

**CFL2**

# **Offshore Legislation**

**8 APRIL 2003**

1. Time allowed : Three (3) hours
2. Total number of questions : Six (6) questions
3. Number of questions to be answered : Five (5) questions [20 marks each]
4. Begin each answer to a new question on a fresh page.
5. Answer **all** questions in **English**.

## ANSWER FIVE (5) QUESTIONS ONLY

1. (a) Give any **one** definition of the word "money laundering" as provided for under the Anti-Money Laundering Act 2001 (AMLA). [2]
- (b) (i) Which section of AMLA provides for the punishment of money laundering offences?[1]  
(ii) Explain the punishment for money laundering. [3]
- (c) Answer "**True**" or "**False**" for each of the following statements:
- (i) AMLA came into force on 15 March 2001. [1]  
(ii) The application of AMLA is limited to tangible property or interest held in Malaysia only. [1]  
(iii) Pursuant to section 3 of AMLA, the definition of "financial institution" includes persons licensed under the Securities Industry Act 1983. [1]  
(iv) AMLA states that reporting institutions are under obligation to maintain records for **six** years from the date the account is closed or the transaction is completed or terminated. [1]
- (d) Apart from AMLA, name the **five** other legislation that are also applicable to offshore bankers. In your answer, write short notes on the effect of each legislation on offshore banking business. [10]  
(Total:20 marks)
2. (a) What is a "mandatory injunction"? [2]
- (b) (i) What is "specific performance"? [2]  
(ii) List **three** instances where specific performance may be granted. [3]
- (c) In relation to contract law, fill in the blanks with the correct word(s) for each of the following:
- (i) An injunction that stops someone from doing something is called a \_\_\_\_\_ injunction. [1]  
(ii) An injunction operates as an \_\_\_\_\_ remedy. [1]  
(iii) An agreement without consideration is \_\_\_\_\_. [1]  
(iv) Contracts may be \_\_\_\_\_ by frustration, performance or by breach. [1]  
(v) The party to a contract seeking damages as one of the remedies for breach of contract is under a duty to \_\_\_\_\_ the loss. [1]
- (d) In relation to the law of tort, answer the following questions:
- (i) What are the functions of the law of tort? [2]  
(ii) Name the section and the relevant legislation that provides for contributory negligence in Malaysia. [2]  
(iii) List any **four** torts that are relevant to bankers. [4]  
(Total:20 marks)

3. (a) Under normal circumstances, an agent will not be liable on any contract he enters into as an agent.  
Describe **five** circumstances where an agent can be held to be personally liable. [10]
- (b) List **two** types of authority an agent may have. [2]
- (c) What is a “mandate”? In your answer, state briefly how a mandate is different from a power of attorney. [3]
- (d) In relation to banks and agencies, answer “**True**” or “**False**” for each of the following statements:
- (i) It is an agent's duty to pay sums received on behalf of his principal. [1]
- (ii) Any person who is **18** years old or above and who is of sound mind may be a principal. [1]
- (iii) A principal is bound by acts of fraud by the agent committed in the course of their business. [1]
- (iv) A principal may terminate an agency by revocation of the agent's authority. [1]
- (v) An agent has the option to obey his principal's instructions. [1]
- (Total:20 marks)
4. (a) List **three** categories of law. [3]
- (b) What is the “doctrine of binding precedent”? [2]
- (c) Answer “**True**” or “**False**” for each of the following statements:
- (i) Legislation made by the State legislature is called “Enactment”. [1]
- (ii) Section 3(2) of the Civil Law Act 1956 states that in the event of a conflict between common law and rules of equity with reference to the same matter, common law will prevail. [1]
- (iii) In Malaysia, the application of customary laws is applied in family law and land ownership. [1]
- (iv) English land law is applicable in Malaysia by virtue of section 6 of the Civil Law Act 1956. [1]
- (v) The High Court has the sole civil jurisdiction over admiralty matters. [1]
- (d) Briefly explain **five** rules of construction of a power of attorney. [10]
- (Total:20 marks)

5. (a) List any **five** types of offshore trust in Labuan. [5]
- (b) Which legislation governs the creation and recognition of offshore trusts in Labuan? [2]
- (c) Joshua, an Australian citizen, is currently on a holiday in Labuan. He has some basic knowledge about offshore trusts and is very interested to set up a trust in Labuan. However, he has some concerns and is not familiar with some of the terms that he has heard about. He now comes to see you to get your expert advice on the following:
- (i) What is meant by the term “perpetuity period”? [2]
- (ii) What is the taxation amount that will be applicable if Joshua sets up an offshore trust in Labuan? [2]
- (iii) Joshua is worried about giving up legal ownership of the trust property and wants to know if there is any way he can “check” if the trustees are doing their job well.  
Advise him on the methods of control and the effect of too much control. [5]
- (iv) What are the advantages of setting up an offshore trust in Labuan? [4]  
(Total:20 marks)
6. (a) In relation to the banker-customer relationship, how can a “conflict of interest” situation arise in dealings? [3]
- (b) What are the prohibitions relating to the “misuse of information” for bank staff? [5]
- (c) (i) A limited partner is not liable as a general partner unless the limited partner participates in the management of the partnership.  
What acts do not amount to a limited partner as participating in the management of the partnership? [10]
- (ii) What is the required composition of partners in an offshore limited partnership? [2]  
(Total:20 marks)

**- END OF QUESTION PAPER -**

## **OUTLINE ANSWERS**

### **Question 1**

This was the first time AMLA was introduced in the examinations. Candidates' lack of clarity of how much was required in answering the topic could be seen in the answers given.

Candidates should note that money laundering is not limited to illegal gains from drug trafficking. In describing the punishment for money laundering they should also give the specific period of imprisonment and the amount of the fine involved.

Candidates were also unable to name and describe accurately the legislation applicable to offshore bankers.

1. (a) The AMLA defines the word “**money laundering**” as the act of a person who (choose any **one** definition):
- engages, directly or indirectly, in a transaction that involves proceeds of any unlawful activity;
  - acquires, receives, possesses, disguises, transfers, converts, exchanges, carries, disposes, uses, removes from or brings into Malaysia proceeds of any unlawful activity; or
  - conceals, disguises or impedes the establishment of the true nature, origin, location, movement, disposition, title of, rights with respect to, or ownership of, proceeds of an unlawful activity;
- (b) (i) Section 4 of the AMLA.
- (ii) Punishment for money laundering is imprisonment of 5 years, or a RM5 million fine, or both the imprisonment and fine.
- (c) (i) False  
(ii) False  
(iii) True  
(iv) True
- (d) The following are legislation applicable to offshore bankers:
- Offshore Companies Act 1990 – sets out the legal framework for the incorporation, registration and administration of offshore companies and foreign offshore companies in Labuan.
  - Offshore Banking Act 1990 – governs offshore banking business in Labuan and covers matters such as licensing and the duties and responsibilities of licensed offshore banks. The Act regulates the operation of persons carrying on offshore banking business in Labuan.
  - Labuan Offshore Business Activity Tax Act 1990 – the profits of offshore banks are taxed under this Act. The tax amount is either 3% of the chargeable profits or RM20,000 a year at the election of the offshore banks.
  - Labuan Offshore Financial Services Authority Act 1996 – establishes the LOFSA, the statutory body solely responsible for the supervision and regulation of the offshore financial industry in Labuan.
  - Labuan Offshore Securities Industry Act 1998 – provides for offshore banks to act as custodians for mutual funds and for the administration of public funds in or from within Labuan.

## Question 2

Candidates were unable to answer most parts of this question.

Although some candidates managed to list the functions of the law of tort and also the torts applicable to bankers, none of them could name the section and relevant legislation that provides for contributory negligence in Malaysia.

2. (a) The remedy of an interlocutory injunction is used to maintain the status quo of the subject matter in a pending suit. A mandatory injunction is a court order requiring something to be done.
- (b) (i) Specific performance is a discretionary remedy. This means that the court has discretion whether or not to grant such a remedy.
- (ii) Specific performance may be granted in the following cases:
- where it concerns agreements relating to land transactions. There is a presumption that the breach of a contract to transfer immovable property cannot be adequately relieved by compensation in money;
  - where it concerns executory contracts; and
  - where actual damage cannot be ascertained.
- (c) (i) prohibitory  
(ii) equitable  
(iii) void  
(iv) discharged  
(v) mitigate
- (d) (i) The law of tort is a branch of civil law. It allows a person (the plaintiff) possessing certain interests protected by law, to claim from another person (the defendant) who has caused damage to the plaintiff, by breaching a relevant duty, such as the duty of care, owed to the plaintiff as imposed on the defendant by the general law.
- (ii) Section 12 (1) of the Civil Law Act 1956.
- (iii) Series of torts that are relevant to bankers:
- Negligence
  - Professional negligence
  - Conversion
  - Defamation
  - Libel

### Question 3

Candidates were confused with what was required in answering the question as they wrote on an agent's rights and duties, rather than the circumstances in which an agent can be held personally liable.

Candidates also had only a vague idea about what a "mandate" is and thus could not explain it accurately.

The "True/False" section on agency was well attempted.

3. (a) Personal liability of a person acting as an agent in the following circumstances:

- **Where an agent agrees to be personally liable**  
Where the agent agrees to be personally liable, such agent, and not his principal shall be liable on the contract entered into.
- **Where the agent fails to disclose the agency**  
Pursuant to Section 179 of the Contracts Act 1950 (CA), contracts entered into through an agent, and obligations arising from acts done by an agent may be enforced in the same manner and will have the same legal consequences as if the contracts had been entered into and the acts done by the principal in person.
- **Where the agent exceeds his actual authority**  
Section 180, CA provides that where an agent does more than he is authorised to do, and when the part of what he does, which is within his authority, can be separated from the part which is beyond his authority, so much only of what he does as is within his authority is binding as between him and his principal.  
  
However, where an agent has acted beyond the scope of his authority and that act cannot be separated from what is within it, the principal is not bound to recognise the transaction. In such an instance, the agent may incur personal liability. (Section 181, CA)  
  
Section 188, CA provides that where a person untruly represents himself to be the authorised agent of another and thereby induces a third person to deal with him as such, then such an agent is liable if his alleged employer does not ratify his act. The agent will have to make compensation to the other in respect of any loss or damage, which he has incurred by so dealing.  
  
Section 189, CA states that a person with whom a contract has been entered into, the character of agent is not entitled to require the performance of it, if he was in reality acting, not as an agent, but on his own account.  
  
Section 186, CA provides that in cases where an agent is personally liable, a person dealing with him may hold him or his principal, or both of them liable.
- **Where the principal does not exist or lacks contractual capacity**  
Where the agent entered into a contract as agent but the principal does not exist or where the principal lacks any contractual capacity, the agent is personally liable.
- **Where the agent signs a bill of exchange (or cheque) in his own name without indicating the agency**  
Section 26(1) of the Bills Exchange Act 1949 provides to the effect that where an agent signs a bill of exchange without indicating that he is signing as an agent, he is personally liable on the bill.
- **Where the agent contracts by deed without being appointed**  
Where the agent contracts by deed without being so appointed by deed, he is personally liable on such a contract.

- **Where trade customs make the agent liable**  
Where the agent enters into a contract where trade customs make him personally liable, the agent will be so liable even though he may have entered into the contract as an agent.
- (b) Actual authority (expressed or implied), and apparent or ostensible authority.
- (c) A mandate is a letter written by an account holder authorising a certain person to operate his bank account. A person so authorised is called the mandate-holder. A mandate only allows the mandate-holder to operate the bank account and such a person has no other authority. A power of attorney is a formal appointment by a donor granting the donee certain powers to act on behalf of the donor as contained in the power of attorney deed.
- (d) (i) True  
(ii) True  
(iii) True  
(iv) True  
(v) False

#### Question 4

Candidates were familiar with the categories of law.

A lack of proper understanding of the concept “doctrine of binding precedent” was obvious in the candidates’ answers.

The “True/False” section on Malaysian law was poorly answered and candidates lost valuable marks.

Candidates confused the “rules of construction” of a power of attorney with the “authentication” of a power of attorney.

4. (a) Law may be classified into 3 categories:
- Public law
  - Private law; and
  - International law
- (b) The practice of the court following its previous decision or a decision previously made by a judge in similar situation is called the doctrine of precedent. As decisions of higher courts bind the lower courts, it becomes the doctrine of binding precedent.
- (c) (i) True  
(ii) False  
(iii) True  
(iv) False  
(v) True
- (d) **Rules of Construction**
- A power of attorney is strictly construed according to the rules of construction.
- **The authority for a power of attorney**  
The authority for a power of attorney is limited to the purpose for which it was given and this purpose must be a legal purpose.
  - **The subject matter of the power of attorney**  
If the subject matter of the power of attorney no longer exists, the authority will be terminated by frustration.

- **The donee’s authority act**  
Sometimes the power of attorney deed may confer on the donee (agent) the authority to do “anything, which he can lawfully do by an attorney” on behalf of the donor (principal).
- **The use of general words**  
The use of general words in the deed does not confer any power to act, which will exceed the proper performance of the particular special duty or duties contained in the deed.  
  
This has particular significance in relation to the issue of bills of exchange and where the borrowing of money is concerned. Hence, if the power of attorney allows the donee “from time to time to negotiate, sell, dispose of, assign and transfer” property, this does not amount to authority to borrow money – e.g. by charging the property.
- **Agreement to ratify in advance the actions of donee by the donor**  
Where by a power of attorney, the donor agrees in advance to “ratify” whatever the donee does or purports to do under the power, this “ratification” cannot be construed so as to extend the donee’s authority beyond the purposes set out in the deed. Moreover, this would also not amount to ratification since ratification can only be retrospective. See *Midland Bank v Reckitt*.
- **Ejusdem generis**  
If general words are used, then they are limited by other special words, which describe the particular acts which the donee is authorised to perform.

#### Question 5

Candidates were able to list the types of offshore trust in Labuan and name the legislation governing the creation and recognition of offshore trusts in Labuan.

Candidates showed little understanding of the term “perpetuity period” as no one gave its complete definition.

Candidates should note that a “letter of wishes” allowed a settlor a certain amount of influence/control over how a trust is conducted.

5. (a) Give any **five** of the following:
- Purpose trust
  - Charitable trust
  - Trading trust
  - Finance trust
  - Personal trust
  - Protective trust
  - Discretionary trust
- (b) The Labuan Offshore Trusts Act 1996 (LOTA)
- (c) (i) The perpetuity period is the maximum period for which an offshore trust can exist. In other words, it is the life span of an offshore trust, which is a maximum of 100 years from the date of creation. This perpetuity period may be specified in the trust instruments although earlier termination is possible.
- (ii) The taxation amount that will be applicable will depend on whether there is any offshore trading activity or not. Pursuant to sections 4 and 7 of the Labuan Offshore Business Activity Tax Act 1990, an offshore trust which carries on any offshore trading activity is taxed respectively upon election at a rate of 3% of the net income, or a fixed sum of RM20,000.

However, if the offshore trust that Joshua wants to set up, conducts purely offshore non-trading activity, then there will not be any tax applicable.

- (iii) There are **two** ways that will allow Joshua to retain “some influence”.

Firstly Joshua, as settlor, may appoint a “protector” to oversee the trustee in the exercise of his (the trustee’s) duties and in the management of the property. Here the protector has a “watchdog” role. This will allow Joshua, who has to give up legal ownership of the trust property, to retain some “influence” over the trustees. Hence, Joshua may use the role of a protector to constitute a control mechanism.

Secondly, Joshua may retain some influence over the trustees by having a “letter of wishes”. This is a confidential communication from the settlor to the trustee indicating his preferences as to how he would wish the trustee to manage and deal with the trust property.

However, Joshua is advised that if he retains too much control on his part, then the trust he sets up would be considered a sham trust. The contention is that the powers retained by the settlor are such that nothing has really passed to the trustee. In other words, there is no trust.

- (iv) Advantages of setting up an offshore trust in Labuan:

- The accumulation of income throughout the trust period is permitted.
- Low taxation for offshore trusts carrying on offshore trading activity – 3% of net income or fixed sum of RM20,000;
- No taxation for offshore trusts with non-trading activity. There is no withholding tax imposed on the distributions received from the offshore trust by the beneficiaries. No stamp duty levied in Labuan.
- Settlers may register the offshore trust with LOFSA to obtain a certificate of registration as proof that an offshore trust has been created in Labuan. This is optional and may be attractive to some settlors.
- Anti-heirship provisions.
- Recognition of letter of wishes.
- Possible appointment of a “protector”.

### **Question 6**

Answers to parts (a) and (b) on conflict of interest situations in dealings and the prohibitions relating to the misuse of information for bank staff were limited in scope and depth. The questions aim to examine more banking practices rather than the legal issues involved.

The candidate also could not answer part (c) on limited partnership, which had been examined many times in previous examinations.

- 6.** (a) Conflicts of interest could arise in dealings:
- Between the bank and its staff;
  - Between the bank and its customers; or
  - Between the staff and the bank’s customers.
- (b) Prohibitions on “misuse of information”:
- Staff will not make use of or copy or remove any information obtained in the course of business, for the direct or indirect benefit of themselves or of any other persons.
  - Staff should not use bank or customer information to their benefit or advantage or that of any other persons.
  - Staff in possession of confidential information will not use it for their benefit or that of their spouses, parents or children in the following ways:
    - to influence any customer or any third party in dealing in any transaction; or
    - to communicate such information to any customer.
  - These prohibitions continue even after the member of staff ceases to be employed by the bank.

- (c) The following acts do not amount to a limited partner as participating in the management of the partnership:
- being a contractor, agent or employee of the partnership;
  - being a director, shareholder or officer of a corporate general partner;
  - consulting and advising a general partner on the activities of the partnership;
  - investigating, reviewing, approving or being advised on accounts or affairs of the partnership;
  - acting as surety or guarantors for the partnership;
  - approving or disapproving an amendment to the partnership agreement.
  - voting on any of the following:
    - dissolution of partnership
    - dealings in assets of the partnership
    - creation or renewal of obligation
    - change in nature of activities of the partnership
    - change in partners
    - transactions in which the general partners have conflict of interest with the limited partners.
- (d) An offshore limited partnership must comprise at least one general partner and one limited partner.