

DIRECTORS' AND OFFICERS' (D&O) LIABILITY

OVERVIEW:

This PDF is an introduction to EI Consulting's "Directors and Officers Liabilities". It is a general description of the legal system in Malaysia regulating D&O liability and recent trends especially where increased exposure has been detected.

D&O potential liability are contained in various enacted legislation including the Companies Act 1965 ("**CA**"), the Income Tax Act 1967, the Employees' Provident Fund Act 1991, the Copyright Act 1987 and the Environmental Quality Act 1974. This memorandum highlights some of these legislations and provides an overview of the principal areas of risk specifically applicable to directors. It should not be taken as a comprehensive list of all potential liabilities specific to directors under Malaysian law. In addition, directors may also be subjected to criminal liability under the Penal Code for such offences as fraud and criminal breach of trust and/or civil liability arising out a breach of their fiduciary duties or a failure to exercise due care and skill in carrying out their duties. These are not within the scope of this memorandum.

The comments as to any trends in the exposure of directors or officers and/or the level of risk given in this memorandum are based on known prosecutions and civil actions reported in law reports in Malaysia.

Overall, there is a gradual increase in the emphasis on directors' accountability particularly in relation to offences under the Securities Commission Act 1993 ("**SCA**") and other offences in relation to the securities industry, which are not covered in the scope of this memorandum since the activities of Eurocopter Malaysia Sdn Bhd do not generally fall within the scope of the SCA.

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A. Malaysian Companies Act 1965 (“CA”)

For the purposes of the CA, references to a “director” or “officer” have been defined in Section 4 of the CA to include the following:

“Director” includes any person occupying the position of director of a corporation by whatever name called and includes a person in accordance with whose directions or instruction the directors of a corporation are accustomed to act and an alternate or substitute director.

“Officer” in relation to a corporation includes any director, secretary or employee of the corporation.

Although criminal liability is not always expressly provided under the specific sections of the CA discussed below, there is a general penalty provision contained in section 369 of the CA which provides that a person is guilty of an offence if:

- (a) he does any prohibited act under the CA;
- (b) omits to do what he is required to do under the CA; and
- (c) otherwise contravenes or fails to comply with any provision of the CA.

1. Section 67 of the CA – Prohibition in giving Financial Assistance

<p>Type of Breach and Description of Offence</p>	<p>Save for specific exceptions contained in the CA, a company is generally prohibited from the following:</p> <p>(a) giving direct or indirect financial assistance (including a loan guarantee, security or otherwise) to any person for the purpose of or in connection with a purchase or subscription of any shares in the company or, where the company is a subsidiary, in its holding company;</p> <p>(b) in any way purchase or deal in its own shares; or</p> <p>(c) lend money on the security of its own shares.</p> <p>The exceptions to this general prohibition include where (a) a financial institution lends money to customers in the ordinary course of business other than for the specific purpose of purchasing shares in that institution; or (b) a company provides assistance to its employees to purchase shares in the company.</p> <p>Criminal and civil liability applies.</p>
<p>Applies to:-</p>	<p>Directors and Officers as defined in the CA.</p>
<p>Potential Penalties</p>	<p>In the event of any contravention of this section, the company giving such assistance is not guilty of an offence but each officer of the company who is in default is guilty of an offence against the CA.</p> <p>The penalty for such contravention is imprisonment for up to 5 years or a fine of up to RM100,000.00.</p> <p>In addition, where a person is convicted of an offence under this section, and the Court is satisfied that the company or another person has suffered loss or damage as a result of such contravention, the Court may order the convicted person to pay compensation to the company or person (as the case may be) of such amount as the Court specifies.</p>
<p>Level of Risk</p>	<p>Medium</p>
<p>Comments / Remarks / Examples</p>	<p>The prohibition under this section has its roots in the English common law and there are similar provisions in corresponding Australian and Singapore legislation. The prohibition contained in Section 67 for Malaysia is generally wider than its counterparts and there are fewer exceptions to it. There is no whitewash procedure in Malaysia.</p> <p>The purpose of the section is to protect the assets of the company and to prevent any unlawful reduction of capital.</p>

Most of the Malaysian cases in relation to this section are in respect of the prohibition of the company to give financial assistance to any person to purchase shares in that company, rather than a company purchasing or dealing in its own shares or lending money on the security of its own shares.

In ***Yap Sing Hock & Anor. v. PP [1992] 2 MLJ 714***, the Malaysian Supreme Court upheld the conviction of the directors of Lien Hoe Sawmill Co. Sdn. Bhd. ("**Lien Hoe**") for causing Lien Hoe to give financial assistance to Yap Sing Hock Holdings Sdn. Bhd. to purchase shares in Lien Hoe. The directors were fined RM2,500.00 or in default 3 months imprisonment.

In ***Kidurong Land Sdn. Bhd. v. Lim Gaik Hua [1990] 1 MLJ 485***, the Malaysian Supreme Court held that a transaction whereby a company assisted in the purchase of its own shares in breach of section 67 and to its prejudice would be a misfeasance on the part of the company's directors and in such a case the company would likely have a remedy against its directors.

2. Section 131 of the CA – Disclosure of Interests

<p>Type of Breach and Description of Offence</p>	<p>Every director of a company who is in any way, whether directly or indirectly, interested in a contract or proposed contract with the company shall as soon as practicable after the relevant facts have come to his knowledge declare the nature of his interest at a meeting of the directors of the company.</p> <p>The requirement to disclose does not apply in any case where the interest of the director consists only of being a member or creditor of a corporation which is interested in a contract or proposed contract if the interest of the director is not regarded as being a material interest. In addition, a director need not disclose that he has guaranteed a loan to the company, or that he is a director of a related corporation which is contracting with the company.</p> <p>Every director of a company who holds any office or possesses any property whereby whether directly or indirectly duties or interests might be created in conflict with his duties or interests as director shall declare at a meeting of the directors of the company the fact and the nature character and extent of the conflict.</p> <p>Criminal liability applies.</p>
<p>Applies to:-</p>	<p>Directors</p>
<p>Potential Penalties</p>	<p>Imprisonment for up to 5 years or a fine of RM150,000.00 or to both.</p>
<p>Level of Risk</p>	<p>Medium</p>
<p>Comments/Remarks/Examples</p>	<p><i>Lim Foo Yong v. PP [1976] 2 MLJ 259</i> was a case where a director appealed against his conviction for failing to disclose his interest in a contract in which the company had entered into. The defendant was the Managing Director of the company. The Court allowed the Defendant's appeal on the basis that the circumstantial evidence of the Defendant's knowledge of the offence was not entirely consistent with the hypotheses that the Defendant was guilty and thus the burden of proof was not satisfied.</p> <p>In the Singapore case of <i>Yeo Geok Seng v. PP [2000] 1 SLR 195</i>, the High Court in Singapore was of the view that a breach of the equivalent of Section 131 in Singapore was a serious offence in which the maximum fine is imposed in most cases unless there are mitigating circumstances. The Court also went on to suggest that the presence of aggravating factors such as a deliberate flouting of the provisions may result in an offender being sentenced to imprisonment. This case may be of persuasive authority in Malaysia.</p>



Interested to know more?

We believe every director and officer in Malaysia deserves to know its responsibilities when accepting the position. We hope this short introduction and two case studies helped you and teased you to gather more information.

In order to help you, EI has gathered a comprehensive document listing the different liabilities which a director has to comply with. We will gladly advise you, or even help you and your company should you wish to.

Do not hesitate to contact us – we are looking forward to reading / hearing from you

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