraud or without any deception, misrepresentation and without these companies being used as a front or façade or a sham to evade or conceal liability, would suffice as a basis to lift the corporate veil. As such, the *Epic Quest* approach may have to be revisited and clarified in due course. And in terms of the adjectival or procedural law, it is axiomatic that lifting of the corporate veil must be pleaded with proper particulars of fraud (identifying whether it is common law fraud or equitable fraud) or conduct suggestive of the use of the company structure as a façade or a sham in order to conceal or evade legal obligations.

[92] In this regard, it is worth noting that the Court of Appeal in *Theta Edge Bhd (previously known as Lityan Holdings Bhd) v Inforiential Sdn Bhd (and Another Appeal)* ("*Theta Edge*")<sup>81</sup> recently dealt with the issue of the parent company and wholly owned subsidiary purportedly operating as a single entity. The respondent had obtained judgment against the subsidiary. The judgment remained unsatisfied. The subsidiary was voluntarily wound up on August 18, 2010 pursuant to section 255 of the Companies Act 1965. The judge allowed the respondent's claim against the appellant and found that the appellant had acted fraudulently to wind up the subsidiary to deprive the respondent of the proceeds of the judgment and hence, pierced the corporate veil of the appellant. On appeal it was contended that the respondent failed to specifically plead the particulars of fraud and also failed to prove any allegation of fraud against the appellant.

[93] In *Theta Edge*, the Court of Appeal allowed the appeal and held that the parent company and its subsidiary were two distinct commercial entities. It held that evidentially, there was no basis to infer that the two companies had operated as a single commercial entity. There was no evidence to confirm that the activities of the two companies were so intertwined that they had operated as a single commercial entity. The Court of Appeal went on to hold that the corporate veil will be pierced only in appropriate circumstances and that it is not open to the courts to disregard the corporate veil purely on the ground that it is in the interest of justice to do so. It held that there must be evidence of either actual fraud at common law or some inequitable or unconscionable conduct amounting to fraud in equity. Ultimately, there was insufficient evidence of actual or equitable fraud made out by the respondent against the appellant and there was no justification to pierce the corporate veil of the appellant.

[94] Although the outcome was not in favour of lifting the corporate veil, the Court of Appeal was implicitly entertaining the single economic entity theory as a plausible basis for the lifting of the corporate veil. But the vexed question (for the Federal Court in future) is whether in light of *Adams v Cape* and the *Boltex* case, the single economic entity principle (per *DHN* and *Hotel Jayapuri*) is still relevant and extant in Malaysian corporate jurisprudence.

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81 [2017] 2 AMR 901; [2017] 2 MLJ 34.

[95] In so far as pleadings are concerned, it is unlikely that the Malaysian courts will condone or overlook a failure to plead a relief predicated on the lifting of the corporate veil and/or a failure to identify the type of fraud that is being alleged and/or to render particulars relevant to the fraud that is being alleged. This is especially since the Federal Court has recently emphasised and reiterated the importance of pleadings. In this regard, it is relevant to quote the Federal Court's decision in *Samuel Naik Siang Ting v Public Bank Bhd*<sup>82</sup> per Ramly Ali FCJ where it was stated that:

[29] It is a cardinal rule in civil litigation that parties are bound by their pleadings and are not allowed to adduce facts and issues which they have not pleaded (see: *State Government of Perak v Muniandy* [1985] 1 LNS 117; [1986] 1 MLJ 490; and *Anuar Mat Amin v Abdullah Mohd Zain* [1989] 1 LNS 74; [1989] 3 MLJ 313). In *Blay v Pollard & Morris* [1930] 1 KB 628, Scrutton LJ ruled that: "*Cases must be decided on the issues on the record; and if it is desired to raise other issues there must be pleaded on the record by amendment.*"

[30] The Supreme Court in *Lee Ah Chor v Southern Bank Bhd* [1991] 1 CLJ 667; [1991] 1 CLJ (Rep) 239; [1991] 1 MLJ 428, had also emphasised the importance of pleadings and ruled that where a vital issue was not raised in the pleadings it could not be allowed to be argued and to succeed on appeal (see also *Ambank (M) Bhd v Luqman Kamil Mohammed Don* [2012] 3 CLJ 551; [2012] MLJU 56 FC).

[31] On the same issue, HRH Raja Azlan Shah FJ (as HRH then was) in *The Chartered Bank v Yong Chan* [1974] 1 LNS 178; [1974] 1 MLJ 157, had also pointed out that "*as the trial judge had decided on an issue which was not raised in the pleadings, the judgment must be set aside and new trial ordered*" (see also: *Haji Mohamed Dom v Sakiman* [1955]).

[96] Quite obviously, the cases of *VTB* and *Prest* are momentous decisions *vis-à-vis* lifting of the corporate veil as they clarify, restate and circumscribe the relevant principles. There are some however, who question whether a unifying principle on lifting of the corporate veil has truly emanated from *VTB* and *Prest*.<sup>83</sup> At any rate, *VTB* and *Prest* are important decisions which will shape and refine company law

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82 [2015] 8 CLJ 944, FC.

83 See Tan Zhong Xing, "The New Era of Corporate Veil-Piercing-Concealed Cracks and Evaded Issues" (2016) 28 *Singapore Academy of Law Journal* 209.

jurisprudence. They will undoubtedly be relevant and (depending on the fact pattern) may even be decisive in cases where the claimant seeks to lift the corporate veil. *Prest* will of course be specifically relevant in cases of matrimonial disputes, particularly on the contentious issue of beneficial ownership of assets by the spouse where legal ownership resides in companies controlled or owned by the spouse or by the nominee of the spouse.

# Enforcement of Foreign Arbitral Awards

*by*

*Justice Azizul A Adnan\**

[1] This article discusses the procedures applicable to, and some of the issues arising in connection with, the enforcement of foreign arbitral awards in Malaysia.

## **Introduction**

[2] The Malaysian Arbitration Act 2005 (Act 646) (“AA 2005”) came into force on March 15, 2006. It was based on the United Nations Commission on International Trade Law (UNCITRAL) Model Law on International Commercial Arbitration (“Model Law”), with certain modifications. The Model Law, which was adopted by a resolution of the UN General Assembly in 1985, aims to establish a unified framework to settle disputes by way of arbitration, with a particular emphasis on commercial disputes. The Model Law is derived from the New York Convention.<sup>1</sup>

[3] In the Malaysian legislation, a distinction is made between international arbitration and domestic arbitration, with the courts retaining greater supervisory functions over domestic arbitration. Part III of the AA 2005 applies to domestic arbitration unless parties opt out, and does not apply to international arbitration unless parties opt in. Part III provides for the powers of the courts to exercise greater control over the conduct of domestic arbitrations, key among which is the ability of parties to refer questions of law to the courts.

[4] The New York Convention did not initially provide for the ability to set aside arbitral awards, but this ability was subsequently included in the Model Law in Article 34, which has been enacted in section 37 of our AA 2005. This is significant in the context of the distinction between an action to set aside an arbitral award (pursuant to

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\* Judge of the High Court of Malaya.

1 The New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958, to which Malaysia had acceded in 1985.

section 37) and an action to resist the enforcement of an award (under section 39), a point to which we will return to later in this article.

### **Procedure for recognition and enforcement**

[5] A party seeking to enforce an arbitral award (whether given pursuant to a domestic arbitration or an international arbitration) must make an application to the High Court under section 38 of the AA 2005. In the context of a foreign arbitral award, such an award may only be recognised as binding if the award was granted in a jurisdiction of a contracting state to the New York Convention.<sup>2</sup> This ought not to pose a problem in practice, as there are some 157 signatories to the Convention. In addition, countries that are not signatories—the very short list as at the date of writing includes states such as Iraq, Yemen, Sudan, Libya and Somalia—are not likely to be active centres for arbitration.

[6] An award that has been recognised as binding under section 38 may be enforced in the same manner as a judgment of the courts. The procedure for recognition, governed by section 38 as well as Order 69 rules 8 and 9 of the Rules of Court 2012, is a two-step process. At the outset, the party seeking to enforce the award makes an *ex parte* application to the High Court by way of an originating summons. The summons must be accompanied by an affidavit exhibiting the duly authenticated original award and the original arbitration agreement, or duly certified copies of such documents. It is incumbent upon the court to ensure that these requirements are met, as the hearing of the summons is conducted *ex parte*, unless the court has directed pursuant to Order 69 rule 8(4) for the originating summons to be first served on the person against whom the award is sought to be enforced.

[7] For ease of reference, section 38 of the AA 2005 is reproduced below:

#### *38. Recognition and enforcement*

- (1) On an application in writing to the High Court, an award made in respect of an arbitration where the seat of arbitration is in Malaysia or an award from a foreign State shall, subject

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<sup>2</sup> The contracting states of the New York Convention may be found at <http://www.newyorkconvention.org/list-of-contracting-states>.

to this section and section 39 be recognized as binding and be enforced by entry as a judgment in terms of the award or by action.

- (2) In an application under subsection (1) the applicant shall produce:
  - (a) the duly authenticated original award or a duly certified copy of the award; and
  - (b) the original arbitration agreement or a duly certified copy of the agreement.
- (3) Where the award or arbitration agreement is in a language other than the national language or the English language, the applicant shall supply a duly certified translation of the award or agreement in the English language.
- (4) For the purposes of this Act, “foreign State” means a State which is a party to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards adopted by the United Nations Conference on International Commercial Arbitration in 1958.

[8] The procedure for recognition and enforcement is set out in Order 69 rules 8 and 9 of the Rules of Court 2012, which provide as follows:

8. *Enforcement of awards (O. 69 r. 8)*

- (1) An application for permission to enforce an award in the same manner as a judgment or an order may be made without notice in an arbitration claim originating summons.
- (2) The arbitration claim originating summons shall –
  - (a) state the name and the usual or last known place of abode or business of the applicant, and the respondent against whom it is sought to enforce the award, respectively; and
  - (b) state either that the award has not been complied with or the extent to which it has not been complied with at the date of the application.
- (3) The applicant shall file by affidavit, written evidence on which he intends to rely when he files his originating summons,

including exhibiting the original arbitration agreement and the duly authenticated original award or, in either case, a duly certified copy thereof and where the award or agreement is in a language other than the national language or English, a translation of it in the English language, duly certified as a correct translation by a sworn translator or by an official or by a diplomatic or consular agent of the country in which the award was made.

- (4) The Court may specify parties to the arbitration on whom the arbitration claim originating summons shall be served.
- (5) With the permission of the Court, the arbitration claim originating summons may be served out of the jurisdiction irrespective of where the award is, or is treated as, made.
- (6) An order giving permission to enforce the award shall:
  - (a) be drawn up by the applicant; and
  - (b) be served on the respondent by –
    - (i) delivering a copy to him personally; or
    - (ii) sending a copy to him at his usual or last known place of residence or business.
- (7) Within fourteen days after service of the order giving permission to enforce the award or, if the order is to be served out of the jurisdiction, within such other period as the Court may set:
  - (a) the respondent may apply to set aside such order; and
  - (b) the award shall not be enforced until –
    - (i) after the expiration of that period; or
    - (ii) if the respondent applies within that period to set aside, until after the application made by the respondent has been finally disposed of.
- (8) The order giving permission for enforcement shall contain a statement of the right to make an application to set aside the order.

- (8A) Order 11, rules 5, 6, and 8 shall apply to the service out of jurisdiction of the arbitration claim originating summons, or any order made in such claim, under paragraph (5).
- (9) Where a body corporate is a party, any reference in this rule to a place of residence or business shall have effect as if the reference were to the registered or principal address of the body corporate.
- (10) Where the award sought to be enforced is in the nature of an interim injunction under subsection 13(6) of the 1952 Act or subsection 19(1) of the 2005 Act, the order shall be granted only if the applicant undertakes to abide by any order the Court or the arbitral tribunal may make as to damages. The order shall be enforceable immediately, and subparagraph (7)(b) shall not apply.

9. *Registration in High Court of foreign awards (O. 69 r. 9)*

Where an award has, under the law in force in the place where it was made become enforceable in the same manner as a judgment given by a Court in that place, an applicant may enforce the award in the manner provided for under rule 8.

[9] There does not appear to be any discretion on the part of the courts to refuse the order sought for once the requirements of section 38 have been met, due to the peremptory language used in that section.

[10] An order granted pursuant to section 38 is thereafter served on the person against whom the award is sought to be enforced. Under Order 69 rule 8(7), that person has 14 days from its receipt of the order of the High Court granting recognition of the award to apply to set it aside. If it fails to do so, the order granting recognition to the award may be enforced against it.

[11] Where an application is made by that person under section 39 to set aside the order granting recognition of the award, the court will hear arguments at an *inter partes* hearing as to why the courts ought to refuse recognition of the award. This is the second stage of the process.

### **Setting aside the order of recognition**

[12] It is important to appreciate the difference between an application to challenge the order granting recognition of an award made under

section 39, and an application under section 37 to set aside the award itself. The difference is particularly significant in international arbitrations, where the party against whom the award is sought to be enforced may have assets in multiple jurisdictions. If a court has allowed an application under section 39 to refuse the enforcement of an award in Malaysia, there is nothing to prevent the other party from seeking to enforce the award in any other jurisdiction where the respondent may have assets.

[13] On the other hand, if the award itself has been set aside, then that would be the end of the matter. No other action may be taken to enforce the award whether in Malaysia or in any other contracting state of the New York Convention.

[14] Under section 39 of the AA 2005, the grounds upon which the courts may refuse the recognition and enforcement of an arbitral award are divided into two categories. Grounds that are primarily fact-driven and which have to be proven by a party are: lack of capacity of any of the parties to conclude an arbitration agreement; lack of a valid arbitration agreement, inadequate notice for the appointment of the arbitrator or for the arbitration; the inability of a party to have presented its case; the award dealt with or decided on matters outside the scope of the arbitration; the composition of, or the procedure adopted by, the arbitral tribunal was not in accordance with the parties' agreement; and the award has not yet become binding or has been set aside or suspended. Grounds that are primarily questions of law and which the court may consider of its own initiative are: the non-arbitrability of the subject matter of the dispute; and the violation of Malaysian public policy.

[15] Section 39(1) is set out below:

39. *Grounds for refusing recognition or enforcement*

- (1) Recognition or enforcement of an award, irrespective of the State in which it was made, may be refused only at the request of the party against whom it is invoked –
  - (a) where that party provides to the High Court proof that –
    - (i) a party to the arbitration agreement was under any incapacity;

- (ii) the arbitration agreement is not valid under the law to which the parties have subjected it, or, failing any indication thereon, under the laws of the State where the award was made;
  - (iii) the party making the application was not given proper notice of the appointment of an arbitrator or of the arbitral proceedings or was otherwise unable to present that party's case;
  - (iv) the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration;
  - (v) subject to subsection (3), the award contains decisions on matters beyond the scope of the submission to arbitration;
  - (vi) the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties, unless such agreement was in conflict with a provision of this Act from which the parties cannot derogate, or, failing such agreement, was not in accordance with this Act; or
  - (vii) the award has not yet become binding on the parties or has been set aside or suspended by a court of the country in which, or under the law of which, that award was made; or
- (b) if the High Court finds that –
- (i) the subject-matter of the dispute is not capable of settlement by arbitration under the laws of Malaysia; or
  - (ii) the award is in conflict with the public policy of Malaysia.

**[16]** The order of court delivered pursuant to section 38 may thus be seen as a conditional order: an arbitral award, by the grant of the section 38 order, is recognised as binding and may be enforced as though it were a judgment of court, but the party against whom the award is being sought to be enforced may nonetheless mount a challenge under section 39 to resist its enforcement. Only where the

party served with the section 38 notice fails to apply to challenge the award within 14 days, or where that challenge fails, may the award be thereafter enforced against that party.

[17] The recent decision of the Federal Court in *CTI Group Inc v International Bulk Carriers SPA*<sup>3</sup> (affirming the decision of Ravinthran Paramaguru J at first instance) held that the grounds set out in section 39 are exhaustive. It was not open to the defendant to challenge the recognition and enforcement of an award under section 39 on grounds that the arbitration agreement produced at the first stage was not an agreement between the plaintiff and the defendant. In respect of the first stage, the Federal Court had this to say:

[88] If the parties are named in the arbitration agreement, or if it is obvious on the face of the arbitration agreement that they are parties to the agreement, obviously the “apparently valid” test in *Darnada, Lombard-Knight* and *Dallah*, or the “prima facie” test in *Attain*, is satisfied. There is nothing more to be done. The award creditor applying for enforcement has discharged its evidential burden. Leave must be granted, and the matter must proceed to the second stage if the award debtor seeks to challenge such leave.

[18] The award debtor in that case sought to challenge the enforcement of the award on the basis that it was not a party to the share transfer agreement (which contained an arbitration clause) that had been exhibited before the High Court. It was a party to two annexes to that agreement, but these annexes had not been exhibited. The High Court had nonetheless granted the section 38 order on the basis that the annexes were an integral part of the share transfer agreement, and thus the non-production of the annexes were irrelevant as the arbitration agreement was found in the share transfer agreement.

[19] Any challenge at the second (substantive) stage was limited to the grounds provided under section 39 only. The Federal Court explained:

[105] In our view, the two-stage process for the enforcement of arbitral awards as contained in ss 38 and 39 of our Arbitration Act (read with Order 68 r 8 of the Rules of Court 2012) does not permit a party seeking to set aside an order made under s 38 to apply to

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3 [2017] 6 AMR 344; [2017] 9 CLJ 499.

set it aside under that very section on the ground that there was no arbitration agreement in existence between the parties. That party must apply to set that order aside under s 39.

[106] When the matter moves to the second stage under s 39, the defendant can only apply to set aside the order made under s 38 upon any one or more of the grounds set out in s 39 and no other.

[20] A further important point arises in connection with a section 39 challenge, and that is whether an award debtor may raise a challenge in the enforcement courts under section 39 without first having applied to set aside the award in the courts exercising supervisory jurisdiction over the arbitration proceedings. This point will be considered at paragraphs 36 *et seq.*, after first discussing the provisions relating to setting aside an award under section 37.

### Setting aside an award

[21] The grounds upon which an arbitration award may be set aside is contained in section 37(1) of the AA 2005, which provides as follows:

#### 37. *Application for setting aside*

- (1) An award may be set aside by the High Court only if –
  - (a) the party making the application provides proof that –
    - (i) a party to the arbitration agreement was under any incapacity;
    - (ii) the arbitration agreement is not valid under the law to which the parties have subjected it, or, failing any indication thereon, under the laws of Malaysia;
    - (iii) the party making the application was not given proper notice of the appointment of an arbitrator or of the arbitral proceedings or was otherwise unable to present that party's case;
    - (iv) the award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration;

- (v) subject to subsection (3), the award contains decisions on matters beyond the scope of the submission to arbitration; or
  - (vi) the composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties, unless such agreement was in conflict with a provision of this Act from which the parties cannot derogate, or, failing such agreement, was not in accordance with this Act; or
- (b) the High Court finds that –
- (i) the subject-matter of the dispute is not capable of settlement by arbitration under the laws of Malaysia; or
  - (ii) the award is in conflict with the public policy of Malaysia.

[22] The first observation that may be made is that these grounds mirror almost exactly the grounds for resisting an enforcement of an award, save that there is no corresponding counterpart in section 37 to the provisions of section 39(1)(a)(vii).

[23] The second important observation is that, even though this is not explicitly set out in section 37, an arbitral award may only be set aside in the jurisdiction of the seat of arbitration, that is, before the courts exercising supervisory jurisdiction over the arbitration proceedings, and not before the enforcement courts.

[24] The reason that this is so is explained in the judgment of Arifin Zakaria CJ (Malaya) delivering the majority decision of the Federal Court in *Lombard Commodities Ltd v Alami Vegetable Oil Products Sdn Bhd*<sup>4</sup> (“*Lombard*”):

[42] The next issue raised by the respondent is that the respondent was never a party to the arbitration agreement. In this regard I agree with the submission for the appellant that if that is so, it is for the respondent to apply to the English court, being the court having

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4 [2010] 1 CLJ 137.

supervisory jurisdiction, to have the award set aside instead of raising the issue before our court, which is merely an enforcement court.

[43] As observed by Coleman J in *A v B* [2007] 1 Lloyd's Report 358:

“... an agreement as to the seat of an arbitration is analogous to an exclusive jurisdiction clause. Any claim for a remedy going to the existence or scope of the arbitrator's jurisdiction or as to the validity of an existing interim or final award is agreed to be made only in the courts of the place designated as the seat of the arbitration.”

[44] In *Sabah Gas Industries Sdn Bhd v Trans Samudera Lines (S) Sdn Bhd* [1993] 3 CLJ 532, it was similarly held that a party who had been given every opportunity to submit and to take part in arbitration proceedings in London ought to have challenged the conduct of the arbitrator and/or validity of the award in the English courts and not here. Similarly in *Hebei Import & Export Corporation v Polytech Engineering Company Limited* FAC V No 10 of 1988 (Hong Kong), the Court of Final Appeal of Hong Kong held that a party may be precluded by his failure to raise a point before the court of supervisory jurisdiction from raising that point or issue before the court of enforcement.

[25] The selection of the seat of arbitration thus also amounts to a submission to the courts exercising jurisdiction over the seat of arbitration in matters pertaining to the validity of the award. Even though the decision in *Lombard* relates to the position under the repealed Convention on the Recognition and Enforcement of Foreign Arbitral Awards Act 1985 (which gave effect to the New York Convention and which was replaced by the AA 2005), the principle that an arbitral award may only be set aside in the jurisdiction of the courts exercising supervisory jurisdiction over the arbitration proceedings would still apply under the AA 2005.

[26] The reference to “an award” in section 37 must therefore be read to mean an award delivered pursuant to an arbitration the seat of which was located in Malaysia. An application cannot be made under section 37 to set aside a foreign arbitral award. An award debtor can only resist the enforcement of a foreign arbitral award in Malaysia by applying to set aside the order of court granting conditional recognition of the award, pursuant to section 39 of the AA 2005.

[27] As alluded to earlier in this article, the practical significance between an action to set aside an award and an action to set aside the court order granting recognition of the award will arise where the award creditor seeks to enforce an award against the award debtor across multiple jurisdictions. If the award debtor is successful in setting aside the award in the supervisory court, that would be the end of the matter, save for appeals against this decision of the supervisory court. Where however the award has not been set aside, the award creditor may seek to enforce the award in any jurisdiction where the award debtor has significant assets. The award debtor can resist the enforcement of the award in the enforcement courts, but even if it is successful in one jurisdiction, that does not prevent enforcement action being undertaken in any other jurisdiction where it may have significant assets.

[28] The case of *Dallah v Pakistan*<sup>5</sup> (“*Dallah*”) provides a good illustration of the application of these principles.

[29] In this case, the claimant was a Saudi Arabian company that had signed an agreement with a trust entity created under Pakistani laws to construct accommodation for Pakistani pilgrims to Mecca. This agreement contained an arbitration clause, by which disputes were to be referred to arbitration in Paris under the International Chamber of Commerce Rules of Arbitration.

[30] The housing project never materialised. Following a change in Government in Pakistan, the trust entity was also dissolved.

[31] *Dallah* commenced ICC arbitration proceedings in Paris against the Government of Pakistan, which was not a signatory to the original agreement. The arbitral tribunal<sup>6</sup> ruled that it had jurisdiction over the government (despite that it was not an original signatory) and awarded *Dallah* USD20 million in damages and legal costs. *Dallah* sought to enforce the awards in United Kingdom (“UK”). The government opposed the UK action to enforce the awards on the basis that the arbitration agreement was not valid under French law, and commenced separate proceedings in France to set aside the awards.

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5 [2010] UKSC 46.

6 Comprising three distinguished members, including the late Lord Mustill.

[32] The UK Supreme Court, applying French law, found that the government could not be considered as a party to the arbitration agreement and therefore the arbitrators did not have the requisite jurisdiction over the government.

[33] The Paris Court of Appeal,<sup>7</sup> however, also applying French law to the same facts, found that the government was the real party to the original agreement and that the use of the trust entity was a mere formality. Unfortunately for Dallah, the decision of the Paris Court of Appeal was delivered after the UK Supreme Court decision, and the latter court did not have the benefit of the grounds of judgment of the former court before delivering its decision.

[34] It is observed that the government of Pakistan had throughout the arbitration proceedings denied being a party to the original agreement and maintained a jurisdictional reservation.

[35] Even though Dallah was precluded from enforcing the arbitral awards in the UK, because the validity of the award was subsequently upheld by the Paris Court of Appeal, it may nonetheless still have proceeded to enforce the award in any jurisdiction where the government of Pakistan has significant assets. If the latter seeks to resist enforcement on grounds of the lack of jurisdiction of the arbitral panel, Dallah may argue that the issue is *res judicata*. An enforcement court would presumably defer to the views of the Paris Court of Appeal, applying French law, to the facts.

**Can an award debtor raise a challenge under section 39 in an enforcement court in Malaysia without first having applied to set aside the award in the supervisory courts?**

[36] The following paragraphs address the question whether an award debtor may raise a challenge in an enforcement court under section 39 without first having applied to set aside the award in the courts exercising supervisory jurisdiction over the arbitration proceedings.

[37] In *Sintrans Asia Services Pte Ltd v Inai Kiara Sdn Bhd*<sup>8</sup> (“*Sintrans*”), the defendant had chartered a dredging vessel from the plaintiff, but

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7 *Gouvernement du Pakistan – Ministère des Affaires Religieuses v Dallah Real Estate and Tourism Holding Co* (Case No 09/28533).

8 [2016] 5 CLJ 746.

had failed to make payment in accordance with the terms of the charter hire agreement. This agreement provided for disputes to be resolved by arbitration in Singapore in accordance with the Singapore Chamber of Maritime Arbitration. The plaintiff sent a notice of arbitration, but the defendant did not participate in its proceedings. The arbitrator subsequently awarded the sums claimed by the plaintiff. The defendant however did not make payment in satisfaction of the award, and hence the plaintiff commenced an originating summons pursuant to section 38 of the AA 2005 seeking the award to be recognised and enforced in Malaysia.

[38] The defendant sought to resist the recognition and enforcement of the foreign arbitral award on grounds that the arbitration agreement was void due to an action *in rem* commenced by the plaintiff before the Admiralty Court. As the defendant had not attended the arbitration proceedings conducted in Singapore, it did not raise any jurisdictional objections before the arbitrator, nor had the defendant commenced any action in Singapore (being the jurisdiction of the supervisory courts) to set aside the arbitral award.

[39] The Court of Appeal held that the defendant's failure to do so meant that it was too late in the day for the defendant to have raised the objections before the enforcement court in Malaysia, and that the proper avenue for challenges of this nature would be before the courts of Singapore.<sup>9</sup>

[40] The point may be made that the defendant in this case was not seeking to set aside the arbitral award in the Malaysian proceedings, but was merely resisting its recognition and enforcement pursuant to the provisions of section 39(1)(a)(ii) of the AA 2005. This was clearly something that it was entitled to do so, based on the plain words of section 39.

[41] In my view, the decision of the Court of Appeal does not mean that a jurisdictional challenge can only be made by an application to set aside the award in the court exercising supervisory jurisdiction. Rather, the absence of any challenge in the seat of arbitration will mean that any section 39 challenge in Malaysia will, or will likely, fail for want of proof.

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<sup>9</sup> See paras 12 and 13 of the judgment of the Court of Appeal.

[42] If an award debtor seeks to challenge the recognition and enforcement of a foreign arbitral award under section 39 on grounds, for example, of the invalidity of the arbitration agreement, it must first show that it had raised the jurisdictional objection before the arbitrator and had commenced an action in the jurisdiction of the seat of the arbitration to set aside the award. The failure of the award debtor to have done so means that it would have failed to “provide proof to the High Court” of the fact of the invalidity of the arbitration agreement. In other words, these are the threshold matters that the award debtor must first establish, in order to be able to prove the existence of any of the matters set out in section 39(1)(a).

[43] The case of *Dallah* provides an excellent illustration that an award debtor can validly resist the recognition and enforcement of an award in the enforcement courts, which is what the defendant had sought to do in the case of *Sintrans*. The crucial distinction was that the government of Pakistan had registered its objection against the jurisdiction of the arbitral panel in the arbitration proceedings in Paris, and had also commenced an action in the Paris courts to set aside the award, even though the decision of the Paris Court of Appeal had not yet been delivered by the time the UK Supreme Court decided to uphold the government of Pakistan’s challenge. In *Sintrans*, however, the defendant had not participated in the arbitration proceedings at all, and had not commenced any action in Singapore to set aside the award.

[44] The Court of Appeal in its earlier decision in the case of *Agrovenus LLP v Pacific Inter-Link Sdn Bhd*<sup>10</sup> arrived at the same result, but applied the doctrine of estoppel to prevent the award creditor from resisting the recognition and enforcement of a foreign arbitral award. In this case, the award debtor had agreed to sell palm olein and kernel oil to the award creditor. A dispute arose as to whether the award debtor had orally agreed to a discount, and the award creditor commenced arbitration proceedings in connection with this dispute. The arbitral panel delivered an award in favour of the award creditor.

[45] The award creditor applied under section 38 for the award to be recognised and enforced in Malaysia against the award debtor. The latter resisted the originating summons, contending that the arbitrator

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10 [2014] 1 AMCR 329; [2014] 4 CLJ 525.

lacked jurisdiction to determine the issue in dispute. However, this jurisdictional objection was raised for the first time at the High Court in Malaysia. In addition, no explanation was provided as to why the objections were not raised before the arbitral tribunal.

[46] The Court of Appeal found that it was not open for the award debtor to have fully participated in the arbitration while keeping up its sleeve the jurisdictional objection, to be used in the event that the award went against it. The court held:

... the fact of failure to object at the proceedings before the arbitral tribunal and thus causing all the parties to act on the basis the respondent accepted that the arbitral tribunal had jurisdiction or scope certainly does not commend itself to an exercise of discretion in favour of the respondent to refuse recognition or enforcement of the award. It calls properly for the application of the doctrine of estoppel as enunciated in *Bousted Trading (1985) Sdn Bhd v Arab Malaysian Merchant Bank Bhd* [1995] 3 AMR 2871; [1995] 3 MLJ 331.

[47] An important practical consideration arises as a consequence. If the Malaysian courts require that the validity of the award be first challenged in the supervisory courts, because proceedings would be extant in the supervisory courts, it would appear to be reasonable for the Malaysian proceedings be stayed until the supervisory court makes a determination on the application to set aside the arbitral award. This would avoid multiple proceedings being conducted in different courts to determine the same issue based on the same facts, and applying the law of the supervisory court as the curial law. It would also avoid the situation where the enforcement court arrives at a different conclusion from the supervisory court, as was the case in *Dallah*.

[48] Further complications could arise if the parties had selected another law other than the law of the jurisdiction of the seat of arbitration as the governing law of the arbitration agreement. Thus, if the law governing the arbitration agreement is specified as English law, with the seat of arbitration in Singapore, any challenge to set aside the arbitral award must take place before the courts of Singapore, applying English law. A challenge to resist enforcement in Malaysia will require the Malaysian courts to also apply English law, although (as explained above) since the Malaysian position appears to require a challenge to have been made in the supervisory court first, parties

would appear to be justified to request for a stay of the Malaysian action pending disposal of the action in the supervisory court.

[49] In conclusion, an award debtor who makes an application under section 39 to challenge the recognition and enforcement of a foreign arbitral award must have raised its objections before the arbitral tribunal (unless of course the contention was that it had never received notice of the arbitral proceedings) and ought to have commenced proceedings in the jurisdiction of the supervisory court to set aside the arbitral award. Where one or both of these matters have not been done, cogent reasons must be given to explain why.

[50] Courts hearing a section 39 application in connection with a foreign arbitral award may well have to apply the governing law of the arbitration agreement to determine issues related to the validity and scope of the arbitration agreement. This law would be the law of the seat of the arbitration, unless the parties had specified some other governing law. The court may also have to consider whether it would be appropriate in the circumstances to stay proceedings pending the outcome of the setting aside proceedings in the supervisory court. Whether such a stay ought to be ordered will be dependent on the facts of each case, and would take into account considerations such as the anticipated time required to dispose of the setting aside application and to exhaust appeals from such a decision.

# Cyber Defamation in Malaysia: An Overview

by

Justice Mohamed Zaini bin Mazlan\*

*“The remedy for speech that is false is speech that is true. This is the ordinary course in a free society. The response to the unreasoned is the rational; to the uninformed, the enlightened; to the straight-out lie, the simple truth.”*

The Supreme Court of the United States in *The United States v Xavier Alvarez* (2012) 132 S Ct 2537 at 2550

## Introduction

[1] The right to freedom of speech and expression is a very important and basic right deserving protection. It is indeed essential to any healthy democratic country. But that right is not absolute. There cannot be any liberty uncontrolled in operation so as to confer a right wholly free from any restraint. Had there been no restraint, the rights and freedoms may become synonymous with anarchy and disorder.<sup>1</sup>

[2] In Malaysia, the right to freedom of speech and expression is guaranteed by Article 10(1) of the Federal Constitution. While it is protected under the supreme law of the land, Parliament may under Article 10(2)(a) by law impose on these rights such restrictions as it deems necessary or expedient in the interest of the security of the Federation or any part thereof, friendly relations with other countries, public order or morality and restrictions designed to protect the privileges of Parliament or of any Legislative Assembly or to provide against contempt of court, defamation, or incitement to any offence. Article 10(4) further states that in imposing restrictions in the interest of the security of the Federation or any part thereof or public order under clause (2)(a), Parliament may pass law prohibiting the questioning of any matter, right, status, position, privilege, sovereignty or prerogative established or protected by the provisions of Part III, Article 152, 153

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\* Judge of the High Court of Malaya.

1 *In Re Ramlila Maidan Incident Dt 4/5/6.2011 v Home Secretary, Union of India & Ors* [2012] 3 MLJ 443, SC.

or 181 otherwise than in relation to the implementation thereof as may be specified in such law.

[3] Raja Azlan Shah J (as His Royal Highness then was) while discussing the constitutionality of the Sedition Act 1948 (Act 15) in *PP v Ooi Kee Saik & Ors*<sup>2</sup> had this to say:

It is of course true, as a general statement, that the greatest latitude must be given to freedom of expression. It would also seem to be true, as a general statement, that free and frank political discussion and criticism of government policies cannot be developed in an atmosphere of surveillance and constraint. But as far as I am aware, *no constitutional state has seriously attempted to translate the "right" into an absolute right*. Restrictions are a necessary part of the "right" and in many countries of the world freedom of speech and expression is, in spite of formal safeguards, seriously restricted in practice. In the United States all types of speech "can claim no talismanic immunity from constitutional limitations. It must be measured by standards that satisfy the First Amendment." (See *New York Times Co v Sullivan* 376 US 255 (1964)). The Supreme Court of India too has conceded that fundamental rights are subject to limitations in order to secure or promote the greater interests of the community.

(Emphasis added.)

[4] The same view was also shared by Eusoff Chin CJ (as he then was) in *Ling Wah Press (M) Sdn Bhd & Ors v Tan Sri Dato Vincent Tan Chee Yioun*<sup>3</sup> when His Lordship was of the view that:

Freedom of speech is not a licence to defame people. It is subject to legal restrictions. An absolute or unrestricted right to free speech would result in persons recklessly maligning others with impunity, and the exercise of such right would do the public more harm than good. Every person has a right to reputation and that right ought to be protected by law – *Jeyaretnam Joshua Benjamin v Lee Kuan Yew & Anor* [1992] 2 SLR 310 at p 332.

### Malaysia and the Internet

[5] The Internet is the world's largest interconnected environment. Access is now no longer limited to the selected few. Now anyone can

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2 [1971] 2 MLJ 108.

3 [2000] 3 AMR 2991; [2000] 4 MLJ 77.

publish his or her thoughts, even anonymously. Information is now communicated globally in nanoseconds through the Internet. Gone are the days when only a select few would have their work or thoughts published, or have access to them. The Internet has provided a new means of expression.

[6] The history of the Internet in Malaysia broadly reflects its development in the United States (“US”) and other countries. It started with the creation of the Advanced Research Projects Agency (“ARPA”) in 1958 by the then US President Eisenhower. The US had the jitters when it saw evidence of Soviet technological advancement with the launch of the Russian satellite Sputnik. ARPA was thus the US response to the Russians. ARPA put in place a computer network linkage with only four computers and it named the network “ARPANET”. Over the years, work began to link ARPANET computers through radio and the connection also developed to include satellite communications. The connections between multiple networks was called inter-networking, or for convenience, the Internet. In other words, the Internet is simply a network of networks. The creation of the service which enables the networks to be accessible was just as important. This was called the World Wide Web (“WWW”).

[7] The beginnings of Malaysia’s Internet began in 1988. At that time the Malaysian Institute of Microelectronic Systems (“MIMOS”) set up a university computer network called *Rangkaian Komputer Malaysia* (Malaysian Computer Network). In the beginning it had four dial-up lines, but they were costly. In 1992, these were replaced by a satellite link to the US and Malaysia obtained firm connection to the Internet. MIMOS then set up the Joint Advanced Integrated Networking (“JARING”) as an Internet service provider (“ISP”). Several other improvements took place and the Internet has not looked back since.

[8] As Malaysia moves towards its aspiration of becoming a developed nation by the year 2020, the Malaysian Government initiated a range of Information and Communication Technology (“ICT”)-related policies to stay competitive in an increasingly globalised environment. An important aspect of ICT is the development of the Multimedia Super Corridor (“MSC”) which is a high-profile project. The project has since gained ground. The main aim of the MSC is to create a top-notch technological environment which would ensure Malaysia’s progress into a knowledge-based society, by attracting gilt-edged companies.

## The Internet and the “bullies”

[9] In order to foster an environment where MSC status companies are provided the best opportunities to flourish, the Government of Malaysia allows them the protection of the MSC Malaysia Bill of Guarantees (“BoGs”). One of the guarantees is that there will be no censorship of the Internet.<sup>4</sup> This assurance was also embodied in section 3(3) of the Communications and Multimedia Act 1998 which states that: “Nothing in this Act shall be construed as permitting the censorship of the Internet.” This “no censorship policy” has indeed appealed to a large number of high-end technology companies which came in droves. This after all, was the main objective of the MSC. On the downside, it has, however, fascinated and attracted unscrupulous Internet users who are out to exploit these digital platforms in the name of freedom of speech and expression by way of cyber defamation.

## Cyber defamation: position in Malaysia

[10] Defamation is the publication of an untrue statement of another, which tends to lower the latter’s reputation in the eyes of the right-thinking public. Libel consists of defamatory statements made in a permanent form, whereas slander consists of those made in a transient form.

[11] Cyber defamation is, quite simply, the publication of defamatory statements through the Internet. In Malaysia, defamation can be subject to civil or criminal proceedings.

### *Civil defamation*

[12] The Malaysian Defamation Act 1957 (“the Act”) has not seen any amendments to adapt to the changes precipitated by the Internet. In particular, the Act does not state whether publications of defamatory statements online should be treated as “publication in a permanent form” so as to amount to libel.<sup>5</sup>

[13] Section 3 of the Act provides that “for the purpose of the law of libel and slander, the *broadcasting of words by means of radio*

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4 “Bill of Guarantees”, MSC Malaysia, <https://www.mdec.my/msc-malaysia/bill-of-guarantees>.

5 *Dato’ Seri S Samy Vellu v Penerbitan Sahabat (M) Sdn Bhd & Ors (No. 2)* [2005] 5 MLJ 539 at [10]-[11].

*communication* shall be treated as publication in a permanent form.” (Emphasis added.)<sup>6</sup> This can be contrasted with the wider formulation in the statutory provisions in Singapore and the United Kingdom (“UK”), where the types of communications treated as publications in a permanent form are broad enough to include online communications:

- (i) The Singapore Defamation Act provides that the “broadcasting of words by means of telecommunication” shall be treated as publication in a permanent form (section 3). “Telecommunication” is defined broadly to include “any system for the transmission, emission or reception of signs, signals, writings, images and sounds of all kinds by means of radiowaves, wire, cable or other electro-magnetic systems” (section 2); and
- (ii) The UK Broadcasting Act 1990 provides that “the publication of words in the course of any programme included in a programme service” shall be treated as publication in a permanent form (section 166). “Programme service” is also defined broadly, encompassing any service which consists of the sending, by means of a telecommunication system, of sounds and/or visual images (section 201).

[14] In the absence of a clear deeming provision in the Act, one must apply common law principles to determine whether online statements are to be treated as publications in a permanent form. Interestingly, “the question whether Internet communications amount to libel and slander appear to have attracted comparatively little attention in the case law”.<sup>7</sup> Blog posts have been regarded as amounting to libel in a number of cases.<sup>8</sup> In the UK, a posting on an internet forum<sup>9</sup> and a tweet<sup>10</sup> have been dealt with as libel. The classification of the

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6 The term “broadcasting by means of radio communication” is defined in s 2 of the Act as “publication for general reception by means of a radio communication within the meaning of the Telecommunications Act 1950 ...” The Telecommunications Act 1950 has since been repealed by the Communications and Multimedia Act 1998. Curiously, unlike its predecessor, the Communications and Multimedia Act 1998 does not contain a provision to define “radio communication”.

7 A Mullis, R Parkes, *Gatley on Libel and Slander*, 12th edn (London: Sweet & Maxwell, 2017).

8 *Datuk Seri Utama Dr Rais bin Yatim v Amizudin bin Ahmat* [2012] 2 AMR 266; [2012] 2 MLJ 807; *New Straits Times Press (M) Bhd v Ahirudin bin Attan* [2007] AMEJ 0195; [2008] 1 MLJ 814; see also *Lee Hsien Loong v Ngerng Yi Ling Roy* [2016] 1 SLR 1321

9 *Godfrey v Demon Internet Ltd* [2001] QB 201.

10 *Cairns v Modi* [2012] EWCA Civ 1382.

communications as libel or slander was, however, not argued as an issue in these cases.

[15] Given the variety of forms and platforms for online communications, such communications may be differentiated based on their nature to determine whether they constitute publication in a permanent form. It has been suggested that contents which require downloading onto a device to be read (such as emails, blog posts, and instant written chats) ought to be properly classified as libel, whereas transient audio or audio-visual communications (such as video-conferences and online audio calls) are likely to be classified as slander.<sup>11</sup>

[16] The Act, however, does not have a single definition of what defamation is. As has been said above, it has not been amended to keep pace with changes brought on by the Internet.

#### *Malaysian Penal Code (Act 574)*

[17] In Malaysia, Chapter XXI of the Malaysian Penal Code (Act 574), and in particular sections 499 to 502, provide an opportunity to the victim to lodge a criminal complaint for defamation against an accused. Under section 499, criminal defamation is defined as “Whoever, by words either spoken or intended to be read or by signs, or by visible representations, makes or publishes any imputation concerning any person, intending to harm, or knowing or having reason to believe that such imputation will harm the reputation of such person, is said, except in the cases hereinafter excepted, to defame that person.” It is a compoundable offence and the punishment for the guilty person is imprisonment for a term which may extend to two years or a fine, or both.

#### *Communications and Multimedia Act 1998 (Act 588)*

[18] The Communications and Multimedia Act 1998 (Act 588) (“CMA”) is another piece of legislation relating to cyber industries and technologies. It was enacted on April 1, 1999 as a result of the MSC project, providing for and to regulate the converging communications and multimedia industries, and for incidental matters.<sup>12</sup> The Malaysian

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11 D Chia, *Defamation: Principles and Procedure in Singapore and Malaysia* (Singapore: LexisNexis, 2016).

12 Long title and preamble of the CMA. See also s 3 for the objects of the Act.

Communications and Multimedia Commission (“MCMC”) was formed to implement the CMA.

[19] In regulating online content, section 211(1) of the CMA provides that “No content applications service provider, or other person using a content applications service, shall provide content which is indecent, obscene, false, menacing, or offensive in character with intent to annoy, abuse, threaten or harass any person.” By virtue of section 211(1), any person who contravenes the aforesaid provision commits an offence and shall, on conviction, be liable to a fine not exceeding RM50,000 or to imprisonment for a term not exceeding one year or to both and shall also be liable to a further fine of RM1,000 for every day or part of a day during which the offence is continued after conviction.

[20] For those who, among others, use network facilities or network services to transmit any communication that is deemed to be offensive and can cause annoyance to another person, they will be criminalised under section 233 of the CMA. The provision in full reads as follows:

233. *Improper use of network facilities or network service, etc.*

(1) A person who –

(a) by means of any network facilities or network service or applications service knowingly –

(i) makes, creates or solicits; and

(ii) initiates the transmission of,

any comment, request, suggestion or other communication which is obscene, indecent, false, menacing or offensive in character with intent to annoy, abuse, threaten or harass another person; or

(b) initiates a communication using any applications service, whether continuously, repeatedly or otherwise, during which communication may or may not ensue, with or without disclosing his identity and with intent to annoy, abuse, threaten or harass any person at any number or electronic address,

commits an offence.

- (2) A person who knowingly –
  - (a) by means of a network service or applications service provides any obscene communication for commercial purposes to any person; or
  - (b) permits a network service or applications service under the person's control to be used for an activity described in paragraph (a),commits an offence.
- (3) A person who commits an offence under this section shall, on conviction, be liable to a fine not exceeding fifty thousand ringgit or to imprisonment for a term not exceeding one year or to both and shall also be liable to a further fine of one thousand ringgit for every day during which the offence is continued after conviction.

[21] This provision was firstly used to charge six bloggers for insulting the Sultan of Perak in relation to the Perak Crisis in March 2009.

[22] There were however some controversies over the use of the said provision. The Malaysian Bar called it as “a serious encroachment on the freedom of speech and expression” and insisted that the government cease the use of section 233(1)(a) of the Act. Steven Thiru, in a press release dated December 21, 2015,<sup>13</sup> said:

The continuous use of section 233(1)(a) of the CMA to clamp down on views, discourse and expression, and to restrict democratic space, creates a climate of fear that threatens to silence Malaysians. Section 233(1)(a) suffocates not only freedom of expression and freedom of speech in Malaysia, but more critically, freedom of thought. In this age of connectivity, where the exchange of ideas and information is rife, no nation that aspires to be recognised and accepted as a world leader in ideas and intellectualism can afford to raise an unquestioning and non-discerning population.

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13 Press release on the “Misuse of the Communications and Multimedia Act 1998 to Stifle Freedom of Speech and Expression Must End”, [http://www.malaysianbar.org.my/press\\_statements/press\\_release\\_%7C\\_section\\_2331a\\_of\\_the\\_communications\\_and\\_multimedia\\_act\\_1998\\_creates\\_a\\_chilling\\_effect\\_on\\_freedom\\_of\\_speech\\_and\\_expression\\_and\\_should\\_be\\_repealed.html](http://www.malaysianbar.org.my/press_statements/press_release_%7C_section_2331a_of_the_communications_and_multimedia_act_1998_creates_a_chilling_effect_on_freedom_of_speech_and_expression_and_should_be_repealed.html).

[23] The statement was made in view of the arrests, investigation and charges made by the authorities against several persons and entities.<sup>14</sup>

[24] Article 19,<sup>15</sup> on their Legal Analysis on the Communications and Multimedia Act 1998's report, was of the view that the two provisions mentioned above are amongst the most problematic provisions from the human rights perspective and had urged the Malaysian Government to urgently amend them. In view of a number of overly broad content-related offences, the following recommendations were put forward in the said report:

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- 14 (1) Radio journalist Aisyah Tajuddin and two of her colleagues were investigated on March 23, 2015 for her alleged appearance in a video posted online, entitled "Hudud Isi Periuk Nasi? (Kupas)";
- (2) *The Malaysian Insider* ("TMI") managing editor Lionel Morais, Bahasa Malaysia news editor Amin Shah Iskandar, and features and analysis editor Zulkifli Sulong were arrested on March 30, 2015; and chief executive Jahabar Sadiq and group CEO of The Edge Media Group (which owns TMI) Ho Kay Tat were arrested on March 31, 2015, for allegedly publishing a news report that claimed the royal institution had opposed the amendment of the Federal Constitution to enable *hudud* laws to be implemented;
- (3) Whistleblower website *Sarawak Report* was investigated, and access to it blocked, in July 2015 for allegedly publishing unverified information relating to the Prime Minister and 1MDB;
- (4) Political analyst Shahbudin Husin was investigated on September 29, 2015 for allegedly posting a comment piece entitled "Kenapa lawatan rasmi Zahid ke Indonesia sama tarikh dengan majlis sanding anaknya di Jakarta?";
- (5) Former Chief Minister of Malacca Tan Sri Abdul Rahim Thamby Chik was charged on October 5, 2015 for allegedly posting an item on his Facebook account concerning the Selangor Raja Muda;
- (6) Parti Sosialis Malaysia Secretary-General S Arutchelvan was charged on November 23, 2015 for allegedly criticising the Court of Appeal's decision against the then Opposition leader Anwar Ibrahim in a Facebook post;
- (7) Activist Khalid Mohd Ismath was charged on November 13, 2015 for making allegedly seditious online posts regarding the Johore royalty;
- (8) Former Minister in the Prime Minister's Department Dato' Zaid Ibrahim was charged on December 3, 2015 for the alleged offence of publishing the transcript of a speech that he delivered at the Royal Selangor Club on his blog. The blog post, entitled "Rally Behind Tun Dr Mahathir Mohammad", called for the removal of the Prime Minister; and
- (9) "Letak Jawatan" Facebook page administrator Joe Haidy Sulaiman was investigated on December 4, 2015 for allegedly defaming the Prime Minister in a Facebook post.
- 15 A British Human Rights Organization named after the article in the Universal Declaration of Human Rights that protects free expression.

#### Recommendations for section 211:

- Section 211 should be thoroughly revised to more narrowly and precisely define what qualifies as prohibited content under the Act, in line with the three-part test under international law;
- Distinction should be made between private communications and content that is publicly available; the former should be explicitly excluded from the scope of the Act;
- The liability of online intermediaries under the Act should be clarified. Service providers should not be held criminally liable for content produced by others; instead, they should be granted immunity from liability.

#### Recommendations for section 233:

- Section 233 should be thoroughly revised to more narrowly and precisely define what constitutes “improper use of network facilities or services” under the Act;
- Section 233(1)(b) should be thoroughly revised to narrowly define the circumstances under which anonymous speech can be penalised under the Act;
- Section 233(2) should more precisely and narrowly define what constitutes “obscene” communication and raise the threshold for liability of intermediaries to one of actual and specific knowledge of illegal use of their facilities.<sup>16</sup>

[25] Since the passage of this Act, there have been attempts to challenge the constitutionality of the said legislation. In the latest case, the High Court at Kuala Lumpur on January 4, 2018 heard an application by R Sivarasa on whether the Federal Court should determine if a provision in the CMA is in breach of the right to freedom of speech and expression. The High Court dismissed the application.

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<sup>16</sup> The full text of the report can be viewed at file:///I:/research/CJ/cyber%20defamation/Malaysia-analysis-Final-December.pdf.

## Online intermediaries

[26] Online intermediaries are organisations that facilitate the use of the Internet, such as Internet service providers (“ISPs”), search engines and social media platforms. Online intermediaries generally perform as conduits such as channels, caches (supplies/stores) or information hosts on the Internet. They are classified into connectivity intermediaries (such as ISPs), navigation intermediaries (such as Google and commercial and social networking providers) and other hosts (such as Wikipedia, Facebook, Twitter and blogs), amongst others. The intermediaries are easily identifiable, and are important features in legal proceedings.

### The liability of online intermediaries

#### *In the United Kingdom (“UK”)*

[27] The previous Defamation Act 1996 did not make any specific provisions. Under section 1 of the Act, ISPs in England were liable for defamation by third parties if they were notified but failed to remove the posts promptly.

[28] A case in point is *Tamiz v Google Inc.*<sup>17</sup> Mr Tamiz was a local politician who was aggrieved with some comments concerning him that appeared in a blog called “London Muslim”. Rightfully so, as he was accused of being a drug dealer and a thief, as well as being hypocritical towards women. Google Inc was sued in its capacity as the operator of Blogger.com. The identities of the commenters were unknown, as they had posted their comments anonymously. Mr Tamiz had prior to commencing the suit, notified Google Inc of the defamatory comments. Google Inc did remove the posts, but it was not done expeditiously, hence the suit. The Court of Appeal held that Google Inc is deemed as a publisher, as it had allowed the defamatory posts to remain, or at least is deemed to have been associated with the comments.

[29] The UK Defamation Act has since been amended and is now known as the Defamation Act 2013 (“DA 2013”). Provisions have now been incorporated to provide protection for online publishers, most notably under sections 5 and 10 of the DA 2013. Section 5 is as follows:

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17 [2013] EWCA Civ 68.

### 5. *Operators of websites*

- (1) This section applies where an action for defamation is brought against the operator of a website in respect of a statement posted on the website.
- (2) It is a defence for the operator to show that it was not the operator who posted the statement on the website.
- (3) The defence is defeated if the claimant shows that –
  - (a) it was not possible for the claimant to identify the person who posted the statement,
  - (b) the claimant gave the operator a notice of complaint in relation to the statement, and
  - (c) the operator failed to respond to the notice of complaint in accordance with any provision contained in regulations.
- (4) For the purposes of subsection (3)(a), it is possible for a claimant to “identify” a person only if the claimant has sufficient information to bring proceedings against the person.
- (5) Regulations may –
  - (a) make provision as to the action required to be taken by an operator of a website in response to a notice of complaint (which may in particular include action relating to the identity or contact details of the person who posted the statement and action relating to its removal);
  - (b) make provision specifying a time limit for the taking of any such action;
  - (c) make provision conferring on the court a discretion to treat action taken after the expiry of a time limit as having been taken before the expiry;
  - (d) make any other provision for the purposes of this section.
- (6) Subject to any provision made by virtue of subsection (7), a notice of complaint is a notice which –
  - (a) specifies the complainant’s name,
  - (b) sets out the statement concerned and explains why it is defamatory of the complainant,

- (c) specifies where on the website the statement was posted, and
  - (d) contains such other information as may be specified in regulations.
- (7) Regulations may make provision about the circumstances in which a notice which is not a notice of complaint is to be treated as a notice of complaint for the purposes of this section or any provision made under it.
- (8) Regulations under this section –
- (a) may make different provision for different circumstances;
  - (b) are to be made by statutory instrument.
- (9) A statutory instrument containing regulations under this section may not be made unless a draft of the instrument has been laid before, and approved by a resolution of, each House of Parliament.
- (10) In this section “regulations” means regulations made by the Secretary of State.
- (11) The defence under this section is defeated if the claimant shows that the operator of the website has acted with malice in relation to the posting of the statement concerned.
- (12) The defence under this section is not defeated by reason only of the fact that the operator of the website moderates the statements posted on it by others.

**[30]** Section 5 provides defences for intermediaries, namely website operators. In essence, they would not be liable for postings done by third parties, provided that:

- (a) The third party can be identified by the claimant;
- (b) The operator has not received a notice of complaint;<sup>18</sup> or
- (c) The operator takes down the post/comments upon receiving the notice of complaint or provides the claimant with the details of the third party.

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18 Provisions for the notice are set out under the Defamation (Operators of Websites) Regulations 2013.

[31] The defence however is defeated, if the criterion under section 5(3) is satisfied, or if the operator had acted with malice in respect of the posting. Malice for instance could be inferred if it can be shown that the operator had encouraged it. It is now incumbent upon an operator to take steps upon receiving a notice from the complainant, if it intends to rely on the defences provided under the section.

[32] Section 10 of the DA 2013 on the other hand is more relevant for ISPs:

10. *Action against a person who was not the author, editor etc.*

- (1) A court does not have jurisdiction to hear and determine an action for defamation brought against a person who was not the author, editor or publisher of the statement complained of unless the court is satisfied that it is not reasonably practicable for an action to be brought against the author, editor or publisher.
- (2) In this section “author”, “editor” and “publisher” have the same meaning as in section 1 of the Defamation Act 1996.

The court will lack the jurisdiction to hear and dispose of a defamation action that is brought against a non-author, editor or publisher of the complained content, unless the court is satisfied that such action could not reasonably be taken against the author, editor or publisher of the content. In any event, the usual defences available under the tort of defamation are provided for under the DA 2013, such as truth,<sup>19</sup> honest opinion<sup>20</sup> and publication on matters of public interest.<sup>21</sup>

### *In Malaysia*

[33] The case of *Kho Whai Phiaw v Chong Chieng Jen*<sup>22</sup> provides an interesting insight on how the court has dealt with the liability of bloggers for third-party content, although the case was not for a defamation suit. The petitioner in that case had presented a petition to the Election Court, to declare the respondent’s victory in the Parliamentary election as void for undue influence. The respondent was claimed to have exerted undue influence by publishing or allowing to

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19 Section 2.

20 Section 3.

21 Section 4.

22 [2009] 4 MLJ 103, HC.

be published on his blog named “Chong Chieng Jen’s Blog”, an article written by a Mr Smith, which was said to have contained threatening statements towards the voters. It was alleged by the petitioner that since the respondent had absolute control over his blog entries, as he could moderate, limit, edit and delete posts or comments on his blog, he should then be liable for the publication, as he would have had knowledge or consented to the article being posted on his blog. The High Court disagreed and held that there was insufficient evidence to prove that the person who had posted the article had any relationship with the respondent, and deemed the former as a stranger. Nonetheless, the court ruled that the respondent could not be regarded as the publisher of Mr Smith’s article, since there was no sufficient evidence to prove that Mr Smith’s article was posted on the respondent’s blog with his knowledge or consent.

[34] The High Court also placed the burden on the petitioner to prove that the respondent had knowledge of the post, and that the respondent had consented to it being posted on his blog. Although the respondent had control over his blog, the court held that the petitioner had failed to prove that the respondent had actual knowledge of the post during the material time, i.e. before the polling date. The court took the view that mere speculation that the respondent knew of the post and could have done something about it was insufficient to attribute actual knowledge on the respondent.

[35] Although the case was eventually heard on appeal to the Federal Court, the apex court chose not to disturb the findings of fact made by the High Court. The case laid down the criteria that knowledge must be proven if online intermediaries are to be liable as publishers of third-party contents.

[36] The situation in Malaysia has since changed with the newly inserted section 114A of the Evidence Act 1950 (Act 56) (“EA 1950”).

### **Section 114A – Presumption of fact in publication**

[37] Unlike the print media, the Internet is capable of camouflaging or providing anonymity to anyone. One of the many obstacles that an aggrieved person faces is identifying the perpetrator. Getting the Internet Protocol (“IP”) address of the perpetrator is one of the conventional ways of tracking, as every machine be it a computer, server or even a mobile phone, has an IP address exclusive to it. ISPs assign a unique IP address to each user account. One of the hurdles

to getting the IP address is if the server storing the address is located abroad and owned by foreign entities. One will then need to initiate a suit in that particular country to compel the relevant ISP to reveal the IP address.

[38] Section 114A of the EA 1950 was incorporated by the Evidence (Amendment) (No. 2) Act 2012 on July 31, 2012. The section reads as follows:

- (1) A person whose name, photograph or pseudonym appears on any publication depicting himself as the owner, host, administrator, editor or sub-editor, or who in any manner facilitates to publish or re-publish the publication is presumed to have published or re-published the contents of the publication unless the contrary is proved.
- (2) A person who is registered with a network service provider as a subscriber of a network service on which any publication originates from is presumed to be the person who published or re-published the publication unless the contrary is proved.
- (3) Any person who has in his custody or control any computer on which any publication originates from is presumed to have published or re-published the content of the publication unless the contrary is proved.
- (4) For the purpose of this section –
  - (a) “network service” and “network service provider” have the meaning assigned to them in section 6 of the Communications and Multimedia Act 1998 [Act 588]; and
  - (b) “publication” means a statement or a representation, whether in written, printed, pictorial, film, graphical, acoustic or other form displayed on the screen of a computer.”

[39] With this amendment, one is presumed to be the publisher of the contents of the publication concerned, if his name, photograph or pseudonym appears in the publication representing himself as the owner, host, administrator, editor or sub-editor, or who in any manner facilitates such publication. One is also presumed to be the publisher, if the publication originated from the network service that he is registered with, or from the computer where the publication originated. It is notably a far easier task than having to procure the IP address. In gist, the burden is imposed on the person to rebut the

presumption that he was the publisher once any of the elements under the section has been satisfied.

[40] In *Tong Seak Kan & Anor v Loke Ah Kin & Anor*,<sup>23</sup> the plaintiffs sued the defendant for a defamatory post that had appeared on two blogs. The plaintiff went through an arduous route to obtain the identity of the defendant. He had firstly commenced a suit in the USA against Google Inc to obtain the IP addresses, and subsequently commenced a suit against Telekom Malaysia and TM Net (the network service providers) to trace the owner of the IP addresses. Only then could the plaintiff commence a defamation suit against the defendant. The plaintiff managed to obtain a judgment in default against the defendant. The defendant in making the application to set aside the judgment, claimed that he was not the owner of the two blogs, and that he had nothing to do with the publication.

[41] In rejecting the defendant's application to set aside the judgment in default, the High Court referred to section 114A(2) of the EA 1950, and held that the defendant is presumed to be the author of the publication. The court further held that the burden lay on the defendant to provide evidence, and prove on a balance of probability that he was not the author. The court was not convinced as the defendant had merely denied being the owner of the two blogs, without adducing sufficient evidence to substantiate his denial. Interestingly, the court there also held that section 114A of the EA 1950 can be applied retrospectively. The same view was taken by the High Court in *Kangaie Agilan all Jammany v Pendakwa Raya*.<sup>24</sup> This retrospective stand however was not followed in *PP v Rutinin Suhaimin*<sup>25</sup> where the High Court held that section 114A does not apply retrospectively.

[42] Another case that emphasised the effect of section 114A of the EA 1950 is the Court of Appeal's decision in the case of *YB Dato' Hj Husam Hj Musa v Mohd Faisal Rohban Ahmad*.<sup>26</sup> The appellant's defamation suit against the respondent was for an article entitled "Husam dan Tamrin Balun Balak 15 Juta" published through a BlogSpot called [ruangbicarafaisal.blogspot.com](http://ruangbicarafaisal.blogspot.com). The respondent however denied writing the article and owning the said BlogSpot. The trial judge,

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23 [2014] 3 AMR 572; [2014] 6 CLJ 904, HC.

24 [2017] MLJU 1647, HC.

25 [2013] 2 CLJ 427, HC.

26 [2015] 2 AMR 296; [2015] 1 CLJ 787, CA.

without considering section 114A of the EA 1950, held that the appellant had failed to establish that the respondent was the writer in the blog and dismissed the suit.

[43] On appeal, the Court of Appeal reversed the High Court's decision, and held that the High Court should have relied on section 114A of the EA 1950, and in doing so should have accepted the evidence proffered by the appellant to link the blog to the respondent. The appellate court reiterated the position that the burden then fell on the respondent to prove that he was not the publisher, and that a mere denial was insufficient.

[44] In *Stem Life Bhd v Mead Johnson Nutrition (M) Sdn Bhd & Anor*,<sup>27</sup> the plaintiff successfully sued the first defendant over some defamatory posts that were published in a forum hosted on the first defendant's website. The High Court, in allowing the plaintiff's claim, held that the first defendant was liable as a publisher as it had editorial control over the forum and had failed to rebut the presumption under section 114A of the EA 1950.

#### **Analysis of section 114A of the Evidence Act 1950 (Act 56)**

[45] Section 114A has made it easier for the authorities, or persons aggrieved with postings done through the Internet, to identify the alleged perpetrator. For instance, one can be deemed as the publisher by the mere fact that the posting was done through his computer, which by its definition includes mobile devices. This presumption however does not automatically result in the person accused being guilty of any cybercrime or liable for defamation. The onus is still on the party resorting to this section, to prove the necessary ingredients of the charge concerned or the alleged defamation.

[46] Nevertheless, the onus is firstly on the person accused to prove that he did not publish the offending article. In any event, any presumption is rebuttable and does not take away the burden on the party wishing to rely on the presumption to firstly establish the facts that entitle it to rely on the presumption. Although section 114A of the EA 1950 has been in force since 2012, there have not been many cases, be it civil or criminal, that have dealt with this section extensively.

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27 [2014] AMEJ 1402; [2013] MLJU 1582, HC.

### Publication rule (single or multiple)

[47] Publication is one of the crucial criteria required to establish a claim for defamation. In the paperless world of the Internet, a posting can be published multiple number of times. This would mean that a new and separate cause of action is created each time a posting is published. Under the single publication rule, the posting is considered published as soon as it was posted, and that the limitation period starts to run from that period.

[48] The multiple publication rule has been criticised for its unsuitability in the modern world. Due to the fact that posts can be uploaded to the Internet in an instant and viewed in multiple jurisdictions, a post can be republished endlessly and exists until it is removed.

[49] The multiple publication rule has its roots in the case of *Duke of Brunswick v Harmer*.<sup>28</sup> This was back in 1847. The plaintiff was only alerted to the defamatory article in the newspaper when he was given a copy of it some 17 years after it was published. In allowing the Duke's claim, the court ruled that each single publication of the article amounts to a fresh cause of action. In modern times, the case of *Loutchansky v Times Newspapers Ltd & Ors*<sup>29</sup> held that each new "hit" on the web page displaying the libellous content constitutes a fresh cause of action. The court further held that the limitation period for a defamation action is revived on a rolling basis, as long as the article remains online.

[50] The position in the United Kingdom has since changed with the new DA 2013. The Act has introduced a single publication rule under section 8, which stipulates that the liability expires a year after the statement was first published. Section 8 reads as follows:

#### 8. *Single publication rule*

- (1) This section applies if a person –
  - (a) publishes a statement to the public ("the first publication"),  
and

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28 (1849) 14 QBD 185.

29 [2001] EWCA Civ 1805.

- (b) subsequently publishes (whether or not to the public) that statement or a statement which is substantially the same.
- (2) In subsection (1) “publication to the public” includes publication to a section of the public.
- (3) For the purposes of section 4A of the Limitation Act 1980 (time limit for actions for defamation etc.) any cause of action against the person for defamation in respect of the subsequent publication is to be treated as having accrued on the date of the first publication.
- (4) This section does not apply in relation to the subsequent publication if the manner of that publication is materially different from the manner of the first publication.
- (5) In determining whether the manner of a subsequent publication is materially different from the manner of the first publication, the matters to which the court may have regard include (amongst other matters) –
  - (a) the level of prominence that a statement is given;
  - (b) the extent of the subsequent publication.
- (6) Where this section applies –
  - (a) it does not affect the court’s discretion under section 32A of the Limitation Act 1980 (discretionary exclusion of time limit for actions for defamation etc.), and
  - (b) the reference in subsection (1)(a) of that section to the operation of section 4A of that Act is a reference to the operation of section 4A together with this section.

[51] With this single publication rule under section 8, the limitation period starts to run from the date of the first publication. The only proviso is that the subsequent publication must be substantially the same, and not materially different from the first publication.<sup>30</sup>

[52] The multiple publication rule seems to still apply in Malaysia. In the case of *YB Hj Khalid bin Abdul Samad v Datuk Aziz bin Isham &*

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<sup>30</sup> Section 8(4).

*Anor*,<sup>31</sup> the plaintiff, a Member of Parliament (“MP”) for Shah Alam, sued the defendants (a chief editor and a national daily newspaper), for libel arising out of their republication of an article defamatory of him, which originally appeared on the official blog of another MP. The issue in this case was whether the defendants could be held liable for an article that was already posted by another MP on his blog. Although the court did not discuss the multiple publication rule, it found the defendants liable for defamation for the republication, on the basis that they had made no attempts to verify the veracity of the article, and had failed to publish any disclaimer indicating that the views expressed in the article were those of the original writer and not of the defendants.

### **Conclusion**

[53] Following an alarming trend of cyber-attacks and the increasing number of criminal cyber offences and civil cyber claims, Malaysia’s first cyber court was established on September 1, 2016. A Practice Direction No. 5/2016 was subsequently introduced to provide a special category for cyber cases, involving both criminal and civil matters.

[54] As the Internet is no longer a luxury and is now a necessity for most, cyber law in Malaysia must develop to accommodate its growth. Though this field of law is still new, I believe that it will not be long before vital issues on the subject will emerge, giving rise to a healthy development of its jurisprudence.

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31 [2012] 1 AMR 376; [2012] 7 MLJ 301.

# Skinning the Cat: Claims Against Private Healthcare Providers

by

*David Pittaway QC\**

[1] There was a time when the relationship between the patient and the medical practitioner in private healthcare was simple and nobody would have thought about suing the private hospital, at least in relation to the medical treatment. The patient entered into a simple contract with the medical practitioner for diagnosis and treatment and the private hospital provided the consulting room and, if required, the operating theatre and a private room. The medical practitioner belonged to one of the medical defence societies and in the event that the services he provided were below an acceptable standard, the medical defence societies indemnified him against the patient's claim.

[2] The development of more sophisticated models for the provision of private treatment has led to a reconsideration of the relationship between the patient and the providers of healthcare. This has been accompanied by recent developments in the law regarding non-delegable duties of care and vicarious liability. The position has also been complicated by increasing statutory regulation of private healthcare. This article summarises the law in two recent pieces of litigation in the United Kingdom ("UK") and Malaysia, and sets out some of the features that courts should, in my view, be considering when examining these types of claims.

[3] These issues had not been before the English courts until the litigation, akin to group litigation, was brought by several hundred former patients against their former breast surgeon, Mr Ian Paterson, for unnecessary mastectomies and unorthodox treatment, principally of breast cancer patients. Mr Paterson was a member of the Medical Defence Union ("MDU"), and for the period when the MDU was prepared to indemnify him, it had in place a policy of insurance

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limited to £10 million including costs. As a result, the claimants began proceedings against the private healthcare provider, Spire Healthcare, which owned the hospitals where Mr Paterson carried out his treatment, and the Heart of England Foundation Trust, the National Health Service (“NHS”) Trust, where he was employed as a consultant surgeon. The trial was listed to be heard in November 2017, however, the litigation was settled in September 2017 for £37.1 million. Mr Paterson is currently serving a sentence of 20 years’ imprisonment for 17 offences of wounding with intent. The Court of Appeal increased the trial judge’s sentence from 15 to 20 years following a referral from the Solicitor-General.

[4] The principal defendant in each of the civil cases was Mr Paterson who it was alleged acted in breach of the duty of care he owed to his private patients, primarily for negligent performance of surgery and over-treatment. The proceedings brought against Spire Healthcare were pleaded on the grounds that it owed a non-delegable duty of care to Mr Paterson’s patients at the two private hospitals in Birmingham where he practised, and on the grounds of vicarious liability for the actions of Mr Paterson and other employees of Spire Healthcare for failing to take action to withdraw his practising privileges. There was also a claim for breach of the implied statutory terms relating to supply of services. Proceedings were also brought against the Heart of England Foundation Trust, the NHS Trust, on differing grounds.

[5] Spire Healthcare is the second largest provider of private healthcare in the UK, operating 39 private hospitals. It has extensive written protocols regulating the nature of its relationship between medical practitioners. The protocols govern the granting of consultants’ privileges to practice at the hospitals and oversight of their practice. Mr Paterson had been granted consultants’ privileges to work as a surgeon at two of its hospitals in Birmingham. Each hospital had medical advisory and clinical governance committees, and had in place arrangements for the review of consultants’ practicing privileges, and systems for appraisal of consultants’ fitness to practice. There were also arrangements for monitoring clinical outcomes and adverse events.

[6] The case against Spire Healthcare was that it owed a duty of care to the patients using the services provided at its hospitals to operate the systems it put in place competently to protect them from harm. It was alleged that Spire Healthcare’s employees were aware, and that other consultants with practising privileges were aware, that there

were deficiencies in Mr Paterson's NHS practice, which had been subject to investigation, and that there had been complaints about his private practice. It was alleged that if Mr Paterson's practising privileges had been withdrawn at an earlier stage he would not have been able to treat his patients privately at the hospital, or by implication, at any other private hospital. An independent report, commissioned by Spire Healthcare, was critical of its management systems, particularly in monitoring Mr Paterson's practice. Spire Healthcare's own procedures reflected the extent to which modern regulatory requirements provide for greater oversight regarding the activities taking place in private hospitals. One of the issues at trial would have been the date by which Spire Healthcare should have acted to investigate Mr Paterson's practices and suspend or withdraw his practising privileges.

[7] If this litigation had come to trial it would have tested the application of non-delegable duties of care and vicarious liability in the field of clinical negligence. Whilst the issues raised in the claims against Mr Paterson were compromised, the Federal Court of Malaysia in *Kok Choong Seng & Sunway Medical Centre Berhad v Soo Cheng Lin*<sup>1</sup> ("Kok") recently considered the application of non-delegable duties of care and vicarious liability in a simpler factual context, examining the relationship between patients, practitioners and private healthcare providers.

[8] Dr Kok operated on a patient to remove a lump from his forearm in a private hospital and, because of his negligence, the patient lost 90% of his left median nerve. The patient required microscopic reconstruction of the left median nerve using a nerve graft from his left leg. He suffered injuries including pain, numbness and weakness in his left arm. He brought proceedings for negligence and breach of contract against Dr Kok and the private hospital for breach of a non-delegable duty to treat him with care and skill and a failure to provide a safe and reliable system for the treatment and referral of patients.

[9] In both sets of cases the pleadings raised the issue of a non-delegable duty of care following the decision of the UK Supreme Court in *Woodland v Essex County Council*<sup>2</sup> ("Woodland"). In that case, the claim against the educational authority arose out of a brain injury sustained

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1 [2017] 6 AMR 609.

2 [2013] UKSC 66.

by a school pupil whilst taking part in swimming lessons during normal school hours. The lessons were taught by a swimming teacher with a lifeguard in attendance, neither of whom were employed by the educational authority. The lessons were provided by an independent contractor. The pool was operated by another local authority. The claimant brought a claim for damages for personal injury, alleging negligence on the part of the swimming teacher and the lifeguard, and a non-delegable duty of care on the part of the education authority. The High Court struck out the claimant's claim on the basis of non-delegable duty and the Court of Appeal affirmed the decision. The claimant's appeal to the Supreme Court was unanimously allowed.

**[10]** Lord Sumption set out the principles establishing a non-delegable duty of care:

6. English law has long recognised that non-delegable duties exist, but it does not have a single theory to explain when or why. There are, however, two broad categories of case in which such a duty has been held to arise. The first is a large, varied and anomalous class of cases in which the defendant employs an independent contractor to perform some function which is either inherently hazardous or liable to become so in the course of his work.

...

7. The second category of non-delegable duty is, however, directly in point. It comprises cases where the common law imposes a duty upon the defendant which has three critical characteristics. First, it arises not from the negligent character of the act itself but because of an antecedent relationship between the defendant and the claimant. Second, the duty is a positive or affirmative duty to protect a particular class of persons against a particular class of risks, and not simply a duty to refrain from acting in a way that foreseeably causes injury. Third, the duty is by virtue of that relationship personal to the defendant. The work required to perform such a duty may well be delegable, and usually is. But the duty itself remains the defendant's. Its delegation makes no difference to his legal responsibility for the proper performance of a duty which is in law his own. In these cases, the defendant is assuming a liability analogous to that assumed by a person who contracts to do work carefully.

...

23. In my view, the time has come to recognise that Lord Greene in *Gold* and Denning LJ in *Cassidy* were correct in identifying the underlying principle, and while I would not necessarily subscribe to every dictum in the Australian cases, in my opinion they are broadly correct in their analysis of the factors that have given rise to non-delegable duties of care. If the highway and hazard cases are put to one side, the remaining cases are characterised by the following defining features:

- (1) The claimant is a patient or a child, or for some other reason is especially vulnerable or dependent on the protection of the defendant against the risk of injury. Other examples are likely to be prisoners and residents in care homes.
- (2) There is an antecedent relationship between the claimant and the defendant, independent of the negligent act or omission itself, (i) which places the claimant in the actual custody, charge or care of the defendant, and (ii) from which it is possible to impute to the defendant the assumption of a positive duty to protect the claimant from harm, and not just a duty to refrain from conduct which will foreseeably damage the claimant. It is characteristic of such relationships that they involve an element of control over the claimant, which varies in intensity from one situation to another, but is clearly very substantial in the case of schoolchildren.
- (3) The claimant has no control over how the defendant chooses to perform those obligations, i.e. whether personally or through employees or through third parties.
- (4) The defendant has delegated to a third party some function which is an integral part of the positive duty which he has assumed towards the claimant; and the third party is exercising, for the purpose of the function thus delegated to him, the defendant's custody or care of the claimant and the element of control that goes with it.
- (5) The third party has been negligent not in some collateral respect but in the performance of the very function assumed by the defendant and delegated by the defendant to him.

[11] Turning to *Kok*, the Federal Court of Malaysia considered the application of non-delegable duties of care and vicarious liability in other Commonwealth jurisdictions, in Australia, in *Kondis v State*

*Transport Authority*<sup>3</sup> (see also *Commonwealth of Australia v Introvigne*<sup>4</sup> and *Burnie Port Authority v General Jones Pty Ltd*<sup>5</sup>) where Mason J held:

In these situations the special duty arises because the person on whom it is imposed has undertaken the care, supervision or control of the person or property of another or is so placed in relation to that person or his property as to assume a particular responsibility for his or its safety, in circumstances where the person affected might reasonably expect that due care will be exercised.

[12] It also considered the decision of the Singapore Court of Appeal in *The Management Corp Strata Title Plan No 3322 v Tiong Aik Construction Pte Ltd & Anor*,<sup>6</sup> where it said that the Court of Appeal had analysed the distinction between vicarious liability and non-delegable duties:

... there are at least two separate legal doctrines which permit “derogation” from the fault-based principle and impose tortious liability on a defendant for the negligence of another: the first is vicarious liability, where an employer may be subject to tortious liability for the negligence of its employee; and the second is non-delegable duties, where a party may be subject to tortious liability even if the negligent party was its independent contractor. In this sense, vicarious liability and liability which arises out of non-delegable duties may be said to be closely linked doctrines. Conceptually, however, the doctrines are separate and distinct.

[13] The Federal Court of Malaysia said:

[30] The Singapore Court of Appeal then expressed approval for the “defining features in *Woodland*” as characteristic of many of the established instances where non-delegable duties arise, and laid out the following test:

“In our judgment, moving forward, to demonstrate that a non-delegable duty arises on a particular set of facts, a claimant must minimally be able to satisfy the court either that: (a) the facts fall within one of the established categories of non-delegable duties; or (b) the facts possess all the features described at [58] above [the five defining features in *Woodland*]. However, we would

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3 (1984) 55 ALR 225.

4 (1982) 41 ALR 577.

5 (1994) 120 ALR 42

6 [2016] SGCA 40.

hasten to add that (a) and (b) above merely lay down threshold requirements for satisfying the court that a non-delegable duty exists – the court will additionally have to take into account the fairness and reasonableness of imposing a non-delegable duty in the particular circumstance, as well as the relevant policy considerations in our local context.”

[14] It referred to its own decision in *Datuk Bandar Dewan Bandaraya Kuala Lumpur v Ong Kok Peng & Anor*,<sup>7</sup> in the context of extra-hazardous operations.

[15] The battle lines were drawn in *Kok* as to whether the concept of non-delegable duty of care and vicarious liability should be applied in the context of the relationship between the patient, the medical practitioner and the private healthcare provider. It appears that the submissions followed predictable lines. On behalf of the plaintiff it was submitted that the hospital was the healthcare provider and that the medical practitioner’s services were integrated into the hospital’s system under the statutory scheme. The hospital had delegated its duty of care to the medical practitioner to provide reasonable care. The plaintiff was a vulnerable person who became a patient of the hospital on admission. Where the hospital is engaged in providing healthcare for profit, it could not escape liability for harm caused in the conduct of that enterprise by delegating performance to an independent contractor. The hospital was negligent for failing to ensure that the patient was treated by an appropriate medical practitioner. On behalf of the hospital it was submitted that the hospital provided the facilities and the medical practitioner was an independent contractor. A distinction was also drawn between the statutory regime for public and private hospitals.

[16] After consideration of the English authorities, in a learned judgment, the Federal Court of Malaysia rejected the argument that a non-delegable duty of care either never or always applied in cases involving private hospitals but depended on the facts of individual cases. It decided, hardly surprisingly, that the patient was a vulnerable person dependent on the hospital against the risk of injury and that the patient was placed under the care of the hospital whilst admitted. The Federal Court of Malaysia, however, found that the hospital had

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7 [1993] 2 MLJ 234.

not undertaken a positive obligation to protect the patient against harm. It concluded that the patient had contracted with the medical practitioner to provide the treatment at any hospital he nominated. Accordingly, it was not satisfied that the critical part of the *Woodland* test, namely that the hospital assumed a positive obligation in relation to the conduct of the operation, was satisfied on the facts of the case. It rejected an additional argument that the hospital should be liable because it had deeper pockets as being contrary to principle. It is worthwhile mentioning that the trial judge had made no finding that the hospital was negligent in its selection of the medical practitioner.

[17] There is, in my view, a societal change in the UK which has taken place over the past 20 or 30 years as to the provision of private healthcare, partly caused by the development of more sophisticated models, providing a greater range of services, and partly by increased statutory regulation, currently by the Care Quality Commission. As I have already said, Spire Healthcare operates 39 hospitals in the UK, 25 of which were purchased from Bupa in 2007 by a private equity firm for £1.4 billion. It later floated Spire Healthcare on the stock exchange, the first private healthcare provider to do so. Spire Healthcare employs somewhere in the region of 8,000 staff, operating a wide range of healthcare services. It is a large commercial organisation.

[18] Once the threshold requirements in *Woodland* have been overcome, the real issue is the extent to which medical practitioners' services have now become integrated into the hospital system to the extent that the private healthcare provider has assumed a positive duty to protect patients from harm. Regardless of the actual contractual position between the patient and a medical practitioner, some patients in the UK would now consider that they are being treated by the private hospital, as opposed to an individual consultant. It can easily be seen how this has become the case as the scale of the services provided becomes larger. Spire Healthcare, for example, has moved into acute care by opening standalone cardiovascular and cancer treatment centres. Half of Spire Healthcare's work comprises orthopaedic procedures such as hip and knee replacements, where the market is growing as a result of NHS rationing and an increasingly active elderly population. About 25% of Spire Healthcare's patients come from the NHS. The range of services provided directly by private healthcare providers continues to grow, from breast screening to podiatry.

[19] Significantly, whilst referrals to individual consultants ordinarily come from general practitioners (“GPs”), that is not necessary where private medical insurance does not require a referral or where patients are privately paying. The private healthcare provider offers consultants, based upon their availability, within a speciality. They also offer their own private GPs to make a referral to consultants who have practising privileges at the hospitals.

[20] Current billing arrangements may also reflect a change in modern practice. The services of the consultant may now be billed by the private healthcare provider and not separately by the consultant. The ancillary services, including the provision of the services of nursing staff and pathology services may also form part of the same invoice issued by the private healthcare provider. Payment may be made to the medical practitioner by the private healthcare provider out of the composite sum received either from the patient directly or his health insurers. Some consultants are now paid directly by the private healthcare provider for the work that they do without any contractual relationship with the patient.

[21] More particularly, the arrangements for granting and maintaining practising privileges, the appraisals, the monitoring of clinical outcomes and adverse events are all indicative of a level of supervision over the medical practitioners at private hospitals. Whilst the clinical decisions remain those of the medical practitioners, there is now an elaborate framework of control in the UK as to an individual medical practitioner’s fitness to practice at a private hospital. In my view, there has been a blurring of the traditional distinction that used to exist between the role of the medical practitioner and the private hospital. These controls may now be considered as an indicator that the private healthcare provider has assumed a positive duty to protect the patient from harm.

[22] In these circumstances it is not difficult to see the circumstances in which an English court could find in the future that private healthcare providers had assumed a positive duty to protect patients from harm, and in the context of modern business operations, that it was fair and reasonable to impose a non-delegable duty. A fact, I suspect, recognised by Spire Healthcare when the claims brought by Mr Paterson’s patients were compromised before trial for £37.1m.

[23] Turning to the issue of vicarious liability, there is a well-recognised two-stage test: first, consideration of the relationship between the primary wrongdoer and the person alleged to be liable, and second, whether that relationship can give rise to vicarious liability. The second stage relates to whether there is a sufficiently close connection between the wrongdoing and the employment so that it would be fair and just to hold the employers vicariously liable. It is settled law this is the correct test, arising from the decisions in *Lister v Hesley Hall Ltd*<sup>8</sup> and *Dubai Aluminium Co Ltd v Salaam*.<sup>9</sup> The passages below have been recently considered in *Cox v Ministry of Justice*.<sup>10</sup>

[24] In *Various Claimants v Catholic Child Welfare Society & Ors*,<sup>11</sup> Lord Phillips said at paragraph 34:

34. Vicarious liability is a longstanding and vitally important part of the common law of tort. A glance at the table of cases in Clerk & Lindsell on Torts, 20th Ed. (2010), shows that in the majority of modern cases the defendant is not an individual but a corporate entity. In most of them vicarious liability is likely to be the basis upon which the defendant was sued. The policy objective underlying vicarious liability is to ensure, in so far as it is fair, just and reasonable, that liability for tortious wrong is borne by a defendant with the means to compensate the victim. Such defendants can usually be expected to insure against the risk of such liability, so that this risk is more widely spread. It is for the court to identify the policy reasons why it is fair, just and reasonable to impose vicarious liability and to lay down the criteria that must be shown to be satisfied in order to establish vicarious liability. Where the criteria are satisfied the policy reasons for imposing the liability should apply. As Lord Hobhouse of Woodborough pointed out in the *Lister* case [2002] 1 AC 215, para 60, the policy reasons are not the same as the criteria. One cannot, however, consider the one without the other and the two sometimes overlap.

35. The relationship that gives rise to vicarious liability is in the vast majority of cases that of employer and employee under a contract of employment. The employer will be vicariously liable when the

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8 [2002] 1 AC 215.

9 [2003] 2 AC 366.

10 [2014] EWCA Civ 132.

11 [2013] 2 AC 1.

employee commits a tort in the course of his employment. There is no difficulty in identifying a number of policy reasons that usually make it fair, just and reasonable to impose vicarious liability on the employer when these criteria are satisfied: (i) the employer is more likely to have the means to compensate the victim than the employee and can be expected to have insured against that liability; (ii) the tort will have been committed as a result of activity being taken by the employee on behalf of the employer; (iii) the employee's activity is likely to be part of the business activity of the employer; (iv) the employer, by employing the employee to carry on the activity will have created the risk of the tort committed by the employee; (v) the employee will, to a greater or lesser degree, have been under the control of the employer.

36. In days gone by, when the relationship of employer and employee was correctly portrayed by the phrase "master and servant", the employer was often entitled to direct not merely what the employee should do but the manner in which he should do it. Indeed, this right was taken as the test for differentiating between a contract of employment and a contract for the services of an independent contractor. Today it is not realistic to look for a right to direct how an employee should perform his duties as a necessary element in the relationship between employer and employee. Many employees apply a skill or expertise that is not susceptible to direction by anyone else in the company that employs them. Thus, the significance of control today is that the employer can direct what the employee does, not how he does it.

[25] In the *Paterson Litigation* it was pleaded that Spire Healthcare was vicariously liable for the acts of Mr Paterson and its employees generally in failing to take action and report Mr Paterson's actions to the management. Vicarious liability for Mr Paterson's actions would have depended on the finding as to whether he was truly an independent contractor. Although the doctrine is entirely separate from a non-delegable duty of care, the facts set out above in relation to the extent that the medical practitioners services have become integrated into the hospital's system are clearly relevant. The greater the integration the less likely the medical practitioner is truly an independent contractor. It may be that the traditional view of the status of the medical practitioner in the private healthcare setting in the UK has become an anomaly as large private healthcare providers have substantially altered their business operations.

[26] The case, however, also raised interesting issues as to the nature of the obligations owed by Spire Healthcare's employees, or indeed other medical practitioners with consultants' privileges at the hospitals, to inform management of matters of which they were aware, affecting the safety and well-being of patients at private hospitals. There are analogies that can be drawn with some of the issues which have arisen in child abuse cases, particularly religious institutions where other members were aware of child abuse but took no action to report it. Again, this is an issue which would extend the boundaries of vicarious liability in the context of the provision of private healthcare. Matters that should have been brought to the attention of the clinical director or matron by, for example, the nursing staff or other medical practitioners as to Mr Paterson's fitness to practice, go to the second stage of the test: whether there is a sufficiently close connection between the wrongdoing and the employment so that it would be fair and just to hold the private healthcare provider vicariously liable.

[27] In *Kok*, on behalf of the plaintiff similar arguments were employed to those used to support the case that the private hospital owed a non-delegable duty of care, namely that the medical practitioner's services were integrated into the hospital's system of providing healthcare. Policy and practical reasons were cited in support of imposing vicarious liability on the hospital: it should be responsible for the risks associated with its commercial enterprise and patients should be able to look to the deepest pockets.

[28] The contrary submission on behalf of the hospital was that the first stage of the test for vicarious liability was not satisfied because the medical practitioner had the means to satisfy the judgment. It was argued that his services were not integrated with or conducted on behalf of the hospital: the patient had selected the surgeon, and the hospital did not have control as to what he did on the premises. The second stage was not satisfied because there was no connection between the tort and the relationship between the medical practitioner and the hospital whom he paid for use of the facilities. It was also argued that vicarious liability should be disregarded with private medical practitioners because they were compulsorily insured and there were no concerns about compensating patients. In any event it was submitted that vicarious liability ran against the legislative scheme, which provided distinct roles for private hospitals and medical practitioners.

[29] The Federal Court of Malaysia rejected the submission that vicarious liability should not apply in cases of private healthcare as being unsupported by legislation. It found, however, that the private hospital was not vicariously liable for Dr Kok's negligence. It appears that the factual circumstances of Dr Kok's relationship with the private hospital were very different from those of Mr Paterson and Spire Healthcare. The court followed the two-stage test in English case law in finding that the test for vicarious liability is to, first, determine the nature of the relationship between the hospital and medical practitioner, and second, the connection between that relationship and the wrongful act by the practitioner. It concluded that the question was fact-dependent on multiple factors calling for an evaluative judgment.

[30] The key factors were that Dr Kok's services were generally not subject to the hospital's control and interference. Dr Kok arranged for the surgery in the course of his own practice at his private clinic. In the Federal Court of Malaysia's view, the absence of even vestigial control negated vicarious liability on its part for Dr Kok's negligence in the conduct of the operation. It concluded that the undertaking of the operation was recognisably part of Dr Kok's independent business. It did not consider that the relationship between the practitioner and the hospital as sufficiently akin to employment to give rise to vicarious liability for Dr Kok's negligent conduct of the operation. It, therefore, did not go on to consider the second stage of the test.

[31] Following the settlement of the *Paterson Litigation* in the UK, it is probable that claimants will now include, in suitable cases, claims against private healthcare providers on the ground of non-delegable duties of care and vicarious liability. There is set out above the range of factors that are now likely to be considered in the English courts as to whether a non-delegable duty of care exists or whether the private healthcare provider should be held vicariously liable for a medical practitioner's actions. It is, as has been said in *Kok*, heavily fact-dependent. The facts in *Kok* were very different from those that would have come out in evidence in the *Paterson Litigation*, leading to the decision in *Kok* being consistent with Lord Sumption's test in *Woodland*.

[32] One other aspect in this changing climate is whether private healthcare providers will wish to consider the terms of the professional

indemnity insurance which they require to be put in place before granting medical practitioners practising privileges. Whilst the medical defence societies in the UK continue to provide discretionary relief for their members, there may be a query as to whether this will be sufficient protection for private healthcare providers against claims in the future.

# The Business Judgment Rule: A Safe Harbour for Directors?#

by

Associate Professor Low Chee Keong\* and Low Tak Hay\*\*

## Abstract

[1] As the complexity and sophistication of business activities increase with operations extending beyond borders and across industries, so too does the demand on management – especially on boards of directors of companies – to ensure that appropriate standards of corporate governance are implemented and enforced. However, one must question whether these standards have become so onerous as to disincentivise otherwise qualified individuals from joining corporate boards.

[2] The Companies Act 2016 has as amongst its objectives the modernisation and simplification of numerous aspects of company law in Malaysia, and maintains the statutory business judgment rule which ambit remains to be definitively set although the provision was originally enacted a decade ago in 2007. Commencing with a concise overview of the duties and responsibilities expected of directors, this article enquires – through a review of the approaches in Australia and the United States of America (“USA”) – whether section 214 will afford directors with adequate protection when they are alleged to have breached their duty of care to the company on which board they serve.

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# This paper updates and expands upon Branson DM, & CK Low, “Balancing the Scales: A Statutory Business Judgment Rule for Hong Kong?” (2004) Vol 32 Part II *Hong Kong Law Journal* 303.

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## Introduction

[3] Directors are regarded as a front line “gatekeeper” for good corporate governance and are continually subject to ever increasing scrutiny with much of the reforms centred upon a regulatory philosophy of keeping them on the “straight and narrow”, often by compelling them to “do X”, “do Y” and/or “do Z”. This approach presumes that legislators and regulators have the inherent ability to subject business decisions to systematic analysis and fails to recognise that such decisions often involve intangible and intuitive insights, especially with the increasing complexity and sophistication of commercial activities.

[4] Ever since the release of the Cadbury Report in 1992,<sup>1</sup> regulatory approaches to the vexed issue of “good corporate governance practices” have been largely “all stick and no carrot” with company directors exhorted to be independent, vigilant, informed and decisive. They are to serve not only on the board but are also required to take on increasingly burdensome responsibilities on audit and other committees, with a corresponding enhancement of expectations as regards the duty that they owe to the company – both individually and collectively – which potentially exposes them to increased liability and penalties.

[5] A number of policy questions arise from such an approach. For example, why should directors not be protected for decisions that were made without any conflicts of interest and with full knowledge and appreciation of the material facts, even if the company was to subsequently suffer a loss? Should the law not be more accommodating by allowing directors to get back to the basics of business within a capitalist framework, namely, to promote entrepreneurship through the facilitation of legitimate business decisions and risk-taking? In short, is it not time to consider rebalancing the scales to reward directors who are prudent, independent and vigilant, and who make reasonable and informed judgments?

[6] The Companies Act 2016,<sup>2</sup> which came into effect on January 31, 2017, has as amongst its objectives the modernisation and simplification of numerous aspects of company law in Malaysia. Its enactment is

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1 Report of the Committee on the Financial Aspects of Corporate Governance (December 1992) available at <<http://cadbury.cjbs.archios.info/report>>.

2 Act 777 of the Laws of Malaysia.

most certainly welcome given that reforms in this important area of the law have largely been undertaken on a piecemeal basis since the introduction of the Companies Act 1965. In this regard, due credit should be given to the Companies Commission of Malaysia, a statutory body formed from a merger of the Registrar of Companies and the Registrar of Businesses, for it was under its auspices that the Corporate Law Reform Committee was established in December 2003 to realise the objective of establishing a dynamic regulatory environment for business in Malaysia while dealing with corporate accountability and governance that is in line with global standards.

[7] The Companies Act 2016 maintains the statutory business judgment rule which scope – although originally enacted a decade ago in 2007 – remains to be definitively determined. Commencing with a concise overview of the duties and responsibilities expected of directors, this article enquires, through a review of the approaches in Australia and the USA, whether section 214 will afford directors with adequate protection when they are alleged to have breached their duty of care to the company on which board they serve.

### **A concise overview of directors' duties in Malaysia**

[8] Part III, Division 2, Subdivision 3 of the Companies Act 2016 titled "Directors' Duties and Responsibilities", sets out the codification of the law, and succinctly articulates at section 211 that "the business and affairs of a company shall be *managed by, or under the direction of the Board*" (emphasis added). In a nutshell, directors of companies are duty bound to act for a proper purpose and in good faith in the best interest of the company,<sup>3</sup> and the requisite standard against which their actions will be judged is provided under section 213(2) which states that:

A director of a company shall exercise reasonable care, skill and diligence with –

- (a) the knowledge, skill and experience which may reasonably be expected of a director having the same responsibilities; and
- (b) any additional knowledge, skill and experience which the director in fact has.

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<sup>3</sup> Section 213(1).

[9] The foregoing is the same as its predecessor provision, namely, section 132(1) and (1A) of the Companies Act 1965. The Court of Appeal in *Pioneer Haven Sdn Bhd v Ho Hup Construction Co Bhd & Anor and other appeals*<sup>4</sup> held that with regard to section 132(1) it is settled law that the duty to act honestly required by statute includes the duty to act in the best interest of the company.<sup>5</sup>

[10] In arriving at their decision, their Lordships cited with approval the leading judicial pronouncement by Pennycuik J who opined in *Charterbridge Corporation Ltd v Lloyds Bank Ltd and Another*<sup>6</sup> that:

The proper test, I think, in the absence of actual separate consideration, must be whether an intelligent and honest man in the position of a director of the company concerned, could, in the whole of the existing circumstances, have reasonably believed that the transactions were for the benefit of the company.<sup>7</sup>

[11] Taking cognizance that delegation and reliance is essential for the effective and efficient running of a modern commercial enterprise, section 215 allows directors to rely on information provided by others if this is done “in good faith and after making an independent assessment of the information or advice, opinions, reports or statements, including financial statements and other financial data, having regard to the director’s knowledge of the company and the complexity of the structure and operation of the company.”<sup>8</sup> The foregoing makes it abundantly and undeniably clear that the standard of care expected of directors is premised on a “mixed objective-subjective” test, taking into account not just what a reasonable person might do in like circumstances but also any special abilities that the individual director possesses.

[12] In a lengthy judgment in *Re Barings plc (No 5)*,<sup>9</sup> Parker J reviewed the morass of authorities on directors’ duties and summarised these into a number of succinct proposals namely:

- i. Directors had, both collectively and individually, a continuing duty to acquire and maintain a sufficient knowledge and

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4 [2012] 3 AMR 297; [2012] 3 MLJ 616.

5 Ibid, at 330 (AMR); 654 (MLJ).

6 [1970] Ch 62.

7 Ibid, at 74.

8 Section 215(2).

9 [1999] 1 BCLC 433.

understanding of the company's business to enable them properly to discharge their duties as directors.

- ii. Whilst directors were entitled (subject to the articles of association of the company) to delegate particular functions to those below them in the management chain, and to trust their competence and integrity to a reasonable extent, the exercise of the power of delegation did not absolve a director from the duty to supervise the discharge of the delegated functions.
- iii. No rule of universal application can be formulated as to the duty referred to in paragraph (ii) above. The extent of the duty, and the question whether it had been discharged, depended on the facts of each particular case, including the director's role in the management of the company.<sup>10</sup>

[13] The foregoing principles were endorsed wholeheartedly in *Re Copyright Ltd*<sup>11</sup> where it was held that the exercise of the power to delegate does not absolve directors from the duty to supervise the discharge of such delegated powers. While both *Re Barings plc (No 5)* and *Re Copyright Ltd* involved applications for the disqualification of directors, they are nonetheless important for reinforcing the view that directors should acquire and maintain sufficient knowledge and understanding of the business of the company on which board they serve, and that they should exercise a sufficient degree of supervision of functions that they may have properly delegated.

[14] In affirming that all directors are required to monitor the management of the business as well as of its finances, the judgment in *Re Copyright Ltd* implicitly accepted that the standard of care expected of directors in Hong Kong is objective, consistent with the common law developments in Australia and England,<sup>12</sup> and has since been applied in *Re Regal Motion Industries Ltd*<sup>13</sup> and *Re Weld Tech Electrical Supplies Co Ltd*,<sup>14</sup> providing sound judicial precedent that while it is permissible for directors to delegate when done properly, their overall responsibility is simply not delegable.

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10 Ibid, at 489. This decision was subsequently affirmed by the English Court of Appeal in *Baker v Secretary of State for Trade and Industry* [2000] EWCA Civ 59.

11 [2004] 2 HKLRD 113.

12 Ibid, at 124–125.

13 [2005] 1 HKLRD 461.

14 [2010] HKEC 899.

[15] The recent decision of the Federal Court of Australia in *Australian Securities and Investments Commission v Healey*<sup>15</sup> (hereafter referred to as “*Centro*”) provides some useful and important guidance given that the “mixed objective-subjective” test has been a part of the Australian corporate landscape for more than a decade.<sup>16</sup> While the decision in *Centro* admittedly revolved around the issue of disclosure in financial statements, it is submitted that its application extends much further as the learned judge reviewed the extent to which directors could rely on advice from third parties.

[16] In a nutshell, the case involved alleged breaches by directors of the duty owed to *Centro*, the company on which board they served, with the approval of consolidated financial accounts that had incorrectly classified A\$1.5 billion in debt as “non-current liabilities” and the non-disclosure of the provision of A\$1.75 billion in guarantees to an associated company after the balance date. Significantly, both transactions had been reviewed without query by its audit committee as well as by its external auditor, PricewaterhouseCoopers.

[17] In finding the directors liable, Middleton J opined that the “importance of the financial statements is one of the fundamental reasons why directors are required to approve them and resolve that they give a true and fair view.”<sup>17</sup> His Honour emphasised that “case law indicates that there is a *core, irreducible requirement of directors* to be involved in the management of the company and to take all reasonable steps to guide and monitor”<sup>18</sup> (emphasis added) and that directors have “a duty greater than that of simply representing a particular field of experience or expertise.”<sup>19</sup>

[18] Crucially, the learned judge noted that although “a reasonable step would be to delegate various tasks to others ... this does not discharge the entire obligation upon directors”,<sup>20</sup> echoing Lord Wolff MR in *Re Westmid Packing Services Ltd*<sup>21</sup> who held that while “a proper degree of delegation and division of responsibility is of course

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15 [2011] FCA 717.

16 Section 180 of the Corporations Act 2001.

17 [2011] FCA 717 at [10].

18 *Ibid*, at [16].

19 *Ibid*, at [18].

20 *Ibid*, at [240].

21 [1998] 2 All ER 124.

permissible, and often necessary, but *total abrogation of responsibility is not*<sup>22</sup> (emphasis added).

[19] This view was embraced wholeheartedly by the then Attorney-General Lord Goldsmith during the parliamentary debate on the proposed codification of the duty of directors to exercise independent judgment – now section 173 of the United Kingdom Companies Act 2006 – when his Lordship opined that:

The duty does not prevent a director from relying on the advice of work of others, but the final judgment must be his responsibility ... As with all advice, *slavish reliance is not acceptable*, and the obtaining of outside advice does not absolve directors from exercising their judgment on the basis of such advice.<sup>23</sup> (Emphasis added.)

[20] Thus, while directors are allowed to delegate some of their responsibilities, they are not entitled to rely blindly on advice without applying their minds independently to the facts as Middleton J took great pains to emphasise that:

Nothing that I decide in this case should indicate that directors are required to have infinite knowledge or ability. Directors are entitled to delegate to others the preparation of books and accounts and the carrying on of the day-to-day affairs of the company. What each director is expected to do is to take a *diligent and intelligent interest* in the information available to him or her, to understand that information, and apply an enquiring mind to the responsibilities placed upon him or her.<sup>24</sup> (Emphasis added.)

[21] Based on the foregoing, a director cannot abrogate responsibility by simply slavishly relying on others without applying him or herself in a diligent and intelligent manner to fully appreciate the significance of the information presented and the gravity of the responsibilities expected. If we accept the decision of Middleton J that once appointed “there is a core, irreducible requirement of directors to be involved in the management of the company and to take all reasonable steps to guide and monitor”, and that all directors have “a duty greater than

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22 Ibid, at 130.

23 See House of Lords Grand Committee Column 282 (February 6, 2006) available at <<http://www.publications.parliament.uk/pa/ld200506/ldhansrd/vo060206/text/60206-37.htm>>.

24 [2011] FCA 717 at [20].

that of simply representing a particular field of experience or expertise”, it must follow that it will no longer be a defence for a director to claim that he or she had simply relied on the advice of an external professional or that he or she was not a member of a committee of the board that made a particular decision which turned out poorly for the company.<sup>25</sup>

### The business judgment rule

[22] In *Howard Smith Ltd v Ampol Petroleum Ltd*,<sup>26</sup> Lord Wilberforce stated that “Their Lordships accept that such a matter as the raising of finance is one of management, within the responsibility of the directors: they accept that it would be *wrong for the court to substitute its opinion* for that of the management, or indeed to question the correctness of the management decision on such a question, if *bona fide* arrived at”<sup>27</sup> (emphasis added). However, it is trite that any optimal company law rule set will seek to attain a number of objectives. These would include permitting the formation and registration of companies with ease; protection of minority to encourage the formation of capital; articulating meaningful fiduciary duties of care, loyalty and to act lawfully so as to protect the company and all its stakeholders; expending public funds for public enforcement of certain duties; as well as the provision of meaningful members’ remedies which includes recognising the modern shareholder’s derivative action in some form.<sup>28</sup>

[23] Arguably, the optimal rule set must also include protection for directors who are independent and disinterested, who inform themselves about the subject matter of decisions they are about to make, and who then make decisions. In other words, the optimal rule set must include some form of business judgment rule. Section 214 provides for such a rule couched in the following terms:

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25 See e.g. CK Low & TY Low, “When is the Board Responsible for Delegation and Reliance?: A Case Study of the MTR Corporation Ltd in Hong Kong” (2016) 30 *Australian Journal of Corporate Law* 285 for a further analysis of this issue.

26 [1974] AC 821.

27 *Ibid*, at 832.

28 Section 346 allows for the initiation of a statutory derivative action by a member under certain circumstances. Such actions allow courts to examine the merits and desirability of actions taken by those who control or manage the affairs of the company which otherwise remains constrained by *Foss v Harbottle* (1843) 2 Hare 461; 67 ER 189. The courts have however recognised the existence of the multiple derivative action: see *Ranjeet Singh Sidhu & Anor v Zavarco plc & Ors* [2015] AMEJ 1720; [2016] 2 CLJ 975.

- (1) A director who makes a business judgment is *deemed to meet the requirements of the duty under subsection 213(2)* and the equivalent duties under the common law and in equity if the director –
  - (a) makes the business judgment for a proper purpose and in good faith;
  - (b) does not have a material personal interest in the subject matter of the business judgment;
  - (c) is informed about the subject matter of the business judgment to the extent the director reasonably believes to be appropriate under the circumstances; and
  - (d) reasonably believes that the business judgment is in the best interest of the company.
- (2) For the purposes of this section, “business judgment” means any decision on whether or not to take action in respect of a matter relevant to the business of the company.

(Emphasis added.)

[24] Interestingly, the deeming provision of section 214(1) appears to equate the fulfilment of the requirements of the business judgment rule to the attainment of the requisite standard of care expected of directors thereby effectively providing a safe harbour for the latter. However, much will depend on the interpretation of the provision by the judiciary in Malaysia especially in view of the fact that it was drawn almost verbatim from the Australian equivalent which has, by and large, failed to meet the initial expectations of providing better and more adequate protection for directors for business decisions or judgments.

### *The business judgment rule in Australia*

[25] Australian business interests began campaigning for a statutory business judgment rule in the early 1990s, which the government was opposed to for a number of reasons, including:<sup>29</sup>

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<sup>29</sup> See Farrar J, “Towards a Statutory Business Judgment Rule in Australia” (1998) 8 *Australian Journal of Corporate Law* 237 at 241–242.

- i. the rule was a creature of judge-made law in the USA and it would not be wise to transplant one aspect of that regime in isolation into a very different regime existent in Australia;<sup>30</sup>
- ii. attempts made by the American Law Institute (“ALI”) and the American Bar Association to codify a business judgment rule had broken down,<sup>31</sup> and
- iii. Australian corporate law had already embodied something similar to the business judgment rule.<sup>32</sup>

[26] In the mid-1990s, the Australian government transferred “jurisdiction” over corporate law reform from the Commonwealth Attorney General’s office to the Treasury. The then Treasurer, Mr Peter Costello, was a supporter of a statutory business judgment rule as he believed that it would encourage entrepreneurship by facilitating legitimate business decisions and risk-taking. In 1999, the Australian Parliament enacted the business judgment rule as section 180(2) of the Australian Corporations Act 2001 which provides:

A director or other officer of a corporation who makes a business judgment is taken to meet [the standard of care] and their equivalent duties at common law and in equity, in respect of the judgment, if they:

- (a) make the judgment in good faith for a proper purpose; and
- (b) do not have a material personal interest in the subject matter of the judgment; and
- (c) inform themselves about the subject matter of the judgment to the extent they reasonably believe to be appropriate; and
- (d) rationally believe that the judgment is in the best interests of the corporation.

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30 This objection was in part answered by statutory abrogation of the rule in *Foss v Harbottle* (1843) 2 Hare 461; 67 ER 189, with concomitant statutory recognition of the derivative suit.

31 This was not factually accurate as the ALI formulation was not proven controversial and was adopted by courts in a number of states in the USA.

32 See e.g. *Re Smith & Fawcett Ltd* [1942] Ch 304; and *Harlowe’s Nominees Pty Ltd v Woodside (Lakes Entrance) Oil Co NL* (1968) 121 CLR 483. See also Farrar J, *Corporate Governance in Australia and New Zealand* (London: Oxford University Press, 2001), pp 135–136.

The director's or officer's belief that the judgment is in the best interests of the corporation is a rational one unless the belief is one that no reasonable person in their position would hold.

[27] Section 180(3) defines a "business judgment" as "any decision to take or not to take action in respect of a matter relevant to the business operations of the corporation".

[28] In large part, the Australian drafters based the statute upon section 401(c) of the ALI's Corporate Governance Project<sup>33</sup> albeit with some salient differences, including a definition of "rational belief". Significantly, the Australian enactment adds language from the English and Australian precedents that the judgment must have been made "for a proper purpose bona fide in the interests of the company as a whole."<sup>34</sup> In the US, judges and commentators regard the business judgment rule as setting forth a short list of objective factors that judges may substitute for more subjective or fact-based inquiries. Using this short list, judges are able quickly to weed out those cases not in need of a trial or other form of more plenary proceeding. Reintroduction of a quasi-subjective element, namely motive, by enquiring whether the director took the action for a proper purpose, robs the business judgment rule of a measure of its utility. Thus, there is an inherent tension between the US objective-factor-only business judgment rule and fidelity to existent Australian case law.

[29] The proper purpose limitation "[p]robably means that the rule cannot be used in takeover defences, unlike US law."<sup>35</sup> In contrast, US courts, especially those in the state of Delaware, have developed a rich takeover jurisprudence which judges directors' adoption of takeover

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33 See Farrar J, *Corporate Governance in Australia and New Zealand* (London: Oxford University Press, 2001), p 138.

34 See e.g. *Howard Smith Ltd v Ampol Petroleum Ltd* [1974] AC 821 at 825 (per Wilberforce LJ); *Australian Metropolitan Life Assurance Co Ltd v Ure* (1923) 33 CLR 199 at 217; and Fridman S, "An Analysis of the Proper Purpose Rule" (1998) 10 *Bond Law Review* 164.

35 See Farrar J, *Corporate Governance in Australia and New Zealand* (London: Oxford University Press, 2001), p 138. *Hogg v Cramphorn Ltd* [1967] Ch 254 was an early judicial application of the proper purpose rule to a takeover. The court struck down a defensive attempt to utilise a trust, ostensibly for the benefit of employees, into which the takeover target had "parked" a number of its shares as the directors had not acted for a proper purpose and honestly for the benefit of the company as a whole.

defences using a somewhat refined version of the business judgment rule as a yardstick, or at least US law does so if it is the independent directors who consider and adopt the defences. The latter, of course, tend to be free of entrenchment motives that may influence “inside” or executive directors and/or senior executives of the company. In essence, before adopting takeover defences, US directors must conduct a reasonable investigation and develop a reasonable belief that a takeover bid or other offeror tactic poses “a realistic danger to corporate policy and effectiveness.”<sup>36</sup> Then, any defence adopted “must be reasonable in relation to the threat posed.” Last of all, the US doctrine does not give unbridled license to corporate directors: there is an absolute prohibition against adoption of “draconian” and “preclusive” takeover defences.<sup>37</sup> It was against this background that the Australian drafters viewed US business judgment rule jurisprudence as being too permissive and they accordingly inserted the “proper purpose” language into its legislation.

[30] Despite the initial optimism that a statutory business judgment rule would provide “certainty for directors” and would “stimulate risk taking and innovation” as well as to “give directors the confidence to make commercial decisions on their own merits”,<sup>38</sup> its first decade failed to live up to this expectation. The protection did not materialise in practice as its application was rejected due to a clear conflict by the defendant director,<sup>39</sup> or that it was held that the business judgment was not “relevant to the business operations of the corporation”,<sup>40</sup> which highlights the aversion of the courts to review business decisions that are made in good faith.<sup>41</sup>

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36 *Unocal Corp v Mesa Petroleum Co* 493 US 946, 954 (Del 1985).

37 *Unitrin, Inc v American Gen Corp*, 651 A 2d 1361, 1384 (Del 1995).

38 Parliament of Australia, Parliamentary Debates – Senate Hansard, December 17, 1992 at p 5297, per Senator Robert Hill.

39 See e.g. *Australian Securities and Investments Commission v Adler* (2002) 41 ACSR 72; and *Australian Securities and Investments Commission v Fortescue Metals Group Ltd* (2011) 190 FCR 364.

40 See e.g. *Gold Ribbon (Accountants) Pty Ltd (in liq) v Sheers* [2006] QCA 335; *MacDonald v Australian Securities and Investments Commission* (2007) 73 NSWLR 612; *Hall v Poolman* (2007) 65 ACSR 123; and *Australian Securities and Investments Commission v Fortescue Metals Group Ltd*, *ibid*.

41 See Verzaly J, “Protecting the Authority of Directors: An Empirical Analysis of the Statutory Business Judgment Rule” (2012) Vol 12 No 2 *Journal of Corporate Law Studies* 429.

[31] In fact, the scope of the statutory business judgment rule was not even examined in detail until *Australian Securities and Investments Commission v Rich*.<sup>42</sup> In that case, Austin J held that the Australian Securities and Investments Commission (“ASIC”) had failed to prove its case that two directors of OneTel Ltd, namely, Mr Rich and Mr Silbermann, had contravened section 180 of the Corporations Act 2001<sup>43</sup> as his Honour concluded that the rational belief required as an element of the business judgment rule in section 180(2) does not have to be reasonable. In other words, a director can invoke the business judgment rule if he shows that he arrived at the business judgment after a reasoning process “whether or not the reasoning process was convincing to the judge and therefore reasonable in an objective sense.”<sup>44</sup>

[32] Significantly, Austin J opined that it was for the *defendants* to bear the onus of proof in order to derive the benefit under section 180(2) but added that the issue was “an important one that will eventually need to be resolved at an appellate level.”<sup>45</sup> While at first glance this looks like a reversal of the envisaged safe harbour since it subjects the elements of a director’s decision to judicial scrutiny – contrary to the very purpose of a business judgment rule – it should nonetheless be emphasised that the rule is not meant to insulate directors from liability. However, on closer analysis the approach adopted by Austin J provides a sensible and reasonable balance: it provides directors with a safe harbour if they can prove all four criteria as set out in section 180(2) but takes this protection away if the plaintiff is able to prove that one or more of the said criteria has not been established.

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42 (2009) 75 ASCR 1. See also Legg M & Jordan D, “The Australian Business Judgment Rule after *ASIC v Rich*: Balancing Director Authority and Accountability” (2014) *Adelaide Law Review* 403.

43 (2009) 75 ASCR 1 at 184–185.

44 *Ibid*, at 154.

45 *Ibid*, at 149. See also Young N, “Directors Duty of Care and Diligence: A Review in Light of the Recent Decision in *ASIC v MacDonald (No 11)*” in Austin RP and Bilski AY (eds), *Directors in Troubled Times* (Ross Parsons Centre of Commercial, Corporate and Taxation Law, 2009) where the author opined at p 80 that the business judgment rule “does not attempt to define the standard of care required of directors making business judgment nor is it formulated as a preliminary presumption that explicitly puts the burden of rebuttal on the party alleging a breach of section 180(1). Rather it is framed as a deemed provision that will operate only if the four conditions in subsection (2) are proved. It is hard to see how a director can avail himself or herself of the business judgment rule without adducing evidence satisfying these conditions.”

In the latter case, the court will then examine whether section 180(1) has been complied with.

[33] In his judgment Austin J held that a “business judgment ... relevant to the business operations of the corporation” must involve “the need for a conscious decision — that is to say, whether or not the directors or officers in fact *turned their minds* to the matter”<sup>46</sup> (emphasis added). Thus, in the opinion of his Honour, the scope of section 180(3) would include:

- i. decisions that are preparatory to the making of a business decision;
- ii. decisions relating to corporate personnel;
- iii. decisions relating to the termination of litigation;
- iv. the setting of policy goals;
- v. the apportionment of responsibilities between the board and senior management; and
- vi. decisions about planning, budgeting and forecasting.<sup>47</sup>

[34] As there is a need for directors to make a conscious decision – through the requirement that they must actively turn their minds to the matter – it must logically follow that the discharge of “oversight” responsibilities such as monitoring the affairs and policies of the company as well as the maintaining of familiarity with its financial position cannot be a “business judgment”. This approach is consistent with the decision of the full Federal Court in *Australian Securities and Investments Commission v Fortescue Metals Group Ltd*,<sup>48</sup> a case that dealt with compliance with the continuous disclosure obligations under the Corporations Act 2001, where the court held that:

... the decision not to disclose the true effect of the agreements cannot be described as “business judgment” at all. A decision not to make accurate disclosure of the terms of a major contract is not a decision related to the “business operations” of the corporation. Rather it is a decision related to compliance with the requirements of the Act.<sup>49</sup>

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46 (2009) 75 ASCR 1 at 151.

47 *Ibid*, at 150.

48 (2011) 190 FCR 364.

49 *Ibid*, at 427, per Keane CJ.

[35] Be that as it may, it must be highlighted that the mere fact that the issue involves compliance will not automatically – on its own – mean that it is not a “business judgment”. It is entirely possible that directors may actively *turn their minds* to matters of compliance such as appeals on rulings by relevant authorities including the tax department or the securities regulator. Indeed, Austin J opined that *Australian Securities and Investments Commission v Rich* was such a case since the defendant directors had to consider matters that ASIC had complained about and they subsequently made decisions with which ASIC disagreed. Under such circumstances, the decisions by the defendant directors taken in planning, budgeting and forecasting were capable of receiving the protection of the Australian statutory business judgment rule.<sup>50</sup>

[36] The pragmatic approach of Austin J was endorsed by the Federal Court in *Australian Securities and Investments Commission v Mariner Corp Ltd*.<sup>51</sup> In this case, ASIC rather belatedly brought action against three directors for a “bluffing” off-market takeover bid which had no realistic chance of success and which in any event was withdrawn when the target company entered into an agreement with a third party that triggered a defeating condition of the offer. ASIC alleged that the announcement of the takeover bid breached various provisions of the Corporations Act 2001 including recklessness as regards performance of the obligation;<sup>52</sup> that the directors had announced a bid that was “deceptive or likely to mislead or deceive”;<sup>53</sup> and that the directors had contravened their statutory duty of care by causing the company to contravene or risk contravening sections 631(2)(b) and 1041H.<sup>54</sup>

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50 (2009) 75 ASCR 1 at 150.

51 (2015) FCA 589. This is the first case in which directors successfully invoked s 180(2) as a defence since its enactment in 2000. See also an earlier Federal Court decision in *Deangrove Pty Ltd (Receivers and Managers Appointed) v Bucky & Anor* [2006] FCA 212 where it was held that receivers – as officers of a company – were entitled to rely on the business judgment rule.

52 Section 631(2)(b).

53 Section 1041H.

54 This was despite the fact that the prohibitions as outlined above applied to the company rather than its directors. The ASIC also alleged that the directors had failed to consider the regulatory constraints on Mariner Corporation acquiring more than certain percentages of the target company. The action was brought by the ASIC on April 2, 2014, some two years after the “bluffing” takeover bid was announced and subsequently withdrawn.

Further and in addition, ASIC alleged that the directors had breached section 180(1) irrespective of whether the company had breached sections 631(2)(b) and/or 1041H.

[37] In holding that none of the directors were liable, Beach J opined that the office of a director must necessarily involve some degree of reasonable risk-taking stating as his Honour did:

Further, relevant to the question of breach of duty is the balance between, on the one hand, the foreseeable risk of harm to the company flowing from the contravention and, on the other hand, the potential benefits that could reasonably be expected to have accrued to the company from that conduct.<sup>55</sup>

After all, one expects management including the directors to take *calculated* risks. The very nature of commercial activity necessarily involves uncertainty and risk taking. The pursuit of an activity that might entail a foreseeable risk of harm does not of itself establish a contravention of s 180. Moreover, a failed activity pursued by the directors which causes loss to the company does not of itself establish a contravention of s 180.<sup>56</sup>

[38] In short, the learned judge took the view that as companies do not operate within a vacuum of absolute certainty it must follow that the assumption of reasonable risks is acceptable provided that this is commensurate with the expected returns or benefits that might reasonably accrue. In the instant case, the directors were able to show that substantial gains would have accrued to the company had the takeover bid been successful while the downside risks were minimal in the circumstances given the numerous conditions that were attached to the bid.

[39] Assessed from the view point of a reasonable person, if the potential benefits of a transaction outweighed the potential risks of harm, the directors should not be held liable for breach of their statutory duty of care under section 180(1). In the words of Beach J:

Even if one or more of the alleged risks of harm to Mariner were reasonably foreseeable, the actual jeopardy that this risks posed to Mariner's interest were, in context, minimal. Further, and in any

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55 (2015) FCA 589 at [450].

56 *Ibid*, at [452] with the emphasis being made by the learned judge.

event the potential countervailing benefits to Mariner of pursuing the proposed takeover bid were significant and outweighed such risks.<sup>57</sup>

[40] It is incumbent upon the directors to adduce the requisite evidence to the standard required to support their assertion that they had not breached their duty to the company on which board they serve. If this condition is fulfilled, it would not be proper for courts to get involved in “second-guessing such judgment calls with the benefit of hindsight, using a largely paper-based analysis and viewing the events from a timeframe perspective divorced from the reality of the speed at which the events occurred in real time.”<sup>58</sup>

[41] Although Beach J held that the directors were not liable, his Honour went further to opine that they would – in any event given the circumstances – be entitled to the protection afforded under the statutory business judgment rule as they fulfilled all the four requirements as set out in section 180(2). The decision to announce the takeover bid was a “business judgment” as defined in section 180(3) as had the transaction been successful, the company stood to reap potentially significant benefits.<sup>59</sup> Given these facts, Beach J had no hesitation in holding that the directors had rationally believed that the decision was taken in the best interests of the company,<sup>60</sup> highlighting that:

... it is important to adopt an *ex ante* perspective where one is not just looking at potential risks and downsides but also the potential benefits. That was the directors’ framework at the relevant time. And that is necessarily the framework within which s 180 must be analysed. A retrospective analysis of a transaction which did not proceed has the tendency to overlook that latter dimension.<sup>61</sup>

[42] The decisions in *Rich* and in *Mariner Corp Ltd* clearly highlight the tensions that exist with the interpretation of the business judgment rule. Part of the courts’ reluctance to review *bona fide* business decisions may be attributable to the inherent differences between the legal frameworks in Australia and the USA, which in turn reflects the

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57 Ibid, at [457].

58 Ibid, at [13].

59 Ibid, at [486]–[487] and [543].

60 Ibid, at [494], [548] and [551].

61 Ibid, at [13].

complexities of legal transplants between jurisdictions. To provide for a more complete understanding of this tension, the “rule that is not a rule” in the USA will be considered in the following section.<sup>62</sup>

### *The business judgment rule in the USA*

[43] The business judgment rule is multi-faceted and is not a “rule” at all given that it has no mandatory content. Its genesis in the USA may be traced back to the cases of *Percy v Millaudon*<sup>63</sup> and *Hodges v New England Screw Co.*<sup>64</sup> In the former, the court took the view that “the adoption of a course from which loss ensues cannot make the [director] responsible, if the error was one into which a *prudent man might have fallen*”<sup>65</sup> while in *Hodges*, the Supreme Court of Rhode Island further clarified this proposition by stating that “a Board of Directors acting in good faith and with reasonable care and diligence, who nevertheless fall into a mistake, either as to law or fact, *are not liable for the consequences* of such mistake”<sup>66</sup> (emphasis added). The modern form is perhaps most aptly set out in *Aronson v Lewis*<sup>67</sup> which defines the business judgment rule as “a presumption that in making a business decision the directors of a corporation acted on an *informed basis, in good faith and in the honest belief* that the action was taken in the best interests of the corporation”<sup>68</sup> (emphasis added).

[44] Most generally, the business judgment rule acts as a presumption in favour of corporate managers’ actions. Stronger still, the rule provides a safe harbour that makes directors and their actions unassailable if certain prerequisites have been met. In litigation, the rule is a means for conserving judicial resources, thereby permitting courts to avoid being mired down in rehashing decisions that are inherently subjective and ill-suited for judges, as opposed to business men and women. Last of all, the rule is the law’s implementation of broad economic policy, built upon economic freedom and the encouragement of informed risk-taking. In short, courts would refuse to second-guess the merits

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62 See Branson DM & CK Low, “Balancing the Scales: A Statutory Business Judgment Rule for Hong Kong?” (2004) Vol 32 Part II *Hong Kong Law Journal* 303.

63 8 Mart (ns) 68 (La 1829).

64 3 RI 9 (1853).

65 8 Mart (ns) 68 (La 1829) at 77–78.

66 3 RI 9 (1853) at 18.

67 473 A 2d 805 (Del 1984).

68 *Ibid*, at 812.

of the decisions of the board of directors if the directors had acted in good faith with due care and loyalty even if the company and/or its shareholders were harmed by those decisions.<sup>69</sup>

[45] As evident from the foregoing, the crux of the business judgment rule is a commitment by the judiciary in the US not to question the substance of actions taken by directors when there is no proof that the directors had acted badly or, plainly put, effectively a policy of judicial non-review. There are really only two formulations of the rule with wide currency, namely, the Delaware business judgment rule and the American Law Institute (“ALI”) formulation. Although not without its critics,<sup>70</sup> the ALI formulation seems to be the “better” of the two, having been adopted by the highest courts of several states.<sup>71</sup> In so far as it is relevant, it states that:

- (c) a director or officer who makes a business judgment in good faith fulfils the [duty of care] if the director or officer:
- (1) is not interested in the subject of his business judgment;
  - (2) is informed with respect to the subject of the business judgment to the extent the director or officer reasonably believes to be appropriate under the circumstances; and
  - (3) rationally believes that the business judgment is in the best interests of the corporation.<sup>72</sup>

[46] In short, directors and their decisions are protected from legal attack if:

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69 See e.g. *Bayer v Beran* 49 NYS 2d 2 (Sup Ct 1944); *Beard v Elster* 160 A 2d 731 (Del 1960); and *Aronson v Lewis* 473 A 2d 805 (Del 1984).

70 See e.g. Carney WJ, “Section 4.01 of the American Law Institute’s Corporate Governance Project: Restatement or Misstatement?” (1988) 66 *Washington University Law Quarterly* 239 at 271–288.

71 See e.g. *Rosenfield v Metals Selling Corp* 643 A 2d 1253, 1261 (Conn 1994); *Omnibank v United S Bank* 607 So 2d 76, 85 (Miss 1992); *Cuker v Mikalauskas* 692 A 2d 1042, 1045–1046 (Pa 1997).

72 See American Law Institute, *ALI Corporate Governance Project* (Philadelphia: American Law Institute, 1994), para 4.01(c). The ALI, founded in 1928, is the leading national law reform organisation in the US. Its membership includes the chief justices of the 50 US states’ supreme courts, the deans of all accredited law schools, and 2,200 elected members which include leading lawyers, judges and law professors. Its products are the restatements which, traditionally, codify and suggest incremental improvements in areas of law such as torts, contracts and conflicts of law that have, by and large, been left to case-by-case development.

- (a) they made a judgment or decision;
- (b) the decision-makers were free from disabling conflicts of interest;
- (c) they exercised some (not necessarily reasonable) care in informing themselves about the matter decided; and
- (d) they had a rational (not necessarily reasonable) basis for the decision they made.

[47] One function of the rule is as a conservator of judicial resources as the courts will not review the substantial merits of a board decision unless the directors had reached that decision through a grossly negligent process. If the rule had required “reasonable” care or a “reasonable” basis for every decision, then courts would have to hold plenary hearings or trials because it is in those *fora* that questions of reasonableness are decided. If so, the rule would not serve its function. Instead, if the four prerequisites as outlined above are present, the defending directors would only need to demonstrate some care and only a rational or plausible basis for the decision made.

[48] Delaware courts state the rule more succinctly and in the language of a “presumption”. Thus, the business judgment rule is “a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company”.<sup>73</sup> Delaware courts look for the same elements as do other courts, namely, a judgment or decision; some care; and good faith or the absence of conflicts of interest or base motive. A key difference is that – because of the use of presumption in Delaware – a plaintiff shareholder has the burden of going forward. The challenging shareholder must demonstrate that the collegial body (the board) was infected by conflicts of interests on the part of a critical group (although perhaps less than a majority) of directors.<sup>74</sup> Alternatively, the shareholder might offer credible proof that the directors merely rubber-stamped the decision of the chief

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73 *Aronson v Lewis* 473 A 2d 805 (Del 1984) at 812. The *Aronson* statement of the rule is the most quoted by Delaware courts eclipsing the earlier precedent of *Warshaw v Calhoun* 221 A 2d 487 (Del 1966) at 492–493 which contained similar but not identical phrasing.

74 *Cede & Co v Technicolor, Inc* 634 A 2d 345 (Del 1993) at 363–365 which noted that the factual question is how much self-dealing or other conflicts taint “the collective independence of the board”.

executive officer (“CEO”), and thus had not made a judgment or decision of their own.<sup>75</sup>

[49] The contrast between the approaches adopted by the ALI and the Delaware courts is thus highly evident. The former is a safe harbour where directors have the burden of establishing the presence of the elements of the business judgment rule. However, once they do so, the payoff is significantly greater as the director concerned would have sailed into an impregnable harbour against litigation arising from a “failed” business decision.

[50] On the other hand, the presumption as laid down by the courts in Delaware may be rebutted, meaning that defendant directors face the possibility of having to go through the ordeal of a trial in order to vindicate themselves. However, the burden shall initially fall upon the plaintiff to “rebut the presumption by introducing evidence either of director self-interest, if not self-dealing, or that the directors lacked good faith or failed to exercise due care”.<sup>76</sup> Should the plaintiff fail to do so the case is effectively over as the court will not ask whether the board made the correct, or best, decision. This approach is most succinctly articulated in *Cede & Co v Technicolor, Inc*<sup>77</sup> when the Delaware Supreme Court held that:

To rebut the rule, *a shareholder plaintiff assumes the burden of providing evidence that directors, in reaching their challenged decision, breached any one of the triads [sic] of their fiduciary duty – good faith, loyalty or due care. If a shareholder plaintiff fails to meet this evidentiary burden, the business judgment rule attaches to protect corporate officers and directors and the decisions they make, and our courts will not second-guess these business judgments. If the rule is rebutted, the burden shifts to the defendant directors, the proponents of the challenged transaction, to prove to the trier of fact the “entire fairness” of the transaction to the shareholder plaintiff.*<sup>78</sup> (Emphasis added.)

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75 *Smith v Van Gorkom* 488 A 2d 858 (Del 1985) which found a breach of duty where the directors made a decision to sell the company after a two-hour meeting, which was called on short notice with no documents or written analyses whatsoever, and essentially merely rubber-stamping the decision of an aged CEO who wanted to sell the company and retire.

76 *Citron v Fairchild Camera & Instrument Corp*, 569 A 2d 53 (Del 1989) at 64.

77 634 A 2d 345 (Del 1993).

78 *Ibid*, at 361.

### *Elements of the business judgment rule*

[51] There are five key components to the rule to the business judgment rule. First, there must have been a *decision or judgment* although sometimes it is said that there must be an *independent* judgment or decision as the mere rubber-stamping the CEO's or controlling shareholder's wish or command will not do. One of the classic cases involved a shareholder contention that, when the directors of the Chicago Cubs Baseball Club voted to uphold the decision of PK Wrigley – its majority owner and chewing gum magnate – to have no lights and therefore no night baseball, those directors were merely implementing Wrigley's inveterate belief that God meant baseball to be a game played in the daytime. According to the plaintiff minority shareholder, the reasoning given by the directors – that night baseball would ruin the neighbourhood surrounding the baseball park Wrigley Field – was pretextual.<sup>79</sup> Nonetheless, the Illinois court afforded business judgment rule protection to the Chicago Cubs' board of directors and its decision.

[52] More recently, the Delaware Chancellor refused to grant business judgment rule protection to the directors of The Walt Disney Company.<sup>80</sup> The directors had permitted the then powerful CEO Mr Michael Eisner to negotiate an employment contract with one of his close personal friends, namely, Hollywood dealmaker Mr Michael Ovitz. Fourteen months later the same directors permitted Eisner to engineer a no-fault termination for Ovitz under which the latter, who had been a dismal failure in the job, collected US\$140 million in severance benefits. The court noted that the directors of Walt Disney failed to make "any decision" and had adopted an "ostrich-like" approach to both the original employment contract and the later no

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79 *Shlensky v Wrigley* 237 NE 2d 776 (Ill Ct App 1968). See also *McMullin v Beran* 765 A 2d 910 (Del 2000) at 916–920 where the court held that directors of subsidiary were not entitled to business judgment rule protection because they delegated their decision to a parent corporation when they themselves "had an ultimate statutory duty and fiduciary responsibility to make an informed and independent decision"; and *Miller v Schreyer* 683 NYS 2d 51 (NY App Div 1999) at 54 which explained that "where the wrong alleged is inaction of the board rather than a conscious decision ... the business judgment rule is inapplicable". See also Holland RJ, "Delaware Directors' Fiduciary Duties: The Focus on Loyalty" [2009] Vol 11 No 3 *U of Pennsylvania Journal of Business Law* 675–701.

80 *In Re Walt Disney Co Derivative Litigation* 825 A 2d 275 (Del Ch 2003).

fault termination. Their decision was therefore not entitled to the business judgment rule protection.

[53] A more or less conscious decision to make no decision is also a judgment or decision for purposes of the rule's application.<sup>81</sup> However, veteran directors say that boards often act by consensus and that consensus builds by a process of accretion, and a requirement that matters be put to motions and votes encourages confrontation. It forces boards to act like legislative bodies or, worse yet, like faculty meetings at colleges and universities. The business judgment rule's emphasis on the process leading to formal judgments also constitutes make-work for lawyers who, as process engineers, come to have a larger role than they should have in the boardroom. Similarly, critics of the modern business judgment rule say that insistence on formal decisions places a premium on play-acting and on paper trails and that this does not improve the quality of decisions that are made.

[54] Secondly, the judgment or decision must be an informed one with the requirement being *some care* – not due care – as elucidated by the Supreme Court of Delaware in the famous (or infamous) case of *Smith v Von Gorkom*<sup>82</sup> when it stated that “[w]e think the concept of gross negligence is also the proper standard for determining whether a business judgment reached by a board of directors was an informed one.”<sup>83</sup> This statement has led arch-conservative commentators to argue that in the modern era, the standard of conduct has changed across the board to gross negligence or slight care, rather than due care,<sup>84</sup> while another noted commentator has urged that the standard to be applied should be a subjective standard, that is, to enquire whether the directors making the decision reasonably believe that they possessed sufficient information.<sup>85</sup> An alternative phrasing that asks how much

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81 *Brane v Roth* 590 NE 2d 587 (Ind Ct App 1992) at 592 where the court held that the “rule does not protect directors who have abdicated their position or absent a conscious decision, failed to act”.

82 488 A 2d 858 (Del 1985).

83 *Ibid*, at 873.

84 One of the most arch of the arch-conservatives was Charles Hansen, a St Louis practitioner, who repeatedly asserted in ALI meetings that the standard of conduct is gross negligence or lower: see Hansen C, “The ALI Corporate Governance Project: Of the Duty of Due Care and the Business Judgment Rule” (1986) 41 *The Business Lawyer* 1237 at 1241.

85 Joseph Hinsey IV, “Business Judgment and the American Law Institute’s Corporate Governance Project: The Rule, the Doctrine, and the Reality” (1984) 52 *George Washington Law Review* 609 at 613–614.

information is enough information – or what information-gathering mechanisms such as through consultants, committees and reports are sufficient – is itself a matter of business judgment. A recent judicial pronouncement in Delaware that goes part of the way toward those commentators' urging is that the "board is responsible for considering only *material* facts that are *reasonably available*, not those that are immaterial or out of the board's reasonable reach"<sup>86</sup> (emphasis added). The court's use of the words "reasonably available" and "reasonable reach" indicate that an objective – rather than wholly subjective – standard is still in place.

[55] Thirdly, there must be an absence of *disabling conflicts of interest* to ensure that the decision-making process is independent. Conflicts that disable, and those that do not, are at the antipodes of a spectrum. At the disabling antipode are direct pecuniary interests of the director, his or her family or associates or an affiliate of the director, in the judgment or decision for which the protections of the rule are sought. However, the receipt of normal directors' fees – or the desire to retain them – does not disable. In *Marx v Akers*,<sup>87</sup> the New York Court of Appeals held that, as a matter of law, the prospect of receipt of future directors' fees in the amount of USD\$80,000 per year did not disable the directors of IBM from setting those fees. A promise of continuation on the board after a change in control also does not disable and similarly the receipt by an investment banking firm of USD\$229,000 in annual fees did not disable the firm's partner from sitting on the board of Chevron Oil Co and from participating in a decision in which the firm had rendered advice.<sup>88</sup>

[56] That a director was the former neighbour of a senior executive of the corporation on the other side of a transaction did not disable as mere illusory allegations of "personal affinity" are insufficient to establish the required standard for lack of independence.<sup>89</sup> By contrast, receipt by a director of an undisclosed USD\$150,000 finder's fee did disable that director.<sup>90</sup> Decisions made by a board with a critical mass of directors wearing second hats as well-paid, long-term consultants,

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86 *Brethem v Eisner* 746 A 2d 244 (Del 2000) at 259, reversing in part *In Re The Walt Disney Co Derivative Litigation* 731 A 2d 342 (Del Ch 1998).

87 666 NE 2d 1034 (NY 1996).

88 *Katz v Chevron Corp* 22 Cal App 4th 1352 (1994) at 1368.

89 *Odyssey Partners v Fleming Cos* 735 A 2d 386 (Del Ch 1999) at 409–410.

90 *Cede & Co v Technicolor, Inc* 634 A 2d 345 (Del 1993) at 362.

hired and fired by the controlling shareholder, have been held as not being entitled to the business judgment rule protection.<sup>91</sup> Bank directors who circumvented local banking laws by forming a “competing loan company” were not entitled to the rule’s protection for that decision because they accepted management fees from the loan company.<sup>92</sup>

[57] Few universal principles may be stated. One may be that so-called structural bias, that is, the predilection of directors to favour those of the same social or economic class, such as fellow directors or senior managers, does not disable. The argument is frequently made in the context of recommendations by special litigation committees that derivative suits not go forward against fellow directors. The “there but for the grace of God go I”<sup>93</sup> motivation that may lurk behind a decision that litigation is not in the corporation’s best interests while real, is not generally speaking legally cognisable. Nonetheless, out of an abundance of caution, and also a subliminal recognition of the structural bias problem, most boards staff special litigation committees with new “expansion” directors who can in no way be alleged to have any connection with the alleged wrongdoing and against whom the structural bias argument has less force. Another universal principle is that if a single decision-maker seeks the protection of the business judgment rule then he or she must, “like Caesar’s wife, be above reproach”.<sup>94</sup>

[58] A sub-species of the conflict of interest species is that of the “dominated director”. Rather than a discernible pecuniary interest, what is alleged is that the director is beholden generally to a controlling

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91 *Clark v Lomas & Nettleton Fin Corp* 625 F 2d 49 (5th Cir 1980) at 52–53. Notably, this was also the case at Enron with a supermajority of directors also holding consulting contracts with the corporation: see e.g. “Enron – The Real Scandal”, *The Economist*, January 17, 2002 available at <http://www.economist.com/node/940091>.

92 *Warren v Century Bankcorporation Inc* 741 P 2d 846 (Okla, 1987) at 848.

93 This phrase is said when something bad that has happened to someone else could have happened to you: see e.g. *Cambridge Dictionary* at <http://dictionary.cambridge.org/dictionary/english/there-but-for-the-grace-of-god-go-i>.

94 *Kahn v Tremont Corp* 694 A 2d 422 (Del Ch 1997) at 430, quoting *Lewis v Fuqua* 502 A 2d 962 (Del Ch 1985) at 967. This idiom is used to advocate high standards of probity for if one is involved with a famous or prominent figure, then one must avoid attracting negative attention or scrutiny: see e.g. *The Free Dictionary* at <https://idioms.thefreedictionary.com/Caesar%27s+wife+must+be+above+su+spicion>.

shareholder or CEO, thus being disabled by his or her lack of independence. However, a plaintiff making such an argument faces an uphill battle as courts are loathe to find that an otherwise reputable business person is not his or her own person. Courts would rather rely on an identifiable pecuniary interest to ground a finding that a particular decision-maker was disabled. Nonetheless, such cases do succeed from time to time as held in *Gries Sports Enter v Cleveland Browns Football Co*<sup>95</sup> where a five-person board staffed by outside counsel, inside counsel, and a corporate employee, all of whom were beholden to the controlling shareholder, who occupied the fourth board slot, was found by the Ohio Supreme Court to have been dominated.<sup>96</sup> A special litigation committee was not sufficiently independent when the directors who staffed it were Stanford University professors reviewing actions taken by Oracle Inc, its CEO and a senior manager, all of whom had made or had promised to make substantial gifts to Stanford University.<sup>97</sup>

[59] By contrast, if counsel and other advisers scrub the board clean by removing all inferences of conflicts or of board domination and if independent non-executive directors convening in executive session run the decision-making process from start to finish, then their decision is entitled not only to the business judgment rule protection but also to the *heightened* business judgment rule protection.<sup>98</sup> What this means analytically is hard to say for it may just only be a word choice for emphasis. However, the result is clear, namely, that the decision made will be very nearly unassailable if the other elements of the business judgment rule are met.

[60] Fourthly, there must be a *rational basis* for the decision. Directors could be free of disabling, indeed all, conflicts or domination by gathering and digesting voluminous information, only to end up with not only an unwise and possibly “off-the-wall” decision. Under the ALI version, such a decision would not be entitled to the business judgment rule protection. For example, decisions to put a man on Mars, or to accept not only a lower but clearly inferior bid for the company,

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95 496 NE 2d 959 (Ohio 1986).

96 *Ibid*, at 968.

97 *In Re Oracle Corp Derivative Litigation* 824 A 2d 917 (Del Ch 2003).

98 *Ivanhoe P'ship v Newmont Mining Co* 535 A 2d 1334 (Del 1987) at 1343.

might be judgments lacking a rational basis.<sup>99</sup> On this score, some judges and commentators say that directors are not liable unless their decision or judgment was “manifest folly”.<sup>100</sup> Others say that directors’ decisions are unassailable unless they amount to a gross abuse of discretion. Those phrasings may be too permissive. By contrast, the statement that “all directorial decisions must have a sound business purpose”<sup>101</sup> goes too far in the other direction.

[61] Lastly, there is an umbrella requirement – brooding omnipresence – of *good faith*. In a transactional setting, an attorney advising a board might run through the elements of the business judgment rule as a checklist: judgment or decision, absence of disabling conflicts, some care, and a rational basis. He or she would then do well to pause, raise his or her head, and sniff – loudly and several times – just like all good lawyers who apply a “smell test”.<sup>102</sup> Thus, even if all of the law’s formal requirements have been met, if the deal under consideration does not feel right or smell right, directors should not do the deal. Alternatively, they should at the very least advise postponement until they dig down to the source of their olfactory concern.

[62] In the context of the business judgment rule, the umbrella requirement of good faith is a surrogate of sorts for a smell test. It also has particular utility in two more delimited areas. Firstly, when the decision-making process has been infected by illicit motives other than pecuniary conflicts. Revenge, spite, jealousy, or other base motives may be behind a decision. In such a case, the lack of good faith would be the proper means by which to attack the decision.<sup>103</sup>

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99 *Gimbel v Signal Cos, Inc* 316 A 2d 599 (Del Ch) at 610; affirmed in 316 A 2d 619 (Del 1974); cf *Paramount Communications, Inc v Time Inc* 571 A 2d 1140 (Del 1990) at 1152 where the court held that despite the decision to accept a clearly inferior bid in a merger of equals, the directors were nonetheless entitled to business judgment rule protection.

100 Arshat SS and Joseph Hinsey IV, “Codified Standard – Same Harbour but Charted Channel” (1980) 35 *The Business Lawyer* 947 at 956. See also n 81 above.

101 *Ski Roundtop, Inc v Hall* 658 P 2d 1071 (Mont 1983) at 1079.

102 See e.g. Roger Cramton, “Enron and the Corporate Lawyer: A Primer on the Legal and Ethical Issues” (2002) 58 *The Business Lawyer* 143.

103 *Re RJR Nabisco, Inc Shareholders Litigation* 1989 WL 7036 (Del Ch Jan 31, 1989) wherein the court stated at 1159 that “Greed is not the only human emotion that can pull one from the path of propriety; so might hatred, lust, envy, revenge, or ... shame or pride. Indeed any human emotion may cause a director to place his own interests, preferences or appetites before the welfare of the corporation”.

The second is knowing approval of illegal conduct. Directors who approved forgiveness of indebtedness by a political party when the forgiveness was tantamount to an illegal campaign contribution were not entitled to protection, even though they had no personal conflicts and they had a rational basis for the decision made.<sup>104</sup>

[63] Directors who knowingly and/or deliberately withhold material information from the board in order to mislead shareholders lack good faith. Under such circumstances, the shroud of protection otherwise afforded by the business judgment rule would fall to the ground.<sup>105</sup> A more recent case held that a cryptic and peremptory refusal of a demand from a derivative action plaintiff in a case of obvious wrongdoing constituted a lack of good faith. The court could thus examine and look into the merits of the denial of the demand itself.<sup>106</sup>

[64] The good faith requirement is something of a catch-all which also demonstrates the flexibility of the business judgment rule. For example, in a dominated director's case, a court could alternatively find that the directors rubber-stamped the decision of a controlling shareholder and made no judgment or decision; that the directors lacked independence; or that the directors lacked the required good faith. In nearly every business judgment rule case, judges have a number of "outs" although in their wisdom they may choose not to use them. This is as it should be because, first and foremost, the business judgment rule is a judicial construct – born out of judges' realisations about the limitations on their abilities – about conservation of the judicial resource and its proper role in business cases.

### *The additional requirements for takeovers*

[65] Takeovers – especially contested or hostile ones – can pose significant risks for directors of target companies who may face potentially inherent conflicts of interest which Moore J described as follows:

Because of the omnipresent specter that a board may be acting primarily in its own interests, rather than those of the corporation and

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104 *Miller v Am Tel & Tel Co* 507 F 2d 759 (3rd Cir 1974).

105 *Potter v Pholad* 560 NE 2d 388 (Minn Ct App 1997) at 395, applying Delaware law from *Emerald Partners v Berlin* 1995 WL 600881 (Del Ch Sep 22, 1995) at 7.

106 *Harhen v Brown* 710 NE 2d 224 (Mass Ct App) at 234–236; reversed at 730 NE 2d 859 (Mass 2000).

its shareholders, there is an enhanced duty which calls for judicial examination at the threshold before the protections of the business judgment rule may be conferred.<sup>107</sup>

[66] The foregoing appears to impose additional burdens upon the directors to show that: (i) they had reasonably perceived a threat to the company; and (ii) their defensive responses were proportional to that threat. However, these requirements were subsequently clarified by the then Vice-Chancellor Leo Strine in the following terms:

It is not at all apparent how a plaintiff could meet this burden in a circumstance where the board met its burden under *Unocal*. To the extent that the plaintiff has persuasive evidence of disloyalty (for example, that the board acted in a self-interested or bad-faith fashion), this would fatally undercut the board's *Unocal* showing. Similarly, it is hard to see how a plaintiff could rebut the presumption of the business judgment rule by demonstrating that the board acted in a grossly careless manner in a circumstance where the board had demonstrated that it had acted reasonably and proportionately. Least of all could a plaintiff show that the board's actions lacked a rational business purpose in a context where the board had already demonstrated that those actions were reasonable, *i.e.*, rational.<sup>108</sup>

[67] Further problems may be envisaged when a takeover involves a controlling shareholder on both sides of the transaction. However, these potential complexities are not necessarily insurmountable and the issue was recently addressed by the Delaware Supreme Court in *Kahn v M & F Worldwide*<sup>109</sup> where it held as follows:

[I]n controller buyouts, the business judgment standard of review will be applied if and only if: (i) the controller conditions the procession of the transaction on the approval of both a Special Committee and a majority of the minority stockholders; (ii) the Special Committee is independent; (iii) the Special Committee is empowered to freely select its own advisors and to say no definitively; (iv) the Special Committee meets its duty of care in negotiating a fair price; (v) the vote of the minority is informed; and (vi) there is no coercion of the minority.<sup>110</sup>

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107 *Unocal Corp v Mesa Petroleum Co* 493 A 2d 946 (Del 1985) at 954.

108 *In re Gaylord Container Corp S'holders Litigation* 753 A 2d 462 (Del Ch 2000) at 475–476.

109 88 A 3d 635 (Del 2014).

110 *Ibid*, at 645.

[68] The foregoing makes it abundantly clear that protection under the business judgment rule will only avail itself with a highly rigorous review of the processes. However, if the requisite conditions are fulfilled, the business judgment rule is invoked despite the initial conflict of interest. Alternatively, a far less onerous option presents itself, namely, to structure the transaction as a non-coercive tender offer of an exchange offer to acquire shares directly from the minority shareholders as in such transactions it will be for the shareholders "to accept or reject the tender based on their own evaluation of their best interests".<sup>111</sup>

### **The way forward for Malaysia?**

[69] Over the past couple of decades the "good" governance movement has increasingly contemplated boards comprised of a super majority of truly independent directors who are free of any significant financial or even social ties to the senior executives.<sup>112</sup> Today, traditional pools of candidates for board service such as the trusted outside lawyer, retired partner of accounting firms or commercial banker are increasingly considered non-independent and are becoming a rarity of sorts on boards of directors in many countries.

[70] This is more so in Asia where a large number of publicly listed companies are either family or state-owned or are considered government-linked. This makes it all the more important to ensure the efficacy and robustness of a business judgment rule so as to encourage truly independent persons to serve as directors since "persons of reason, intellect and integrity would not serve if the law exacted from them a degree of prescience not possessed by others".<sup>113</sup> Once on the board, a strong business judgment rule is necessary to encourage these directors to engage in the type of informed risk-taking that is essential to business success.

[71] Returning to the judicial point of view, courts are ill-equipped to review business decisions. These decisions often involve intangibles, intuitive insights or surmises as to business matters such as competitive

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111 *In re Siliconix Inc, S'holders Litigation* 2001 WL 716787 (Del Ch June 19, 2001) at 6.  
112 See e.g. Branson DM, "Corporate Governance 'Reform' and the New Corporate Social Responsibility" (2001) 62 *University of Pittsburgh Law Review* 605 at 627 where he describes the "good governance movement".

113 Arsht S, "The Business Judgment Rule Revisited" (1979) 8 *Hofstra Law Review* 93 at 97.

outlook, cost structure, as well as economic and industry trends. Business decisions often come down to matters of touch and feel, not susceptible to systematic analysis. In the circumstances, the business judgment rule is a filter that enables courts to screen out non-meritorious or vexatious challenges to the actions of directors and executives which serve no purpose save to divert management time and effort from more worthwhile activities.

[72] Although section 214 substantially mirrors its Australian counterpart, namely, section 180(2) of the Corporations Act 2001 – which is not surprising since it was the source of the Malaysian provision – it should not necessarily follow that we should restrict ourselves strictly to a consideration of Australian jurisprudence. This is especially so since the Australian provision was itself influenced by developments in the common law business judgment rule in the USA.

[73] In the circumstances, which route would likely suit Malaysia better? It is suggested that the statutory language allows for an interpretation based on a “hybrid Australian-ALI” approach as there is no reason why we cannot adopt the best practices in both jurisdictions to achieve an appropriate balance between allowing for calculated risk-taking by directors on the one hand and potential lawsuits by the company and/or shareholders should directors fall short of reasonable expectations on the other. In short, this will provide a safe harbour for directors who are able to establish – on the balance of probability – the four elements as set out in section 214 albeit to the reasonable person objective standards that are set out in the provision.

[74] The decisions in *Australian Securities and Investments Commission v Rich* and in *Australian Securities and Investments Commission v Mariner Corp Ltd* will provide some guidance given section 214 of the Companies Act 2016 draws substantially – although not verbatim – from its Australian counterpart, namely section 180(2) of the Corporations Act 2001. In fact, the decision of Austin J in *Australian Securities and Investments Commission v Rich* – as regards the reasonableness of belief – has been applied by Nallini Pathmanathan J, as she then was, in *Petra Perdana Berhad v Tengku Dato’ Ibrahim Petra bin Tengku Indra Petra & Ors* wherein her Ladyship set down some reference points against which this was to be assessed namely:

- (a) the importance of the business judgment that is to be made;
- (b) the time available for obtaining information;

- (c) the costs related to obtaining information;
- (d) the director's confidence in exploring the matter;
- (e) the state of the company's business at that time and the nature of the competing demands on the board's attention; and
- (f) whether or not the information is available to the director.<sup>114</sup>

[75] This approach may mean that directors will effectively have "two bites of the cherry" since they can first try to avail themselves of a "safe harbour" which is impregnable to lawsuits but should they fail they still have the option of adducing evidence to show that they fulfilled the standard of care expected of them as set out in section 213(2). However, it must be emphasised that key in determining whether protection under the business judgment rule applies is through a close scrutiny of the *decision-making process* and not the general state of knowledge of the directors. The latter falls within the ambit of section 213(2) and hence the phrase "two bites of the cherry".

### Conclusion

[76] It would be prudent to recognise section 214 of the Companies Act 2016 for what it is, namely, a statutory compromise between two competing policy objectives. On the one hand it seeks to recognise the director's authority to make decisions without being second-guessed, while on the other it seeks to ensure that the director remains accountable. However, one should not adopt an over-reliance on the subjective state of mind of directors in relation to both the process adopted to inform themselves and to whether a business judgment is in the best interests of the corporation, for without an objective element in the business judgment rule, the standard of care required of directors may become overly protected and, as a consequence, the objective of accountability is compromised.

[77] It is trite that an ideal board of directors will always be careful, loyal and act in good faith. However, directors as ordinary human beings are not infallible. As highlighted by both Austin J in *Australian Securities and Investments Commission v Rich* and by Nallini Pathmanathan J, as she then was, in *Petra Perdana Berhad v Tengku Dato' Ibrahim Petra bin Tengku Indra Petra & Ors*, the protection afforded under section 214 may

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114 [2014] 4 AMR 658 at 757.

be available even if a director was not aware of all available information material to the business decision so long as it can be proven that he or she reasonably believed that he or she had taken appropriate steps to inform him or herself about the subject matter during the course of the decision-making process.

[78] As the complexity and sophistication of business activities increase with operations extending beyond borders and across industries, so too does the demand on management – especially on boards of directors of companies – to ensure that appropriate standards of corporate governance are implemented and enforced. Significantly, the Federal Court of Australia has held in *Australian Securities and Investments Commission v Cassimatis (No 8)*<sup>115</sup> that directors may be liable for breaches of their duty even if they are the sole shareholders of the company. Whether a director has discharged the duty that is owed to the company involves the assessment of a number of factors including the foreseeable risk of harm to the interests of the company, the magnitude of that harm, the potential benefits accruing from the director’s conduct and the burden to the company of any action to alleviate the foreseeable harm. In this case, Edelman J opined that “harm” meant harm to any of the interests of the company – which is not confined merely to financial harm – and does not require proof of actual or prospective loss as it can extend to the intangibles such as harm to the reputation of the company.

[79] With increasingly onerous demands imposed upon directors of companies – who are often viewed as the primary gatekeeper – there is a need to “balance the scales” so that the office remains sufficiently desirable to attract and retain the next generation of corporate leaders. To this end, courts should prudently refrain from the exercise of judicial activism to interfere with, and to substitute their own judgment in, business decisions that are properly the domain of directors where these are done carefully, loyally and in good faith. The statutory business judgment rule as set out in section 214 provides an avenue to attain these objectives and a pragmatic approach by the judiciary would go a long way towards the same.

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115 [2016] FCA 1023.

# The Shine on *Semenyih Jaya*: Resurrecting Judicial Power

by

*Dato' Dr Gurdial Singh Nijar\**

[1] On April 20, 2017, the Federal Court delivered a decision in *Semenyih Jaya Sdn Bhd v Pentadbir Tanah Daerah Hulu Langat & Anor*<sup>1</sup> ("*Semenyih Jaya*"). It brought into sharp focus several crucial intertwined issues relating to the nature of the pivotal role of the judiciary in our country's constitutional architecture. Yet, it has kindled little interest. Many in the judiciary seem quite indifferent to its ramifications. Academia has hardly raised any speculative problems even for the sheer pleasure of resolving them.<sup>2</sup>

[2] Will this Federal Court decision be hailed in Malaysian judicial annals as a monumental *cause celebre*, or as an unfortunate aberration of judicial overreach? The aim here is to provide a conceptual framework for understanding and analysing the decision. This article is arranged as follows:

- A. The antecedent context in which the case arose;
- B. The decision;
- C. An analysis of the case and its ramifications;
- D. Does the case go beyond the Land Acquisition Act 1960 (Act 486)?

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1 [2017] 4 AMR 123; [2017] 5 CLJ 526. The panel comprised of Federal Justices: Zulkefli Ahmad Makinudin (CJ (Malaya)), Hasan Lah, Zainun Ali, Abu Samah Nordin and Zaharah Ibrahim. The decision was delivered by Zainun Ali FCJ.

2 Pierre Bourdieu, "The Scholastic Point of View" (1990) 5 *Cult Anthropol* 380.

E. Judicial activism and judicial review; and

F. The future.

## A. The antecedent context

### *The genesis*

[3] It has always been the assumption that two crucial elements underpin the jurisdiction of our courts. One, that the judiciary is a distinct and separate part of the governance structure under the Federal Constitution. The other two arms of government are the legislature (the law-making body) and the executive (the law-applying body). This distribution of the governance of the State to the three organs reflects the idea of the separation of powers first theorised by Aristotle in his *Politics*;<sup>3</sup> and later made famous by Montesquieu in *De L'Esprit des Lois*.<sup>4</sup> AV Dicey suggested that this separation of powers is vital in a country whose constitution is based on the rule of law.<sup>5</sup> The rule of law is incorporated in our constitution *vide* the definition of law in Article 160(2). It is defined to include the common law of England. And as the Federal Court declared, “the rule of law forms part and parcel of the common law of England”.<sup>6</sup> The Federal Court in *Loh Kooi Choon v Government of Malaysia*<sup>7</sup> was more pointed, identifying the rule of law as one of the three basic concepts of the constitution:

The third basic concept is that no single man or body shall exercise complete power, but that it shall be distributed among legislative and judicial branches of government, compendiously expressed in modern terms that we are a government of laws, not men.

Critically, the separation of powers means that neither the executive nor the legislature can curtail the function of the judiciary.

[4] Two, the role of the judiciary is to uphold the fundamental

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3 <http://www.gutenberg.org/cache/epub/6762/pg6762.txt>.

4 English translation by Thomas Nugent: *The Spirit of Laws* (Kitchener: Batoche Books, 2001); <https://socialsciences.mcmaster.ca/econ/ugcm/3ll3/montesquieu/spiritoflaws.pdf>.

5 Albert Venn Dicey, *Introduction to the Study of the Law of the Constitution* (5th ed 1897) (1885).

6 *Lee Kwon Woh v PP* [2010] 2 AMR 231, FC at 242; [2009] 5 MLJ 301, FC at 314–315.

7 [1977] 2 MLJ 187 at 188, per Raja Azlan Shah LP.

precepts of the constitution. It ensures that the constitution is not violated. This task assumes particular importance when there is a contestation between the citizenry and the executive or any governmental department. Hence the judiciary must be independent of the executive. Violation of these aspects – the separation of powers buttressed by an independent judiciary – leads to constitutional authoritarianism, where the other arms of government assume the right to curtail judicial power.

### *Judicial power in the Federal Constitution*

[5] Judicial power is embedded in Part IX of the Federal Constitution in Article 121. The original text read as follows:

The judicial power of the Federation shall be vested in a Supreme Court and such inferior courts as may be provided by federal law.

[6] Then in 1963 *vide* Act 26/1963 the text was amended to read as follows:

... the judicial power of the Federation shall be vested in two High Courts of co-ordinate jurisdiction and status, namely –

(a) One in the States of Malaya ...;

and

(b) One in the States of Sabah and Sarawak,

and in such inferior courts as may be provided by federal law.

[7] The amendment took effect on September 16, 1963 – and was prompted by Singapore’s departure from Malaysia on this date.

[8] There was no structural change effected by the amendment. The expression “as may be provided by federal law” related to the creation of the courts and not its power. This is made clear by the section from which the “vesting” power phraseology is derived, namely, section 71 of the Australian Constitution.<sup>8</sup> It reads:

The judicial power of the Commonwealth shall be vested in a Federal Supreme Court, to be called the High Court of Australia, and in such

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<sup>8</sup> As stated in *Kok Wah Kuan v PP* [2007] 4 AMR 568; [2007] 4 CLJ 454, CA.

other federal courts as the Parliament creates, *and in such other courts as it invests with federal jurisdiction.* (Emphasis added.)

[9] Significantly, the courts remained the sole repository of judicial power drawing their jurisdiction from the Federal Constitution on the basis of the separation of powers.

### *The 1988 Amendment*

[10] In 1988, Article 121 was further amended vide the Constitution (Amendment) Act 1988 (Act A704).<sup>9</sup> The amendment deleted the words “the judicial power of the Federation shall be vested in the High Courts and the inferior courts of the country”, and replaced these with the statement that the courts “shall have such jurisdiction and powers as may be conferred by or under federal law”. The intent was to clip the judicial power of the courts and to limit it to what the other branches of government prescribed. It has been described as essentially the response of a government intent on stopping its executive and legislative authority from being scrutinised or undone by judicial decisions.<sup>10</sup> The International Commission of Jurists described the amendment as a “threat to the structural independence of the judiciary”.<sup>11</sup> The former Lord President cited this report to express his concern of the amendment.<sup>12</sup>

### *Judicial power reasserted*

[11] A decade later the Court of Appeal through Justice Gopal Sri Ram made the first direct assertion that the amendment had not divested the courts of the judicial power of the Federation, and that the constitutional separation of powers remained intact. This was in the 2007 decision of *Kok Wah Kuan v PP*<sup>13</sup> (“*Kok Wah Kuan*”). The decision made clear that “judicial power” – to decide disputes between the government and its citizens, as well as between subjects in civil and criminal matters – lies only with the judiciary under Article 121(1) of the Federal Constitution.

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9 It came into effect on June 10, 1988.

10 Andrew Harding, *The Constitution of Malaysia: A Contextual Analysis* (Hart Publishing, 2012).

11 *Report on Malaysia, International Commission of Jurists*, August 13, 2001.

12 Sultan Azlan Shah, “The Role of Constitutional Rulers and the Judiciary Revisited” in Sinnadurai, V (ed), *Constitutional Monarchy, Rule of Law and Good Governance* (Professional Law Books, 2004), p 385.

13 [2007] 4 AMR 568; [2007] 4 CLJ 454, CA.

[12] All this was to change when *Kok Wah Kuan* was heard by the Federal Court in 2007. A 4-1 majority ruled that the jurisdiction and powers of the High Court will be as prescribed by federal law. Meaning, it was for Parliament to decide on what powers it will give to, or take away from, the judiciary. Essentially the legislature, and by extension the executive, ruled – through its control of the majority in the legislature. In 2009, another bench of the Federal Court refused to disturb the decision.

[13] In one fell sweep, *Kok Wah Kuan* repudiated the doctrine of the separation of powers. “This doctrine is not a provision of the Malaysian Constitution”, declared the Federal Court. This ignored the trail of authorities cited by the Court of Appeal in *Kok Wah Kuan* referred to above that the constitution is largely structured such as to distribute power to the three institutions: the legislative, the executive and the judiciary. This structure implies that the basic principle of the separation of powers will apply. It is this structural arrangement that led Sir Owen Dixon, regarded as Australia’s pre-eminent jurist and a former Chief Justice of the High Court of Australia, to conclude:

If you knew nothing of the separation of powers, if you made no comparison of the American instrument of government with ours, if you were unaware of the interpretation it had received before our Constitution was framed according to the same plan, you would still feel the strength of the logical inferences from Chapters I, II and III and the form and content of ss 1, 61 and 71. It would be difficult to treat it as a mere draftsman’s arrangement.<sup>14</sup>

[14] *Kok Wah Kuan* effectively demolished the independence of the judiciary and the rule of law. Parliamentary supremacy trumped constitutional supremacy – a clear violation of the Federal Court’s 1976 landmark ruling in *Ah Thian v Government of Malaysia* (see paragraph [26] below).

[15] Lord Diplock, speaking for the Privy Council a year later in 1977, had counselled particular caution in interpreting a federal constitution “in which the question immediately in issue may have depended in part upon the separation of the judicial power from the legislative or executive power of the federation ...”: *Moses Hinds & Ors v The Queen*.<sup>15</sup>

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14 *R v Kirby, Ex p Boilermakers’ Society of Australia* (1954) 94 CLR 254 at 275.

15 [1977] AC 195.

[16] It is noteworthy that several courts thereafter continued to assume that they could exercise such powers, and that the amendment to Article 121 did not alter the legal status of judicial power. It vested entirely in the courts: *Dato Seri Anwar Ibrahim v PP*.<sup>16</sup>

### **B. The *Semenyih Jaya* case**

[17] The case started rather innocuously. The appellant company's land was acquired by the government. Dissatisfied with the compensation awarded by the land administrator, it lodged an appeal with the courts. The High Court (and later the Court of Appeal) rejected the company's claim for a further RM18.2 million for loss of profits and related development costs. The decision of the High Court was made by two assessors who sat with the judge. The judge had no role in the decision making. This radical change in the structure of the adjudicatory scheme to exclude the judge and vest such power almost entirely with the assessors was brought about by an amendment to the Land Acquisition Act 1960 (Act 486) ("LAA") which took effect on March 1, 1998.<sup>17</sup>

[18] The key constitutional issue that arose for consideration by the Federal Court, pursuant to the grant of leave, was "whether the amendment was valid in the face of Article 121 of the Constitution that contemplates that judicial power of the courts should be exercised by judges only". This necessitated an analysis of Article 121 and the impact of the amendment to the scope of this Article.

[19] In this context, the Federal Court traced the history of the role of the two assessors who were to sit with the judge. Initially, they were merely to aid the judge on the issue of compensation. This power was later removed completely,<sup>18</sup> but restored at a subsequent date.<sup>19</sup> Then by the latest amendment to section 40D of the LAA their role was broadened, from advisors to fact-finders and sole adjudicators as to the amount of compensation payable. Their decision was final and non-appealable.

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16 [2010] 5 AMR 677 at 741, [43]; [2010] 5 MLJ 145, FC at 182, [55]: "... it is incumbent to revert once more to the art 121 as the constitutional source of judicial power ...".

17 Land Acquisition (Amendment) Act (Act A499): amending s 40D(3) and the proviso to s 49.

18 *Vide* Act A575 with effect from January 20, 1984.

19 *Vide* Act A999.

[20] In a masterly analysis, Justice Zainun Ali speaking for the Federal Court, ruled that the judicial power of the court resides in the judiciary and no other. It is exercisable by a judge and no one else. Non-members of the judiciary – in this case, the assessors – had no right to exercise that power. The upshot was that the amendment was declared *ultra vires* Article 121 of the Federal Constitution. It overruled the earlier Federal Court *Kok Wah Kuan* decision which held to the contrary.

### *The reasoning*

[21] The Federal Court held that *Kok Wah Kuan* gave an unduly narrow interpretation of Article 121(1) by holding that the specific jurisdiction and powers of the High Court were as conferred by federal law. In the words of Justice Abdul Hamid Mohamad:

But to what extent such judicial powers are vested in the two High Courts depend on what federal law provides, not on the interpretation the term (*sic*) “judicial power” as prior to the amendment. That is the difference and that is the effect of the amendment.<sup>20</sup>

[22] Justice Zainun had no difficulty in demonstrating the rather facile nature of the argument – resisting Justice Hamid’s over-literalist approach in interpreting the constitution in these terms:

Whilst it is correct to say that the powers of the High Courts to adjudicate legal disputes are those which have been conferred by Federal laws, in our view the legal implication of Article 121(1) extends well beyond that. In this connection, there is general acceptance that the Federal Constitution has to be interpreted organically and with less rigidity ...

[23] Approving the strong dissent of Justice Richard Malanjum in *Kok Wah Kuan* that the courts – as the third arm of the government – cannot be relegated to the role of “servile agents of a Federal Act of Parliament ... to perform mechanically any command or bidding of a federal law”, the Federal Court ruled that the amendment had the effect of undermining the judicial power of the judiciary; and that this impinged on two central basic features of the Federal Constitution, namely:

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20 [2017] 4 AMR 123 at 146, [70]; [2017] 5 CLJ 526 at 555, [68].

- (i) The doctrine of separation of powers; and
- (ii) The independence of the judiciary.

[24] Bestowing sovereignty of Parliament (one wing of government) over the judiciary (another such wing) was manifestly inconsistent with these basic features. Consequently it was a law passed after Merdeka Day which was inconsistent with the Federal Constitution and rendered void by Article 4(1) of the Federal Constitution.

[25] The Federal Court elaborated on the reasons why Parliament does not have the power to amend these basic features of the Federal Constitution.

[26] First, allowing Parliament to circumscribe the jurisdiction of the courts would establish Parliamentary supremacy and suborn the judiciary to Parliament. This was contrary to the consistent past pronouncements of the Federal Court, such as *Ah Thian v Government of Malaysia*<sup>21</sup> and *Sivarasa Rasiah v Badan Peguam Malaysia & Anor.*<sup>22</sup> In the former case, the then Lord President Suffian made clear that:

The doctrine of Parliamentary supremacy does not apply in Malaysia. Here we have a written constitution. The power of Parliament and of state legislation in Malaysia is limited by the Constitution, and they cannot make any law they please.

[27] *Semenyih Jaya* approved the *dictum* of Gopal Sri Ram (then FCJ) in *Sivarasa* that:

Parliament cannot enact laws (including Act amending the Constitution) that violate the basic structure.

[28] Reliance was placed on the Privy Council decision in *Liyange v The Queen*<sup>23</sup> which struck down as void any law that allowed usurpation of judicial powers by the legislature. Reaching to the Supreme Court of India's decision in *Indira Nehru Gandhi v Raj Narain*,<sup>24</sup> Justice Zainun established the critically integral link between the separation of powers and the exclusivity of judicial power which carries with

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21 [1976] 1 LNS 3; [1976] 2 MLJ 112.

22 [2010] 2 AMR 301; [2010] 3 CLJ 507.

23 [1967] 1 AC 259.

24 AIR 1975 SC 2299.

it the independence of the judiciary. In her Ladyship's characteristic succinct style:

The important concepts of judicial power, judicial independence and the separation of powers are as critical as they are sacrosanct in our constitutional framework.<sup>25</sup>

### *Section 40D unconstitutional*

[29] On this fundamental conceptual framework, the Federal Court then examined the constitutionality of the particular offending section in the LAA, namely section 40D. It held that the power to award compensation was a judicial power under Article 121 of the Federal Constitution; that the section conferred power on a non-judicial person and that this violated Article 121(1) of the Federal Constitution.

[30] In addition to our Supreme Court judgment by Mohd Azmi SCJ in *PP v Yap Peng*,<sup>26</sup> a plethora of high authority judgments from various jurisdictions were cited to buttress the conclusion. Amongst them are *Hinds v The Queen*,<sup>27</sup> *AG Australia v The Queen & the Boilermakers Society*,<sup>28</sup> and *De Lange v Smuts*.<sup>29</sup>

### **C. An analysis of the case**

[31] The first and quintessential proposition that emerges from *Semenyih Jaya* is that Parliament cannot enact any law that violates the basic structure of the Federal Constitution – namely judicial power, judicial independence and the separation of powers. It will be struck down as unconstitutional.

[32] Does this not detract from Article 159(1) which allows for amendments to the Federal Constitution? The Article reads:

Subject to the following provisions of this Article and to Article 161E the provisions of this Constitution may be amended by *federal law*. (Emphasis added.)

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25 *Semenyih Jaya* [2017] 4 AMR 123 at [91]; [2017] 5 CLJ 526 at [90].

26 [1987] 1 CLJ 550.

27 [1976] AC 195, PC at 213, per Lord Diplock.

28 [1957] AC 288, PC.

29 [1998] (3) SA 785, Constitutional Court of South Africa.

[33] It is submitted that this Article must be read in conjunction with Article 4(1) which states:

This constitution is the supreme law of the Federation and *any law passed after Merdeka Day* which is inconsistent with *this Constitution* shall be void to the extent of such inconsistency. (Emphasis added.)

[34] The reference in Article 4(1) is to render void any law passed after Merdeka Day. This refers to all Acts of Parliament that is federal law, under Article 159(1). What is rendered void is any such federal law that is inconsistent with “this constitution”. That is to say, the Federal Constitution read as a whole. This must perforce refer to any law that seeks to alter any basic feature of the Federal Constitution. That is to say to its construct – the most fundamental of which is the separation of powers.

[35] The cumulative effect of this reasoning thus accommodates and reconciles with ease the basic structure concept established by *Semenyih Jaya* with Article 159(1). To reiterate, any federal law must not alter the basic structure of the Federal Constitution.

[36] This argument can be supported by taking a simple example. Can Parliament abolish elections, or even the institution itself, turning the country into an absolute dictatorship by the expedient of amending the several provisions of the Federal Constitution that deal with elections and related provisions? Surely not, on the basis that Article 4(1) would be violated as the amendments would be inconsistent with “this constitution” as established on Merdeka Day. That is with its basic structure, which involves the existence of the three arms of government and the separation of each from the other; the make-up of the legislature through elections and the consequent establishment of the executive.

#### **D. Does *Semenyih Jaya* go beyond the Land Acquisition Act 1960 (Act 486)?**

[37] There have been mixed signals, including by some panels of the apex court, that the decision is limited to the issue of whether non-judicial persons can adjudicate cases in court and is confined to matters relating to the LAA. This view has been expressed explicitly as well as implicitly.

[38] An example of the latter emerged recently. It involved a challenge to the decision by the Director General of Immigration (“DG”) of Sabah banning a Malaysian citizen from entering Sabah. The applicant sought judicial review of the DG’s order. One of the grounds was that section 59A of the Immigration Act 1959/63 (Act 155) – which explicitly ousted judicial review (except for a narrow range of procedural infirmities) – was unconstitutional; and that the Federal Court decision in *Pihak Berkuasa Negeri Sabah v Sugumar Balakrishnan*<sup>30</sup> (“*Sugumar*”) which had held this ouster provision as valid needed to be revisited. The application was dismissed by the High Court and the Court of Appeal.

[39] The applicant applied for leave to appeal to the Federal Court. One of the questions on which leave was sought was the necessity to reconsider *Sugumar* (decided some 15 years earlier) in the light of *Semenyih Jaya*. The Federal Court in *Semenyih Jaya* had ruled that judicial review was an integral constituent of the concepts that underpinned the basic structure of the Federal Constitution, in particular the separation of powers and the independence of the judiciary. Justice Zainun had identified judicial review as a key “check and balance” mechanism guaranteeing the preservation of the concepts of judicial power, judicial independence and separation of powers and ultimately the rule of law. In her translucent pronouncement, these concepts “... have been juxtaposed time and again in our judicial determination of issues in judicial reviews. Thus an effective check and balance mechanism is in place to ensure that the executive and the legislature act within their constitutional limits and that they uphold the rule of law. The Malaysian apex court had prescribed that the powers of the executive and the legislature are limited by the Constitution and that the judiciary acts as a bulwark of the Constitution in ensuring that the powers of the executive and the legislature are to be kept within their intended limit.”

[40] This echoed the words of the Federal Court in *Pengarah Tanah dan Galian, Wilayah Persekutuan v Sri Lempah Enterprise Sdn Bhd*<sup>31</sup> and made clear beyond peradventure that a provision in any federal law ousting judicial review (as upheld in *Sugumar*) would

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30 [2002] 3 AMR 2817; [2002] 3 MLJ 72.

31 [1979] 1 MLJ 135.

be antithetical to the rule of law and judicial independence and consequently unconstitutional. The refusal by the Federal Court to refuse leave on this question<sup>32</sup> neutered the effect of *Semenyih Jaya*. In effect it rejected the role of judicial review in upholding the basic construct of the Federal Constitution. Henceforth, Parliament would be free to enact any law to undermine the basic structure of the Federal Constitution.

[41] Such a judicial stance also ran foul of the plethora of cases both before and after *Sugumar* declaring that judicial review could not be ousted, no matter how widely worded the Act of Parliament was. Starting with the 1975 decision by the late administrative law doyen Justice Eusoffe Abdoolcader in *Sungai Wangi Estate v Uni*<sup>33</sup> declaring as of no effect any provision in a law that sought to immunise administrative decisions from judicial scrutiny. This legal proposition was followed and repeated in several other key cases: see for example *Enesty Sdn Bhd v Transport Workers Union & Anor*;<sup>34</sup> *Government of Malaysia & Ors v Loh Wai Kong*;<sup>35</sup> *Minister of Home Affairs v Persatuan Aliran Kesedaran Negara*;<sup>36</sup> *Syarikat Kenderaan Melayu Kelantan Bhd v Transport Workers' Union*;<sup>37</sup> *Hoh Kiang Ngan v Mahkamah Perusahaan Malaysia & Anor*;<sup>38</sup> *R Ramachandran v The Industrial Court of Malaysia*;<sup>39</sup> and *Majlis Perbandaran Pulau Pinang v Syarikat Berkerjasama-sama Serbaguna Sungai Gelugor dengan Tanggungan*.<sup>40</sup>

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32 The questions were as follows: (a) Was the decision of the Federal Court in *Pihak Berkuasa Negeri Sabah v Sugumar Balakrishnan* [2002] 3 AMR 2817; [2002] 3 MLJ 72 *per incuriam* and for that reason is not binding as precedent for cases dealing with s 59A of the Immigration Act 1959/1963?; and (b) Whether *Sugumar's* case is still good law on the question of ouster of judicial review in the light of the post-*Sugumar* apex court decisions (the most recent: *Semenyih Jaya Sdn Bhd v Pentadbir Tanah Daerah Hulu Langat & Anor* [2017] 4 AMR 123; [2017] 5 CLJ 526) which state that judicial review/access to justice is an integral component and a basic feature of the Federal Constitution and cannot be ousted? See *Ambiga Sreenevasan v Director of Immigration, Sabah & Ors* (Federal Court Application No. 08-398-08/2016).

33 [1975] 1 MLJ 136.

34 [1986] 1 MLJ 18.

35 [1979] 2 MLJ 33.

36 [1990] 1 CLJ Rep 186.

37 [1995] 2 AMR 1601; [1995] 2 MLJ 317.

38 [1996] 3 AMR 3693; [1995] 3 MLJ 369.

39 [1997] 1 AMR 433; [1997] 1 MLJ 145.

40 [1999] 3 AMR 3529; [1999] 3 MLJ 1.

[42] The post-*Sugumar* decisions were also to the same effect. In *Minister of Finance, Government of Sabah v Petrojasa Sdn Bhd*<sup>41</sup> the Federal Court stated the current state of the law on ouster clauses of the kind envisaged by *Sugumar*:

The position *now* is that the courts in the Commonwealth, Malaysia including, have moved away from the traditionalist approach that the Crown can do no wrong. Therefore, the courts in Commonwealth jurisdictions generally have held that the executive arm of the government is amenable to judicial review proceedings. (Emphasis added.)

[43] This was followed by *YAB Dato' Dr Zambry bin Abd Kadir & Ors v YB Sivakumar a/l Varatharaju Naidu (Attorney General Malaysia, intervener)*<sup>42</sup> and *Sivarasa Rasiah v Badan Peguam Malaysia & Anor.*<sup>43</sup>

[44] Remarkably, the Federal Court, in refusing leave on these critical questions, snubbed nine pre-*Sugumar* and four post-*Sugumar* decisions.

### E. Judicial activism and judicial review

[45] Judicial review has been correctly described as a cornerstone of good governance.<sup>44</sup> What is crucial in matters of such review is the role of the courts in upholding the fundamental precepts of the Federal Constitution. In this context, *Semenyih Jaya* stands out as a shining example. The Federal Court ruled as unconstitutional a statutory provision because it violated the basic structure of the Federal Constitution by circumscribing the jurisdiction of the judiciary. It bears reiteration that the courts should not for the sake of preserving comity defer to the legislative/executive will. Else, as noted earlier, we end up with “constitutional authoritarianism” – where the other arms of government assume the right to curtail judicial power through the use of the executive’s majority in the legislature. This renders Parliament (and not the Federal Constitution) supreme and consequentially suborns the judiciary to Parliament, as ruled the Federal Court. In this respect, courts cannot limit their role to merely interpreting the language of the law enacted by Parliament. For it is this that would subvert the rule of law and the constitutional construct of a democratic

41 [2008] 5 AMR 1 at 23, [41]; [2008] 4 MLJ 641 at 665, [78].

42 [2009] 5 AMR 604; [2009] 4 MLJ 24.

43 [2010] 2 AMR 301; [2010] 2 MLJ 333.

44 Md Raus Sharif, “Judicial Review: The Malaysian Experience” July [2017] JMJ 1–28.

nation. In this sense the space of judicial discourse is subject to constraints; that is to say that judges cannot decide cases in whatever way they like in systems committed to the rule of law,<sup>45</sup> as *Semenyih Jaya* illustrates. Finally, as courts operate within a socially organised order, they need to pay attention not only to the “legal legitimacy” of their decisions, but also to social legitimacy considerations.<sup>46</sup> Such considerations should pull judges towards judicial activism. And, as Raja Azlan Shah said on his elevation as a High Court judge in 1965, the heavier and nobler task to “take an active part in the adaptation of the law to (societal) changes”.<sup>47</sup>

## F. The future

[46] What then of the future of *Semenyih Jaya*? Will its resounding masterly analysis from on-high advance the development of constitutional and administrative jurisprudence by the courts, and add to the dynamics of constitutional interpretation and administrative law that has been so assiduously built up over the years by our judiciary? Significantly, *Semenyih Jaya* strikes in favour of judicial independence at a time when faltering public perception needs to be bolstered in this regard. It cannot be marginalised nor shunted aside. In short it is critical that the lustre of *Semenyih Jaya* must come shining through. To preserve judicial independence and, ultimately, reinforce the rule of law.

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45 Michel Foucault, “Orders of Discourse” (1971) 10 *Social Science Information* 7.

46 Richard Fallon Jr, “Legitimacy and the Constitution” (2004–2005) 118 *Harvard LR* 1787 at 1794–96; Michael Wells, “‘Sociological Legitimacy’ in Supreme Court Opinions” (2007) 64 *Washington & Lee LR* 1011 at 1020–27.

47 Visu Sinnadurai (ed), *Judgments of His Royal Highness Sultan Azlan Shah with Commentary* (Professional Law Books Publishers, 1986).

# Of Public Interest, Freedom of Speech and the Law of Defamation

by

Darryl SC Goon\*

[1] It is trite, well worn and well settled in many eloquent iterations that freedom of speech under our Federal Constitution is not absolute.<sup>1</sup> Among several statutory and other common law curtailments of freedom of speech is the tort of defamation, which demands that freedom of speech must at some point give way to protection against reputational damage.

[2] The common law's reverence for reputation is epitomised by the famous verses from Shakespeare's *Othello*.<sup>2</sup> However those poignant verses have been so often quoted that they have become equally well worn in the context of the law of defamation. In fact, they have been judicially described as being a "customary or some say obligatory reference"<sup>3</sup> in association with the law of defamation. Deference and prudence suggest that they not be repeated here.

[3] The life of the common law in protecting reputation was committed and vigorous up to the early part of the last century. Those were times when social circumstances were very different from now. Social media in the current forms that exist were not within contemplation then. So dedicated to the protection of reputation was the law then that long and complicated trials were conducted and the only hint of displeasure was the award of very nominal damages.<sup>4</sup>

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1 See *Syarikat Bekalan Air Selangor Sdn Bhd v Tony Pua Kiam Wee* [2015] 6 AMR 66 at 78, [33]; [2015] 6 MLJ 187 at 202, [33]; *Datuk Harris Mohd Salleh v Datuk Yong Teck Lee & Anor* [2017] 7 AMR 317 at 337, [36]; [2017] MLJU 1525 at [36].

2 Shakespeare's *Othello*, Act III, Scene III, Iago to Othello.

3 See observation of Harmindar Singh JC (as he then was) in *Dato' Seri Anwar bin Ibrahim v The New Straits Times Press (M) Sdn Bhd & Anor* [2010] 3 AMR 514 at 520, [2]; [2010] 2 MLJ 492 at 498, [2].

4 So dramatically portrayed by the award of one half penny "the smallest coin of the realm" in Leon Uris' book, *QB VII*.

[4] By contrast, in England today, the law of defamation<sup>5</sup> has evolved so far that claims in defamation stand liable to be struck off as being an abuse of process if the claim, though legally viable, is considered trivial or pointless; where the damage suffered if proved to the hilt is negligible, such as would be disproportionate to the cost, time and effort of a full trial. Progressively, it would seem, society grew somewhat anxious over the litigation process where the effort and public expense outweighed the practical value of the outcome – the issue at hand being the protection of reputation often in circumstances which tended to water down the freedom of speech and expression. It would appear that the greater welfare of the people, the public weal or interest, was the true engine for the changes.

[5] While the Federal Constitution expressly provides under Article 10(1)(a) that “every citizen has the right to freedom of speech and expression”, it also expresses in an inescapable manner, preceding the conferment of that right, that it is subject to three subsequent clauses in Article 10.<sup>6</sup> Relevant to the subject matter of this article is clause (2)(a). Here, the Constitution stipulates that Parliament may by law impose some restrictions as to provide against, inter alia, contempt of court and defamation. Towards this end there is then the Defamation Act 1957 (Act 286). Yet, interestingly enough, the restrictions (and the variations of them) are found, in the main, driven by the common law through the decisions of our courts rather than by Parliament. The combination of Article 10(1)(a) and 10(2)(a), the Defamation Act 1957 (Act 286) and our courts’ declarations of the law of defamation sometimes seems suited.

[6] No right or freedom can possibly be absolute when reposed in an individual when that individual exists in a society. Equal freedoms and rights for all come bound inevitably with corresponding duties and responsibilities. If, at a practical level, it makes them inherently inconsistent then it needs simply to be accepted that freedom of speech and the law of defamation are inconsistent concepts. The ultimate practical consideration then is: where should the boundary be where they collide? This constitutional tussle between freedom

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5 In fact, the *Jameel v Dow Jones* principle extends to other types of cases where the freedom of expression is impacted, e.g. malicious falsehood and breach of confidence. Cf *Tesla Motor Ltd v BBC* [2013] EWCA Civ 152; and *Abbey v Gilligan* [2012] EWHC 3217, QB.

6 Clauses (2), (3) and (4).

of speech and the laws of defamation exists in one form or another in most, if not all, common law jurisdictions – indeed, even among non-common law countries in Europe in the form of Article 10 of the European Convention on Human Rights.<sup>7</sup>

[7] However, as regards the above, lately a new phenomenon has emerged under the somewhat prosaic rubric of “public interest” – the interest of the public at large seems to be the focus for greater latitude to be given to freedom of speech in the context of the law of defamation.

[8] In recent legal memory, perhaps the starting point of the re-emergence of freedom of speech in legally dramatic terms in the context of the public interest is the decision of the House of Lords in *Derbyshire County Council v Times Newspapers Ltd & Ors*<sup>8</sup> (“*Derbyshire*”).

[9] As Balcombe LJ stated in the Court of Appeal, “The facts in the case are fortunately refreshingly simple.”<sup>9</sup> It concerned two newspaper articles. The articles questioned the propriety of investments made by a local authority for its superannuation fund. The local authority was the Derbyshire County Council which took issue with the articles. It considered the articles defamatory and initiated legal action against the publishers, Times Newspapers Ltd, its editor and two journalists. The Council maintained that the articles were written and published, “... of and concerning the council and of and concerning the council in the way of its discharge of its responsibility for the investment and control of the superannuation fund.” By reason of these publications the Council maintained that it “has been injured in its credit and reputation and has been brought into public scandal, odium and contempt, and has suffered loss and damage.” The action was thus grounded in the tort of defamation.

[10] The defendants in *Derbyshire* applied to strike out the action. They maintained that it disclosed no cause of action because the Council cannot maintain such an action. The application was dismissed by Morland J in the High Court.<sup>10</sup> It was at the Court of Appeal that the principle that a local council, “... cannot maintain an action for

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7 See *infra*.

8 [1993] AC 534.

9 *Derbyshire County Council v Times Newspapers Ltd & Ors* [1992] 3 All ER 65 at 69, between paras C and D.

10 *Derbyshire County Council v Times Newspapers Ltd & Ors* [1991] 4 All ER 795.

libel for any words which reflect upon it as the county council for Derbyshire in relation to its governmental and administrative functions in Derbyshire, including its statutory responsibility for the investment and control of the superannuation fund” was declared. However, the Court of Appeal arrived at this conclusion based on Article 10 of the European Convention on Human Rights<sup>11</sup> which it maintained it was permitted to do by reason of what it considered to be an uncertainty in the law due to the apparently conflicting decisions in *Manchester Corp v Williams*<sup>12</sup> and *Bognor Regis Urban District Council v Campion*.<sup>13</sup>

[11] Article 10 of the European Convention on Human Rights is interesting. Similar to our Federal Constitution, it manifests again the theme of the struggle between the freedom of speech and the need to protect against reputational damage. How the twain are portrayed in Article 10 is set out below:

#### ARTICLE 10

##### **Freedom of Expression**

1. *Everyone has the right to freedom of expression. This right shall include freedom to hold opinions and to receive and impart information and ideas without interference by public authority and regardless of frontiers. This Article shall not prevent States from requiring the licensing of broadcasting, television or cinema enterprises.*
2. *The exercise of these freedoms, since it carries with it duties and responsibilities, may be subject to such formalities, conditions, restrictions or penalties as are prescribed by law and are necessary in a democratic society, in the interests of national security, territorial integrity or public safety, for the prevention of disorder or crime, for the protection of health or morals, for the protection of the reputation or rights of others, for preventing the disclosure of information received in confidence, or for maintaining the authority and impartiality of the judiciary.*

(Emphasis added.)

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11 Although the United Kingdom had adhered to this convention, it had not then enacted it into domestic law as was pointed out by Lord Keith of Kinkel at the House of Lords; see *Derbyshire County Council v Times Newspapers Ltd & Ors* [1993] AC 534 at 550E–F.

12 [1891] 1 QB 94.

13 [1972] 2 QB 169.

[12] In addition to the fact that the freedom granted here is not absolute, two other points of interest may be noted. First, the recognition that the freedom granted “carries with it duties and responsibilities” and, second, that such restrictions to it may be prescribed “for the protection of reputation” as are “necessary in a democratic society”. Thus, even in a democratic society, the protection of reputation may be a necessity for which the freedom of speech and expression has to make way.

[13] Lord Keith of Kinkel, who delivered the opinion of the House of Lords, declared that there was no need to have recourse to Article 10. In his opinion, under the common law of England, a local authority does not have the right to maintain an action in damages for defamation “... without finding any need to rely upon the European convention.”<sup>14</sup> The fundamental rationale for Lord Keith’s conclusion is to be found in the following two passages in his opinion:

There are, however, features of a local authority which may be regarded as distinguishing it from other types of corporation, whether trading or non-trading. The most important of these features is that it is a governmental body. Further, it is a democratically elected body, the electoral process nowadays being conducted almost exclusively on party political lines. It is of the highest public importance that a democratically elected governmental body, or indeed any governmental body, should be open to uninhibited public criticism. The threat of a civil action for defamation must inevitably have an inhibiting effect on freedom of speech.<sup>15</sup>

... I regard it as right for this House to lay down that not only is there no public interest favouring the right of organs of government, whether central or local, to sue for libel, but that it is contrary to the public interest that they should have it. It is contrary to the public interest because to admit such actions would place an undesirable fetter on freedom of speech.<sup>16</sup>

[14] Thus ultimately it was because of, and in, the public interest that the rule in *Derbyshire* was declared. Public interest that is equated with the right to uninhibited public criticism of democratically elected

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14 *Derbyshire County Council v Times Newspapers Ltd & Ors* [1993] AC 534 at 550E and 551F.

15 *Ibid*, at 547F.

16 *Ibid*, at 549C.

governmental bodies. In this fashion, public interest triumphed over the individual's right (albeit in the form of a local authority) to protect against reputational damage.

[15] However, it may be significant to observe that surely the local authority is an entity in itself. The local authority, although a governmental body as Lord Keith puts it, is not itself a democratically elected entity. It is the control and staffing of that entity (the local authority) that are in the hands of democratically elected officials representing various political parties. Viewed from this perspective, would not the control and staffing of incorporated companies and statutory bodies by democratically elected officials who form the government of the day also satisfy the rationale in *Derbyshire*? If this be correct, the implication of the rule in *Derbyshire* may well be more far-ranging than it appears.

[16] Does the rule in *Derbyshire* apply in Malaysia? In *Kerajaan Negeri Terengganu & Ors v Dr Syed Azman Syed Ahmad Nawawi & Ors*<sup>17</sup> (“*Kerajaan Negeri Terengganu*”), Yeoh Wee Siam J, as her Ladyship then was, came to the conclusion that it does. In so doing, it was held that the State Government of Terengganu could not maintain an action in defamation. In coming to this conclusion, the learned judge found that there was an absence of statutory provision which might address the issue as to whether a state government may maintain an action in defamation. On that basis, resort was then had to the common law and what was declared in *Derbyshire* that under the common law a local authority does not have the right to maintain an action in defamation. The learned judge then held that *a fortiori* a state government would also not have such a right. The principle in *Derbyshire* was thus adopted. The learned judge also provided her rationale for adopting *Derbyshire* in the following terms:

[30] Accordingly, I adopt the principles laid down in *Derbyshire* (supra), and hold that the 1st Plaintiff, which is the government of the State of Terengganu, is a public authority. As such it does not have a personal reputation to protect. Neither does it have a governing reputation, as in the case of a corporation or statutory body/authority, to protect. The State Government is duly elected by the members of the public through the democratic process and it should be transparent and accountable to the electorate. There should be freedom of speech

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17 [2012] AMEJ 0184; [2013] 1 CLJ 107.

and expression by members of the public in order to act as a check and balance on the executive and the government. It is therefore not in the interest of the public that the State Government be allowed to institute or maintain any action for libel or slander against any person. Otherwise, it would stifle constructive queries or comments which can contribute to and ensure good governance of the subjects by the State Government. There can be no financial loss suffered by the State Government even if defamatory statements are made against it by any persons.<sup>18</sup>

Thus, public interest again emerges the victor in this struggle.

[17] There is then the case of *Lembaga Kemajuan Tanah Persekutuan & Anor v Datuk Seri Dr Wan Azizah Wan Ismail & Ors*<sup>19</sup> (“*Lembaga Kemajuan Tanah Persekutuan*”). It was held in this case that the rule in *Derbyshire* does not apply to the plaintiff in *Lembaga Kemajuan Tanah Persekutuan*. The learned judge, Kamaludin Md Said J, held *inter alia* that he was bound by the prior decision of the Court of Appeal in *Lembaga Kemajuan Tanah Persekutuan & Anor v Dr Tan Kee Kwong*<sup>20</sup> and that the Federal Land Development Authority (“FELDA”) is not a democratically elected body.

[18] As at the date of this article, one significant reported decision on the rule in *Derbyshire* and its applicability is that of the Court of Appeal in *Government of the State of Sarawak & Anor v Chong Chieng Jen*<sup>21</sup> (“*Government of the State of Sarawak*”).<sup>22</sup> In this case, the defendant is a Member of Parliament and a State Assemblyman. The defendant caused to be published in the publication *Sin Chew Daily News*, and in a leaflet by the Democratic Action Party, a statement about

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18 Ibid, at p 17 (AMEJ); 120, [30] (CLJ).

19 [2014] AMEJ 1497; [2015] 2 CLJ 692.

20 Unfortunately, the grounds of the Court of Appeal’s decision were not reported. The learned judge in the High Court held that the plaintiff was neither a public authority nor local authority and that the rule in *Derbyshire* did not apply; however, it was also held that the plaintiffs had failed to prove that defamatory words were uttered or caused to be published by the defendant. The decision was upheld by the Court of Appeal and the Federal Court (see “Apex Court bins Felda’s defamation suit against PKR lawmaker”, *Malay Mail Online*, September 4, 2014). The Court of Appeal held that *Derbyshire* did not apply as the plaintiffs being a statutory body and a registered company were not local authorities.

21 [2016] 5 AMR 85; [2016] 3 MLJ 41.

22 There is the decision of the Court of Appeal in *Tony Pua Kiam Wee v Syarikat Bekalan Air Selangor Sdn Bhd* [2013] 1 LNS 1433 which concerned what was technically a private company registered under the Companies Act 1965 (Act 125).

mismanagement of the State's financial affairs and the disappearance of a sum of RM11,000,000,000. The State Government of Sarawak and the State Financial Authority Sarawak took issue and sued. An application under Order 14A of the Rules of Court 2012 was filed and one of the questions posed was whether the first plaintiff, being the State Government of Sarawak and/or the second plaintiff, being a government department and an organ of the government, have the right to sue and to maintain an action for damages in defamation. The High Court ruled in favour of the defendant and struck out the action. The Court of Appeal however, allowed the plaintiffs' appeal. In so doing, the Court of Appeal held that the rule in *Derbyshire* does not apply. The view of the Court of Appeal hinges on the application of section 3 of the Government Proceedings Act 1956 (Act 359) which, rather awkwardly, states as follows:

3. Subject to this Act and of any written law where the Government has a claim against any person which would, if such claim had arisen between subject and subject, afford ground for civil proceedings, the claim may be enforced by proceedings taken by or on behalf of the Government for that purposes in accordance with this Act.

[19] The majority of the Court of Appeal in *Government of the State of Sarawak* stated that "Section 3 gives the government the same right as a private individual to enforce a claim against another private individual by way of civil action. It is a statutory right and not a common law right".<sup>23</sup> Put that way, it would mean that section 3 does not prescribe the *type* of causes of action available to the government or what claims the government may make but merely makes available to it the procedural facility that is available between subjects, *inter se*, to enforce a claim. However, the majority judgment delivered by Abdul Rahman Sebli JCA went one step further to state that "... the statutory right given to the government by s 3 of the Government Proceedings Act to sue for defamation cannot be taken away by the application of the common law principle propounded by the House of Lords in the *Derbyshire County Council* case or, for that matter, any other common law positions in other common law jurisdiction".<sup>24</sup> This appears pivotal in the decision of the court.

<sup>23</sup> *Government of the State of Sarawak & Anor v Chong Chieng Jen* [2016] 5 AMR 85 at 105, [66]; [2016] 3 MLJ 41 at 55, [23].

<sup>24</sup> *Ibid*, at 112, [120] (AMR); 64, [77] (MLJ).

[20] The dissenting view in *Government of the State of Sarawak* is compelling. It is that on a proper construction "... s 3 of the GPA is a general piece of legislation to cloth(e) the government the *legal status to sue or be sued, nothing more or nothing less*".<sup>25</sup> According to the dissent, delivered by David Wong JCA, section 3 does not provide the answer, "... whether the government possess (*sic*) a 'cause of action' in an action for defamation" and to that question, the answer is to be found in the common law. Thus, the dissenting perspective of section 3 is that it was designed to enable the government to have proceedings brought on its behalf to enforce a claim that it may have but does not provide for what type of claims the government may make or the causes of action available to it.

[21] The decision in *Government of the State of Sarawak* is that *Derbyshire* is not to apply – however, that is not due to any rejection of its underlying principles in favour of the public's interest but purely as a matter of statutory interpretation.

[22] Equally significant is the decision of the Court of Appeal in *Utusan Melayu (M) Bhd v Dato' Sri DiRaja Hj Adnan bin Hj Yaakob*<sup>26</sup> ("*Utusan Melayu*"), which arrived at a conclusion opposite to that in *Government of the State of Sarawak*. This was an action commenced against the Utusan Melayu (M) Bhd founded on the tort of defamation. An application was made by the defendant to strike out the plaintiff's action based upon the principle in *Derbyshire*. The High Court dismissed the application on the basis that the action was brought by the plaintiff in his personal capacity and not in his official capacity as the Menteri Besar of the State of Pahang. The defendant's appeal was allowed by the Court of Appeal. The Court of Appeal was of the view that the allegations in the impugned article were directed at the plaintiff as Menteri Besar. It was also observed that it was "*manifest*" that the plaintiff's pleadings asserted that the impugned article had attacked him in his capacity as Menteri Besar. On this basis the Court of Appeal, whose judgment was delivered by Idrus Harun JCA, stated that:

[20] It is of some significance to emphasise that, the legitimate issue herein is not so much on the applicability or otherwise of the common law principle as laid down by the House of Lords in

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25 Ibid, at 93, [17] (AMR); 70, [109] (MLJ).

26 [2016] 4 AMR 548; [2016] 5 MLJ 56.

*Derbyshire County Council* but rather the right to discuss or criticise the government and public officials by the citizens in the exercise of their right under Article 10 clause (1)(a) of the Federal Constitution. It matters not, whether the common law principle is applicable for, in our judgment, such right is in fact and in law an integral part of the right to freedom of speech and expression. The basic right of every citizen which is deeply and firmly ingrained in Article 10 clause (1)(a) of the Federal Constitution that can only be restricted by federal law in accordance with clause (2)(a) thereof. This fundamental right must therefore be given due recognition and protected as one which is guaranteed by the Federal Constitution. Thus, even assuming for a moment that the *Derbyshire* principle is not part of our law on defamation, or the appellant's case does not principally rely on the common law principle, we would say that the principle clearly emanates from and is already well-entrenched in Article 10 clause (1)(a) of the Federal Constitution which guarantees the right to freedom of speech and expression, which right in our judgment encompasses the rights of the citizens to discuss the government and those holding public office of the respondent's position conducting public affairs and administration of the state. On that score, and as public interest dictates, a democratically elected government and its officials should be open to public criticism and that it is advantageous that every responsible citizen should not be in any way fettered in his statements where it concerns the affairs and administration of the government. Any action to the contrary would in our view, be against public interest and directly affect the fundamental right guaranteed by Article 10 clause (1)(a) of the Federal Constitution unless it is clearly allowed by federal law.<sup>27</sup>

[23] The Court of Appeal in *Utusan Melayu* adopted the statements of David Wong JCA in relation to the constitutional rights of citizens in his dissent in *Government of the State of Sarawak*. However, what did not appear to have been addressed in *Utusan Melayu* was the ambit and applicability of section 3 of the Government Proceedings Act 1956 (Act 359) which was significant in *Government of the State of Sarawak*.

[24] In light of the conflicting Court of Appeal decisions, it is hoped that the Federal Court will soon have the opportunity to put the conundrum to rest.

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27 Ibid, 560 (AMR): 69 (MLJ).

[25] In the United Kingdom (“UK”), the public interest theme continued to develop. It next featured in the defence of qualified privilege. The traditional limits of qualified privilege under the common law were drawn, usually but not necessarily,<sup>28</sup> in respect of publications that were private. Qualified privilege did not, for example, extend to publications of defamatory material<sup>29</sup> to the public at large save in extremely rare circumstances.<sup>30</sup> Often, the duty and interest elements that were required would fail to apply to publications to the public at large. However, this limitation was relaxed not long after *Derbyshire*.

[26] *Reynolds v Times Newspapers Ltd & Ors*<sup>31</sup> (“*Reynolds*”), was another decision of the House of Lords. Decided less than 10 years after *Derbyshire*, it registered another triumph in favour of public interest. In *Reynolds*, an article was written about the political crisis in Ireland in 1994 which resulted in the plaintiff’s resignation as *Taoiseach*, the Prime Minister of the Republic of Ireland. The plaintiff claimed that the article contained words which bore the meaning that he had deliberately and dishonestly misled the *Dail*, the lower house of Parliament in the Republic of Ireland, by suppressing crucial information about the Irish Attorney General, whom he had sought to have appointed to the Presidency of the High Court, and also that he had misled his cabinet by withholding information and lying. The plaintiff succeeded but was awarded 1 penny as damages. The plaintiff appealed and the defendants cross appealed. The plaintiff’s appeal was allowed by the Court of Appeal but a retrial was ordered owing to factual misdirection to the jury in the judge’s summing up which amounted to the denial of a fair trial. The defendants’ appeal was dismissed by the Court of Appeal which held that the publication was not covered by qualified privilege.

[27] The defendants appealed to the House of Lords asserting that there should be recognised a generic qualified privilege encompassing the publication by a newspaper of political matters affecting the people

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28 See *Cox v Feeney* [1863] 4 F & F 13 at 19; and *Purcell v Sowler* [1877] 2 CPD 215, both cited by Lord Nicholls of Birkenhead in *Reynolds v Times Newspapers Ltd & Ors* [2001] 2 AC 127 at 195.

29 As opposed to *comments* on facts that were regarded as fair and to be in the public interest; now “honest comment” (see *infra*).

30 See *Gatley on Libel and Slander*, 12th edn (London: Sweet & Maxwell), p 633, Chapter 15, para 15.1.

31 [2001] 2 AC 127.

of the UK. The majority of the House of Lords, led in the main by Lord Nicholls of Birkenhead, declined the defendants' assertion of a generic qualified privilege. However the Law Lords did recognise that the existing basis upon which qualified privilege rests, i.e. the duality of duty and interest, was wide enough to apply to publications to the public.<sup>32</sup>

[28] As Lord Nicholls put it in discussing the factors the Court of Appeal had regarded as relevant in what it termed as the "circumstantial test", "... factors are to be taken into account in determining whether the duty-interest test is satisfied or, as I would prefer to say in a simpler and more direct way, whether the public was entitled to know the particular information".<sup>33</sup> Lord Nicholls then set out ten matters that ought to be taken into account in assessing the applicability of qualified privilege.<sup>34</sup> These ten matters were not meant to be exhaustive. In the process, Lord Nicholls emphasised that:

Above all, the court should have particular regard to the importance of freedom of expression. The press discharges vital functions as a bloodhound as well as a watchdog. The court should be slow to conclude that a publication was not in the public interest and, therefore, the public had no right to know, especially when the information is in the field of political discussion. Any lingering doubts should be resolved in favour of publication.<sup>35</sup>

[29] This predilection in favour of and the concern for public interest had been expressed in eloquent terms in the Court of Appeal. Lord Bingham of Cornhill CJ expressed the following:

We do not for an instant doubt that the common convenience and welfare of a modern plural democracy such as ours are best served by an ample flow of information to the public concerning, and by vigorous public discussion of, matters of public interest to the community. By that we mean matters relating to the public life of the community and those who take part in it, including within the expression "public life" activities such as the conduct of government and political life, elections (subject to section 10 of the Act of 1952, so

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32 *Reynolds v Times Newspapers Ltd & Ors* [2001] 2 AC 127 at 194–195 and 204–205, per Lord Nicholls; at 213, per Lord Steyn; at 225 and 227, per Lord Cooke; at 234–235, per Lord Hope; and at 239, per Lord Hobhouse.

33 *Ibid.*, at 197F–G.

34 *Ibid.*, at 205A–C.

35 *Ibid.*, at 205E–F.

long as it remains in force) and public administration, but we use the expression more widely than that, to embrace matters such as (for instance) the governance of public bodies, institutions and companies which give rise to a public interest in disclosure, but excluding matters which are personal and private, such that there is no public interest in their disclosure. Recognition that the common convenience and welfare of society are best served in this way is a modern democratic imperative which the law must accept. In differing ways and to somewhat differing extents the law has recognised this imperative, in the United States, Australia, New Zealand and elsewhere, as also in the jurisprudence of the European Court of Human Rights.

...

As it is the task of the news media to inform the public and engage in public discussion of matters in the public interest, so is that to be recognised as its duty. The cases cited show acceptance of such a duty, even where publication is by a newspaper to the public at large. In modern conditions what we have called the duty test should, in our view, be rather more readily held to be satisfied.<sup>36</sup>

[30] Thus yet again, public interest prevailed to expand the ambit of the “duty-interest” based qualified privilege in the law of defamation to accommodate publications to the public at large but subject to judicial assessment of the circumstances to ensure what has become known as “responsible journalism”. This process that exists in the common law which affords judicial assessment of the circumstances “... enables interference with freedom of speech to be confined to what is necessary in the circumstances of the case”.<sup>37</sup> This is the “elasticity” of the common law that Lord Nicholls spoke of, “[t]his elasticity enables the court to give appropriate weight, in today’s conditions, to the importance of freedom of expression by the media on all matters of public concern”.<sup>38</sup>

[31] Significantly, the Federal Court has also held that the *Reynolds* defence of qualified privilege is available in Malaysia. In *Syarikat Bekalan Air Selangor Sdn Bhd v Tony Pua Kiam Wee*<sup>39</sup> (“*Syarikat Bekalan Air Selangor Sdn Bhd*”), among the questions of law posed to the

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36 *Reynolds v Times Newspapers Ltd & Ors* [1998] 3 All ER 961 at 1004A–E.

37 *Reynolds v Times Newspapers Ltd & Ors* [2001] 2 AC 127 at 204.

38 *Ibid.*

39 [2015] 6 AMR 66; [2015] 6 MLJ 187.

Federal Court was: “Whether the defence of qualified privilege as set out in the English House of Lords case of *Reynolds v Times Newspapers Ltd* (*Reynolds* privilege) is available to an individual who is not a journalist?” This question was answered in the affirmative. Although the question posed was not specifically whether the *Reynolds* defence applies in Malaysia, it would be pedantic to suggest that in answering the question posed in the affirmative, the Federal Court did not intend that the privilege was applicable generally as well.

[32] *Syarikat Bekalan Air Selangor Sdn Bhd* demonstrates in crystalline terms the core values of the common law system. In recognising that the decision in *Reynolds* “... marked a decisive departure from the traditional pro-reputation orientation of defamation law in England ...” and choosing to adopt it underscores again the common law’s preferment of public interest. Although *Reynolds* itself concerns the press and journalists, its willingness to not so limit the defence further demonstrates how the common law in the hands of our courts can remain current and relevant. The Federal Court, whose judgment was delivered by Azahar Mohamed FCJ, did so by stating thus:

[33] In our view, the public interest defence should by no means [be] synonymous with journalists or media publications. On the ground of public interest, there is a sufficient basis it should be in the same way extended to anyone who publishes or discloses material of public interest in any medium to assist the public better comprehend and make an informed decision on matters of public interest that affects their lives. To safeguard the extension of this privilege is not abused, as a necessary balance, it is the duty of the court to robustly ensure that anyone who is accorded with the privilege meet the test of responsible journalism, about which more will be said later in this judgment. This, in our view, underpins the significance of protecting the right of freedom of expression on public interest matter and at the same time providing adequate protection for reputation.<sup>40</sup>

[33] At the same time the Federal Court was cognisant of the fact that the “... *Reynolds* privilege defence places a considerable role in

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40 Ibid, at 78, [33] (AMR): 202, [33] (MLJ). The extension of the *Reynolds* defence is also consistent with the position in the UK, see *Jameel (Mohammed) & Anor v Wall Street Journal Europe Sprl* [2007] 1 AC 359, HL, per Lord Hoffman; *Seaga v Harper* [2008] 1 All ER 965, PC; and *Charman v Orion Publishing Group Ltd & Ors* [2008] 1 All ER 750, CA, cases cited in *Syarikat Bekalan Air Selangor Sdn Bhd*.

the hands of judges to deliberate fairly and come to a just decision with utmost care whether the impugned publication amount (*sic*) to an occasion of privilege".<sup>41</sup>

[34] In its recent decision in *Datuk Harris Mohd Salleh v Datuk Yong Teck Lee & Anor*<sup>42</sup> ("*Datuk Harris Mohd Salleh*"), the Federal Court submitted the *Reynolds* defence to close scrutiny. The case concerned a claim in defamation primarily between one individual against the other, both of whom were former Chief Ministers of the State of Sabah. It applied the ten-point test formulated by Lord Nicholls in a careful and detailed analysis of the facts of the case to determine if the requirement of responsible journalism was discharged. In the ultimate, liability was found and the appeal allowed. In the course of its judgment, the Federal Court cited several significant passages of Lord Nicholls' opinion in the House of Lords in *Reynolds* with emphasis on the importance of freedom of expression and, at the same time, the importance of reputation:

... Without freedom of expression by the media, freedom of expression would be a hollow concept. The interest of a democratic society in ensuring a free press weighs heavily in the balance in deciding whether any curtailment of this freedom bears a reasonable relationship to the purpose of the curtailment.

...

Reputation is an integral and important part of the dignity of the individual. It also forms the basis of many decisions in a democratic society which are fundamental to its well-being: whom to employ or work for, whom to promote, whom to do business with or to vote for. Once besmirched by an unfounded allegation in a national newspaper, a reputation can be damaged forever, especially if there is no opportunity to vindicate one's reputation. When this happens, society as well as the individual is the loser.<sup>43</sup>

[35] It is noteworthy that the Federal Court in *Datuk Harris Mohd Salleh* also pointed out that malice would not defeat the *Reynolds*

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41 *Syarikat Bekalan Air Selangor Sdn Bhd v Tony Pua Kiam Wee* [2015] 6 AMR 66 at 78, [33]; [2015] 6 MLJ 187 at 202, [33].

42 [2017] 7 AMR 317; [2017] MLJU 1525.

43 *Ibid*, at 340, [44] (AMR); p 13 (MLJ).

defence. This it did by reference to Lord Hoffmann's speech in *Jameel (Mohammed) v Wall Street Journal Europe Sprl ("Jameel")*<sup>44</sup> where his Lordship stated that:

46 Although Lord Nicholls uses the word "privilege", it is clearly not being used in the old sense. It is the material which is privileged, not the occasion on which it is published. There is no question of the privilege being defeated by proof of malice because the propriety of the conduct of the defendant is built into the conditions under which the material is privileged. The burden is upon the defendant to prove that those conditions are satisfied. I therefore agree with the opinion of the Court of Appeal in *Loutchansky v Times Newspapers Ltd (Nos 2-5)* [2002] QB 783, 806 that "*Reynolds* privilege" is "a different jurisprudential creature from the traditional form of privilege from which it sprang". It might more appropriately be called the *Reynolds* public interest defence rather than privilege.<sup>45</sup>

[36] The next step was for the *Reynolds* defence to develop into an identifiable defence in its own right – not a defence of qualified privilege but a defence of "publication in the public interest". Well-wishers and proponents already existed. They were in the form of none other than Lord Hoffman and Baroness Hale. In *Jameel*, Lord Hoffmann observed that:

50 In answering the question of public interest, I do not think it helpful to apply the classic test for the existence of a privileged occasion and ask whether there was a duty to communicate the information and an interest in receiving it. The *Reynolds* defence was developed from the traditional form of privilege by a generalisation that in matters of public interest, there can be said to be a professional duty on the part of journalists to impart the information and an interest in the public in receiving it. The House having made this generalisation, it should in my opinion be regarded as a proposition of law and not decided each time as a question of fact. If the publication is in the public interest the duty and interest are taken to exist.<sup>46</sup>

[37] Commenting on the *Reynolds* defence in the same case, Baroness Hale expressed that:

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44 [2007] 1 AC 359.

45 Ibid, at 381, [46].

46 Ibid, at 382.

146. It should by now be entirely clear that the *Reynolds* defence is a “different jurisprudential creature” from the law of privilege, although it is a natural development of that law. It springs from the general obligation of the press, media and other publishers to communicate important information upon matters of general public interest and the general right of the public to receive such information. It is not helpful to analyse the particular case in terms of a specific duty and a specific right to know. That can, as experience since *Reynolds* has shown, very easily lead to a narrow and rigid approach which defeats its object. In truth, it is a defence of publication in the public interest.<sup>47</sup>

[38] Indeed, it may also be said that ascribing to what the press does as being a “duty” seems somewhat artificial. The courts do not control the press. If there is information that is in the public interest, there is no legal obligation for the press to inform the public. If there is any “duty” to do so, it is not enforceable – thus if at all, the duty is merely an unenforceable voluntary moral obligation. Accordingly, to persist in regarding the *Reynolds* defence as being part of the “duty-interest”-based qualified privilege seems rather incongruous.

[39] Only about a year later, *Reynolds* was accredited for dealing another blow to the protection of individual reputation in the name of public interest. This is now known as the defence of reportage.<sup>48</sup> It is a word introduced into the vocabulary of defamation law by Mr Andrew Caldecott QC, a leading English barrister who specialises in defamation law.<sup>49</sup> The term “reportage” was first formally adopted by the English Court of Appeal in *Al-Fagih v HH Saudi Research & Marketing (UK) Ltd*<sup>50</sup> (“*Al-Fagih*”). The term was thought by Simon Brown LJ in that case to be “a convenient word to describe the neutral reporting of attributed allegations rather than their adoption by the newspaper”.<sup>51</sup> This defence was said to be within, or emanating out of, *Reynolds* by reference to the ninth of Lord Nicholls’ ten-point test for responsible journalism – i.e. “9. The tone of the article. A

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47 *Ibid*, at 408.

48 Apparently the term, having gained acceptance in the “*libel lexicon*”, no longer requires to be italicised; see *Roberts v Gable* [2008] 2 WLR 129 at 156, [68] per Ward LJ.

49 *Ibid*, at 144, per Ward LJ.

50 [2001] EWCA Civ 1634; [2002] EMLR 215.

51 *Al-Fagih v HH Saudi Research & Marketing (UK) Ltd* [2001] EWCA Civ 1634 at p 2, [6].

newspaper can raise queries or call for an investigation. It need not adopt allegations as statements of fact".<sup>52</sup>

[40] In *Al-Fagih*, the publications reported a dispute that arose between Dr Mohammed Al-Mas'aari and Al-Fagih. They were both prominent political figures in a dissident Saudi Arabian political organisation opposed to the existing Saudi Arabian government. The complaint was about an allegation that one made of the other, which was reported by the defendant. The publications complained of had stated that Dr Mohammed Al-Mas'aari had informed the defendant's journalist that Al-Fagih had spread rumours about him and had said that his mother had procured women for him for salacious purposes.

[41] What Dr Mohammed Al-Mas'aari told the defendant's journalist was found to be a canard and untrue. Before the learned trial judge, it was urged that the "defendant had done no more than provide an accurate day-to-day account of the unfolding dispute. It had not taken sides. It had not adopted the allegations and counter-allegations as true but had merely reported what each had said. Its staff had no reason to believe that the words complained of were not true. The defendant had observed the standards of responsible journalism".<sup>53</sup>

[42] However, the learned judge rejected the defence of qualified privilege saying, "I reject that defence as I did not accept that the defendant had observed the standards of responsible journalism. [The defendant's journalist] had made no attempt to verify the truth of [Dr Mohammed Al-Mas'aari's] allegation as he could and should have done. When the series of articles was viewed as a whole, I considered that the defendant had taken sides and had implied that the allegation was true. Although I recognised that there was some public interest in the reporting of the dispute, I held that the potential harm to the claimant from the publication of the unverified allegation outweighed the public interest in publication".<sup>54</sup>

[43] In mitigation it was urged that the defendant's journalist was not recklessly indifferent to the truth of the allegation. To this the

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52 *Reynolds v Times Newspapers Ltd & Ors* [2001] 2 AC 127 at 205.

53 *Al-Fagih v HH Saudi Research & Marketing (UK) Ltd* [2001] EWCA Civ 1634 at p 2, [4].

54 *Ibid.*

learned judge's position was, "I do not accept that [the journalist] was not reckless. I think he was".<sup>55</sup> Thus, in the learned judge's view, the failure to verify the truth of the allegation floored the defendant's defence of qualified privilege.

[44] The Court of Appeal in *Al-Fagih* accepted that "... the fact is that at the time of the publication complained of the newspaper was reporting the allegations entirely neutrally and, there being no complaint as to the later articles, it would be wrong to deny the claimed qualified privilege by reference to them".<sup>56</sup> On the issue of the failure to verify, Simon Brown LJ, with whom Latham LJ agreed, held as follows:

[52] I am saying, however, that there will be circumstances where, as here, that may not be "most unsatisfactory" – where, in short, both sides to a political dispute are being fully, fairly and disinterestedly reported in their respective allegations and responses. In this situation it seems to me that the public is entitled to be informed of such a dispute without having to wait for the publisher, following an attempt at verification, to commit himself to one side or the other.<sup>57</sup>

The appeal was allowed.

[45] Reportage was further blessed by another Court of Appeal in *Roberts & Anor v Gable & Ors*<sup>58</sup> ("*Roberts*"). Although the principle had been considered in the earlier cases of *Jameel (Mohammed) v Wall Street Journal Europe Sprl*<sup>59</sup> in the Court of Appeal and in *Galloway v Telegraph Group Ltd*,<sup>60</sup> it was not applied. It was in *Roberts* that the principle was fully developed.<sup>61</sup> In *Roberts*, the Court of Appeal addressed the apparent contradiction between the repetition principle in the law of defamation and that of reportage. It was made clear that there is no contradiction between the two principles. Ward LJ explained that "... the answer to the first question is that the repetition rule and reportage are not in conflict with each other. The former is concerned

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55 *Ibid*, at p 7, [24].

56 *Ibid*, at p 13, [54].

57 *Ibid*, at p 13, [52].

58 [2008] 2 WLR 129.

59 [2005] QB 904.

60 [2006] EWCA Civ 17.

61 Ward LJ in *Roberts* saw force in the argument that the ambit of the reportage defence was not clearly defined or confined in *Al-Fagih*; see *Roberts & Anor v Gable & Ors* [2008] 2 WLR 129 at 146, [40].

with justification, the latter with privilege. A true case of reportage may give the journalist a complete defence of qualified privilege. If the journalist does not establish the defence then the repetition rule applies and the journalist has to prove the truth of the defamation words".<sup>62</sup>

[46] On the juristic basis of the reportage principle, *Roberts* makes clear that it is a defence of qualified privilege. It is a form or special example of the *Reynolds* type of qualified privilege. It is a "special kind of responsible journalism but with distinctive features of its own".<sup>63</sup> It is not a separate generic defence of its own right because of the decision in *Reynolds*.

[47] In *Reynolds*, the case for a new category of qualified privilege based on the subject matter of political information was rejected. *Reynolds* made clear that the underlying rationale for the defence of qualified privilege is public policy and the need for the "duty-interest" element. This requirement would exclude information that would only interest an officious bystander. In this regard, *Roberts* explains that for reportage to apply, the information published must first be in the public interest. It is also necessary that the publication, "... judging the thrust of it as a whole, must have the effect of reporting, not the truth of the statements, but the fact that they were made".<sup>64</sup> This distinction was expressed to be analogous to that in the law of evidence of a hearsay statement as disclosed in the case of *Subramaniam v PP*<sup>65</sup> – i.e. a statement that is offered as having, as a fact, been made rather than offered for the truth of its content.

[48] Ward LJ further explained that "If upon a proper construction of the thrust of the article the defamatory material is attributed to another and is not being put forward as true, then a responsible journalist would not need to take steps to verify its accuracy. He is absolved from that responsibility because he is simply reporting in a neutral fashion the fact that it has been said without adopting the truth".<sup>66</sup> The test to be applied is objective and protection from

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62 *Roberts & Anor v Gable & Ors* [2008] 2 WLR 129 at 152–153, [59].

63 *Ibid.*, at 153, [60].

64 *Ibid.*, at 153, [61].

65 [1956] 1 WLR 965 at 969.

66 *Ibid.*

the privilege is lost if the journalist adopts the report and makes it his own or if he fails to report the story in a fair, disinterested and neutral way. All the circumstances are to be assessed to determine if the journalist had adopted the allegation.<sup>67</sup> If there was no adoption of the allegations, the journalist is absolved from having to verify the information published – reportage as a defence of qualified privilege would thus apply. It should also follow that if the legal criteria for the principle to apply are met, by the very nature of the defence, whether the publication was with malice or not is not relevant. This should follow by parity of reasoning to that applied by Lord Hoffmann in respect of the irrelevance of malice to the *Reynolds* defence (see supra).

[49] Having regard to the decisions in *Reynolds*, *Al-Fagih*, *Roberts* and the subsequent decision in *Charman v Orion Publishing Ltd*,<sup>68</sup> the interplay of the *Reynolds* defence, reportage and the rule against repetition would be thus: one would start with reportage (where it applies, the need for verification is unnecessary), if it does not apply, then one would examine if the *Reynolds* defence applies (though the journalist would have had to try to verify the information)<sup>69</sup> and if that does not apply then the repetition rule will take effect and the only defence that would be left available for the journalist would be justification.

[50] As with *Reynolds*, reportage is rooted in the bedrock of public policy and public interest. The principle of reportage was explained, discussed and considered by the High Court in *Dato' Seri Anwar bin Ibrahim v The New Straits Times Press (M) Sdn Bhd & Anor*.<sup>70</sup> However, the principle was found not to be applicable. In the words of the learned judge:

... the article is certainly not put forward in a fair, disinterested and neutral fashion because it does not contain the version of the other side of a dispute, if at all there is a dispute. I also do not think that this is a neutral report because what SD1 is trying to do, as she herself admits, is to explore the links between APPC, Douglas Paal, the funding by

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67 See also *Charman v Orion Publishing Ltd* [2007] EWCA Civ 972.

68 [2007] EWCA Civ 972.

69 Relying on *Reynolds* as an alternative has been described as “problematic”; see the comment of Sedley LJ in *Charman v Orion Publishing Ltd* [2007] EWCA Civ 972.

70 [2010] 3 AMR 514; [2010] 2 MLJ 492.

the Malaysian government and the plaintiff. Her intention, therefore, is not mere neutral reporting but to assert something more sinister on the part of the plaintiff than what had appeared in the New Republic article. She was in a sense adding her own spice and putting “meat on the bones” (see *Associated Newspapers Ltd & Ors v Dingle* [1964] AC 371 at 411 per Lord Denning) and making what I considered to be independent inferences. I am therefore unable to accept her subsequent assertions that her article was a mere reproduction.<sup>71</sup>

[51] In other words, it was neither neutral reporting nor responsible journalism. Hopefully, it will not be long before the Federal Court receives the opportunity to consider and declare the position of reportage in our jurisprudence.

[52] The momentum of change has also seen the renaming of the defence of fair comment. In *Joseph & Ors v Spiller & Anor (Associated Newspapers Ltd & Ors intervening)*<sup>72</sup> (“*Joseph*”), the English Supreme Court recommended the defence of fair comment be renamed “honest comment”. New Zealand was in fact the forerunner in introducing the term honest comment – “(... honest opinion, as the right has been aptly rechristened in New Zealand)”.<sup>73</sup> Section 8 of the New Zealand Defamation Act 1954 states as follows:

In an action for defamation in respect of words consisting partly of allegations of fact and partly of expression of opinion, a defence of fair comment shall not fail by reason only that the truth of every allegation of fact is not proved if the expression of opinion is fair comment having regard to such of the facts alleged or referred to in the words complained of as are proved.

[53] This provision is of course practically identical to section 9 of our Defamation Act 1957 (Act 286) save that under section 9, the words “libel, or slander” are used instead of “defamation”. Pursuant to reforms recommended by the Committee on Defamation in 1977, the defence of fair comment in section 8 of the New Zealand Defamation Act 1954 was replaced under the new New Zealand Defamation Act 1992.

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71 Ibid, at 540-541, [80] (AMR); 520, [79] (MLJ).

72 [2011] 1 AC 852.

73 Per Lord Nicholls in *Reynolds v Times Newspapers Ltd & Ors* [2001] 2 AC 127 at 165C-D.

## Honest Opinion

### 9. *Honest opinion*

In proceedings for defamation, the defence known before the commencement of this Act as the defence of fair comment shall, after the commencement of this Act, be known as the defence of honest opinion.

### 10. *Opinion must be genuine*

- (1) In any proceedings for defamation in respect of matter that includes or consists of an expression of opinion, a defence of honest opinion by a defendant who is the author of the matter containing the opinion shall fail unless the defendant proves that the opinion expressed was the defendant's genuine opinion.

[54] As can be seen, in New Zealand, the burden of proof of honest opinion is now clearly imposed on the defendant who has to prove that the opinion expressed was the defendant's genuine opinion. The use of the term "honest opinion" is reported to have been at the behest of a prominent lawyer in New Zealand who wrote to the then Minister of Justice suggesting that honesty and opinion both be included in the title to avoid confusion.

[55] Apart from Lord Phillips stating that "There is only one reform that I would seek to make by this judgment" and that was that the defence of fair comment should be renamed "honest comment", the Supreme Court in *Joseph* also discussed several other areas for possible reform in the law of defamation. Suggestions were made by counsel who appeared in the case, Mr Price and Mr Caldecott (who seems omnipresent in major defamation causes). Among the suggestions was that fair comment, or now honest opinion, should be expanded to embrace facts which were not known to the defendant, or even in existence when he made the comment. It was also suggested that fair comment be extended to inferences of fact. Lord Phillips himself commented that "There may be a case for widening the scope of the defence of fair comment by removing the requirement that it must be on a matter of public interest".<sup>74</sup> Lord Phillip's suggestion is in fact

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<sup>74</sup> *Joseph & Ors v Spiller & Anor (Associated Newspapers Ltd & Ors intervening)* [2011] 1 AC 852 at 887, [113].

far-reaching both in practical and juridical terms. Presumably the emphasis would be on what is fair or whether the view given is an honest one based upon the facts disclosed – *whether a public interest element exists or not*. This would result in a major triumph for freedom of speech.

[56] To borrow from Lord Phillips of Worth Matravers,<sup>75</sup> the law of defamation, too, has been and is on the move. The pressure for reform is perhaps not so great from conscientious law reformers but more so from the circumstances that society has evolved into. The most significant is the fact that the media available to defame are now legion. The Internet, together with very powerful, convenient and very portable mobile devices all contribute to making the transmission of both words and visual ideas easy, rapid and inexpensive. Court actions cannot possibly be the answer to the myriad of defamatory allegations that may be and are conveyed through the social media via the many available options like Facebook, YouTube, Instagram, WhatsApp and WeChat. Even the current President of the United States of America uses Twitter as a very powerful source of an instantaneous means of broadcasting his thoughts. Equally significant is that these options are freely and cheaply available to a wide spectrum ranging from those below the age of majority to pensioners. The opportunity to defame and speak ill of others or to convey derogatory portrayal of others is therefore greatly magnified.

[57] The law of defamation is available to every individual, be he a prominent public figure or an ordinary man on the street. Yet, going to court for everyone who has suffered reputational damage through, for example, social media cannot be the answer. Many of these defamatory materials may be regarded as trivial or petty and yet they entitle the victim to a valid cause of action. That however has been changed in England with the advent of the Civil Procedure Rules (“the CPR”) and the coming into force of the Human Rights Act 1998. By virtue of the interpolation of these two instruments, there is now a growing jurisprudence in England for the striking out of defamation actions on the ground of abuse of process.

[58] This approach to rid the courts of the burden of having to deal with defamation causes which are simply not worth the courts’ time

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<sup>75</sup> See *Various Claimants v Catholic Child Welfare Society & Ors* [2013] 2 AC 1 at 11, [19].

and costs is traceable to the decision of the High Court in *Schellenberg v BBC*.<sup>76</sup> In this case, the plaintiff had settled an action against the *Guardian* and the *Sunday Times* when it appeared that he was likely to lose the case. The settlement was upon terms disadvantageous to the plaintiff. Notwithstanding the settlement, the plaintiff pressed on with his claim against the BBC. Eady J struck out the action against the BBC as an abuse of process. In so doing Eady J stated:

Even in a jury action it is regarded under the CPR as a judge's duty to take a realistic and practical attitude. He or she is expected to be more proactive even in areas where angels have traditionally feared to tread. I have seen nothing to suggest that the CPR are to be applied any less rigorously, or the judges are to be less interventionist, in litigation of the kind where there is a right to trial by jury. That important right is sometimes described as a "constitutional right", although the meaning of that emotive phrase is a little hazy. Nevertheless I see no reason why such cases require to be subjected to a different pre-trial regime. It is necessary to apply the overriding objective even in those categories of litigation and in particular to have regard to proportionality. Here there are tens of thousands of pounds of costs at stake and several weeks of court time. I must therefore have regard to the possible benefits that might accrue to the claimant as rendering such a significant expenditure potentially worthwhile.<sup>77</sup>

[59] Relying on the overriding objective of Part 1 of the CPR, Eady J famously declared that he was bound to ask whether "the game is worth the candle". Eady J's views were subsequently approved by the Court of Appeal in *Wallis v Valentine*<sup>78</sup> ("*Wallis*") and *Jameel v Dow Jones*<sup>79</sup> ("*Jameel v Dow Jones*").

[60] In *Wallis*, the action was struck out for being an abuse of process as the judge had found that even if the claimant succeeded, his damages would be very modest, perhaps nominal, and not such as could justify the costs of an action which was estimated to last 14 days in circumstances where the claimant had no assets. In addition, the claimant was said not to be motivated by the desire for vindication, but was pursuing a vendetta.<sup>80</sup>

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76 [2000] EMLR 296.

77 *Ibid*, at 318.

78 [2002] EWCA Div 1034.

79 [2005] QB 946.

80 See Lord Phillips in *Jameel v Dow Jones* [2005] QB 946 at 966–967.

[61] It is the Court of Appeal's decision in *Jameel v Dow Jones* that is regarded as the leading decision on this point. It is in this case that Lord Phillips MR (as he then was), following the line of Eady J's comment, declared that "[t]he game will not merely not have been worth the candle, it will not have been worth the wick."<sup>81</sup> Lord Phillips expressed that view after concluding that if the claimant was to succeed in that action, he would be vindicated but both the damage and the vindication will be minimal. He also concluded that the cost of the exercise would have been out of all proportion to what would have been achieved. Allowing the appeal, the claimant's action in defamation was struck out by the court. In coming to its conclusion in *Jameel v Dow Jones*, the Court of Appeal made reference to the overriding objective of the CPR and the coming into force of the Human Rights Act 1998.

[62] The overriding objective of the CPR requires the court to deal with cases "... justly and at proportionate cost"<sup>82</sup> and this includes the requirement to save expense. It requires courts to deal with cases in ways which are proportionate to the amount of money involved, the importance of the case, the complexity of the issues, the financial position of each party and allotting to it an appropriate share of the court's resources, while taking into account the need to allot resources to other cases.

[63] Section 6(1) of the UK Human Rights Act 1998 states that "[i]t is unlawful for a public authority to act in a way which is incompatible with a Convention right" – the Convention being the European Convention on Human Rights. Lord Phillips in *Jameel v Dow Jones* observed that:

Section 6 requires the court, as a public authority, to administer the law in a manner which is compatible with Convention rights, in so far as it is possible to do so. Keeping a proper balance between the article 10 right of freedom of expression and the protection of individual reputation must, so it seems to us, require the court to bring to a stop as an abuse of process defamation proceedings that are not serving the legitimate purpose of protecting the claimant's reputation, which includes compensating the claimant only if that reputation has been unlawfully damaged.<sup>83</sup>

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81 *Ibid.*, at 969–970.

82 Rule 1.1(1) of the UK Civil Procedure Rules 1998.

83 *Jameel v Dow Jones* [2005] QB 946 at 966, [55].

[64] While the principle in *Jameel v Dow Jones* has been extended to malicious falsehood and breach of confidence,<sup>84</sup> how far indeed may the principle extend? The principle seems to have created two categories of rights – rights which are enforceable by legal action and rights which are too trivial to enforce by legal action or the enforcement of which is disproportionate to cost and expense. In *Sullivan v Bristol Film Studios Ltd*,<sup>85</sup> the court refused to apply the principle in *Jameel v Dow Jones* to a claim for infringement of copyright. What was interesting was the remark by Lewison LJ that “If I am entitled to recover a debt of £50 I should, in principle, have access to justice to enable me to recover it if my debtor does not pay. It would be an affront to justice if my claim were simply struck out.”<sup>86</sup>

[65] The *Jameel v Dow Jones* principle has found favour in at least two local cases. *Sulaihah bt Maimunni v UEM Builders Bhd & Anor*<sup>87</sup> (“*Sulaihah bt Maimunni*”) was a case in which both the claim and counterclaim were brought in the tort of defamation. The learned judge, Hamid Sultan Abu Backer J (as he then was), held that even if either had a valid cause in defamation the damages may only be nominal and will not be proportional to the court’s resources, costs, judicial time and the strain on the tax payers’ purse. Citing the principle in *Jameel v Dow Jones*, the learned judge held that it was trite that the court has the inherent jurisdiction to strike out a matter *in limine* as an abuse of process and that there was a greater obligation to do so under the new Rules of Court 2012. Both the claim and counterclaim were accordingly struck out.

[66] *Chan Tse Yuen & Co v Yap Chin Gaik, Elaine & 2 Ors*<sup>88</sup> (“*Chan Tse Yuen & Co*”) was a case in defamation based on a solicitor’s letter of demand. While the learned judge, S Nanda Balan J, held that absolute privilege applied, he also held that the action was an abuse of process in the *Jameel v Dow Jones* sense. The learned judge held in effect that the benefit of the litigation was disproportionate to the cost that would have to be incurred. In this case, the impugned publication was only published to the plaintiff’s solicitors. Also invoked was the court’s

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84 Cases cited supra.

85 [2012] EWCA Civ 570.

86 *Sullivan v Bristol Film Studios Ltd* [2012] EWCA Civ 570 at [29].

87 [2012] MLJU 1088.

88 [2018] 1 AMR 34; [2017] 1 LNS 1409.

undisputable inherent jurisdiction to strike out a claim for abuse of process. The claim was accordingly struck out.

[67] Both *Sulaihah bt Maimunni* and *Chan Tse Yuen & Co* may have in effect extended the court's inherent jurisdiction to strike out a cause that is trivial or, even if successful, the benefits of which would be disproportionate to the cost and judicial time that would have to be incurred. This extension is indeed a robust development in favour of culling claims which, though valid in law, are too trivial or trifling versus the cost and expense of judicial time – perhaps a revitalisation of the *de minimis* principle. Ultimately, the cost and expense of judicial time would translate into cost that is borne by the public and the waste of judicial time that could be spent on expediting and dealing with more substantial matters.

[68] The principle in *Derbyshire*, the *Reynolds* defence, reportage, developments in the defence of qualified privilege and honest opinion, and the principle in *Jameel v Dow Jones* were all products of the common law. This is the strength of the common law. It has the ability to keep pace with developments in society and to ensure that the right balance between individual rights and public interest is achieved. Yet in all these developments, it is perhaps Parliament that we should be looking to for rapid and substantial law reform, with clear philosophical underpinning.

[69] In the UK, the Defamation Act 2013 has introduced far-ranging reforms. A higher threshold has been set for actionable defamation. Section 1(1) states that "A statement is not defamatory unless its publication has caused or is likely to cause serious harm to the reputation of the claimant." Section 1(2) states that "For the purposes of this section, harm to the reputation of a body that trades for profit is not 'serious harm' unless it has caused or is likely to cause the body serious financial loss". The common law defences relating to honest opinion and public interest are further liberalised by sections 3 and 4. Defences are made for website operators and publishers of peer-reviewed statements in scientific or academic journals under sections 5 and 6 respectively. There are many more major changes introduced by the legislation. All these would seem to be a significant triumph for the freedom of speech, public interest and the law in keeping current and staying relevant.

[70] Is “he that filches my good name robs me of that which not enriches him, and makes me poor” still a valid sentiment in this day and age? The whispering campaigns that appear so popular in many societies, the breaches of confidence under cover of the caveat “strictly between you and me” and the extravagance and extremity of modern day language seem somehow to render artificial and unnecessary the righteous indignation expressed in a civil suit for damages in libel or slander. Treating defamation with the deference of the old common law is no longer in sync with the reality of our time. Yet it has powerfully been put that the “[p]rotection of reputation is conducive to the public good. It is in the public interest that the reputation of public figures should not be debased falsely.”<sup>89</sup> This is the conundrum.

[71] In the political field, it would also be valid to maintain that the suitability of a candidate for election should not freely be allowed to be debased without justification. The public at large would stand liable to be misled when exercising their constitutional right to decide in the democratic process.<sup>90</sup> The converse is equally powerful. Is it not right that a clearly unsuitable political candidate be exposed? In *Goldsmith & Anor v Bhojrul & Ors*,<sup>91</sup> Buckley J held it would be contrary to the public interest to permit a political party seeking power at an election to sue in defamation. The suit brought by Sir James Goldsmith and the Referendum Party was struck out. In coming to this view, Buckley J relied on the rationale in *Derbyshire* and stated that “... it seems to me that the public interest in free speech and criticism in respect of those bodies putting themselves forward for office or to govern is also sufficiently strong to justify withholding the right to sue. Defamation actions or the threat of them would constitute a fetter on free speech at a time and on a topic when it is clearly in the public interest that there should be none.”<sup>92</sup> It would not therefore be wrong that where freedom of speech and defamation clash, the freedom of speech must prevail if the public’s interest is at stake.

[72] Our courts have kept pace with the common law’s evolving sentiments regarding the law of defamation and the public interest

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89 Per Lord Nicholls in *Reynolds v Times Newspapers Ltd & Ors* [2001] 2 AC 127 at 201B–C.

90 Reminiscent of the allegation of Russia’s interference with the recent presidential elections in the United States of America.

91 [1997] 4 All ER 268.

92 *Goldsmith & Anor v Bhojrul & Ors* [1997] 4 All ER 268 at 270–271.

that seek to keep it at bay. The courts have probably done all that they can do. Moving from case to case and declaring the law in a non-legislative manner is a slow process to accommodate change. The judiciary is not the most apt of institutions to formulate policy that is both politically sound in the interest of the public as a whole and, at the same time, constitutionally correct – preserving both meaningful freedom of speech and realistic protection from reputational damage. Governed by a legislation that is sixty years old without revision, the law of defamation in Malaysia now demands a complete review and significant rethinking, to keep abreast with the present and to provide for the foreseeable future. This is a job that only the legislature can undertake effectively and justifiably.