

CFL2

Offshore Legislation

10 MAY 2000

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) Answer “**True**” or “**False**” for each of the following:
- (i) The Labuan Offshore Financial Services Authority was created to govern the offshore financial industry set up in Labuan. [1]
 - (ii) Offshore investment banking is mainly governed by the Offshore Investment Banking Act 1990. [1]
 - (iii) Offshore banks are allowed to lend in Ringgit Malaysia to offshore companies. [1]
 - (iv) The Code of Good Banking Practice implemented on 1 July 1995 does not compulsorily bind offshore banks. [1]
 - (v) All partners of an offshore limited partnership can be limited partners. [1]
- (b) (i) Name the statute that governs the rate of tax paid by offshore banks. [1]
- (ii) What is the rate of tax that offshore banks pay? [3]
- (iii) Name the regulatory body of offshore banks in Labuan. [1]
- (c) (i) Describe how powers of attorney are authenticated, documented and executed in West Malaysia. [4]
- (ii) What registration requirements (if any) are there for powers of attorney (including powers of attorney in relation to land matters) in all of the following:
- Peninsular Malaysia
 - Sabah
 - Sarawak
 - Labuan
- [6]
(Total:20 marks)

2. (a) Name the various courts in Malaysia which are:
- (i) superior courts [3]
 - (ii) subordinate courts [2]
- (b) Answer “**True**” or “**False**” for each of the following:
- (i) The constitutions of Malaysia and the United Kingdom are both unwritten. [1]
 - (ii) The doctrine of judicial precedent is also known as “*stare decisis*”. [1]
 - (iii) The highest court of appeal in Malaysia is the Judicial Committee of the Privy Council. [1]
 - (iv) According to the Civil Law Act 1956, in the event of a conflict between common law and equity, the latter prevails. [1]
 - (v) The former highest court of appeal, the Supreme Court is now replaced with the Federal Court. [1]

- (c) There are about 60 offshore banks carrying on business in Labuan. State **five** basic criteria for obtaining an offshore banking licence. [5]
- (d) Answer "**True**" or "**False**" for each of the following:
- (i) Generally, offshore banks are not allowed to deal with residents of Malaysia unless the residents have obtained the permission of the Controller of Foreign Exchange to do so. [1]
 - (ii) Non-residents may maintain current accounts with offshore banks. [1]
 - (iii) The Banking and Financial Institutions Act 1989 apply generally to all offshore banks. [1]
 - (iv) Offshore investment banks are not allowed to accept deposits on current account, deposit account, savings account, or any other account as may be specified by the Labuan Offshore Financial Services Authority (LOFSA). [1]
 - (v) Credit card business is not allowed to be carried on by offshore banks under the Offshore Banking Act 1990. [1]
- (Total:20 marks)
3. (a) The acts of an agent are binding on the principal if they are performed within the authority of the agent. Describe what is meant by "actual" and "apparent" authority of an agent. [5]
- (b) Offshore bankers often act as agents for their customers. State **ten** duties owed by agents to their principals. [10]
- (c) State the circumstances under which a power of attorney (which is not irrevocable) may be revoked. [5]
- (Total:20 marks)
4. (a) What are the legal expectations and duties of offshore banks in the prevention of money laundering activities? Elaborate your answer with the provisions of relevant legislation and policies covering money laundering adopted by offshore banks. [10]
- (b) (i) Comment on the duty of an offshore banker in respect of confidentiality with regards to his/her customers and his/her banking affairs. [5]
- (ii) State the instances when a banker can disclose such information relating to the affairs of his/her customers. [5]
- (Total:20 marks)
5. (a) Name the **two** statutes which govern the setting up of Labuan trust companies. [2]
- (b) Can a Labuan trust company be an offshore company? [1]
- (c) Describe the type of business carried on by Labuan trust companies? [3]
- (d) State and describe (by giving definitions), the persons and parties who may be involved in a trust. [4]
- (e) State **ten** benefits of creating offshore trusts. [10]
- (Total:20 marks)

6. (a) In the context of the tort of negligence, explain the following terms and phrases:
- (i) duty of care [3]
 - (ii) standard of care [4]
 - (iii) damage suffered must not be too remote [3]
- (b) Answer “**True**” or “**False**” for each of the following:
- (i) The principle of undue influence is provided for in the Contracts Act 1950. [1]
 - (ii) There is a presumption of undue influence between a solicitor and his client. [1]
 - (iii) The burden of proving that the contract was not induced by undue influence lies on the person being induced. [1]
 - (iv) The effect of undue influence is to render the contract void. [1]
 - (v) A banker is deemed to be in a position to dominate the will of his client where the client’s mental capacity is permanently affected by reason of old age. [1]
- (c)
- (i) What is the age of majority under the Age of Majority Act 1971? [1]
 - (ii) The general rule in Malaysia is that contracts made by minors are void. State **three** exceptions. [3]
 - (iii) Are agreements by way of wager valid, void or voidable? [1]

OUTLINE ANSWERS

Question 1

Understanding of the concepts such as, “rate of tax” and “registration requirements” was fair. Students had difficulty though, in explaining the registration requirements for powers of attorney.

1. (a) (i) True
(ii) False
(iii) False
(iv) True
(v) False
- (b) (i) The Labuan Offshore Business Activity Tax Act 1990
(ii) 3% of chargeable profits or RM200 000, a year, depending on the choice of the bank
(iii) Labuan Offshore Financial Services Authority
- (c) (i) **Process of Authentication**
A power of attorney must be made by deed. This means that it is signed by the donor in the presence of a witness attesting to his signature, or it is signed at his direction in his presence and the presence of two witnesses who attest to his signature. This process is called authentication of a power of attorney.

Execution of Powers of Attorney in Peninsular Malaysia

If a power of attorney is executed in Peninsular Malaysia, the power of attorney instrument must be authenticated in the form set out in the First Schedule of the Powers of Attorney Act 1949, by virtue of Section 3(1)(a) Powers of Attorney Act, 1949, by either:

- a magistrate
- a Justice of Peace
- a Land Administrator
- a notary public
- a Commissioner for Oaths
- an advocate and solicitor, *or*
- an officer acting in the course of his employment, of a company carrying on the business of banking in Peninsular Malaysia and incorporated by or under any written law in force in Peninsular Malaysia

(ii) **Peninsular Malaysia**

Section 4 of the Powers of Attorney Act requires all powers of attorney within Peninsular Malaysia to be deposited in the High Court. In addition, if the Powers of Attorney relates to land, the Power of Attorney needs to be registered with the relevant Land Registry/Land Office.

Sabah

In Sabah, the Powers of Attorney Act does not apply. There is no legal requirement for powers of attorney to be registered with the High Court. Some Magistrates' Courts allow for lodgement of powers of attorney. However, the land laws of Sabah strictly requires that all powers of attorney in relation to land must be properly attested and the power of attorney must be filed in the Land Office concerned.

Sarawak

In Sarawak, the Powers of Attorney Act does not apply. There is no legal requirement for powers of attorney to be registered with the High Court. However, the land laws of Sarawak strictly requires that all powers of attorney in relation to land must be properly attested and the power of attorney must be filed in the Land Office concerned.

Labuan

In Labuan, the Powers of Attorney Act does not apply. There is no legal requirement for powers of attorney to be registered with the High Court. However, Section 98 of the Sabah Land Ordinance requires that all powers of attorney in relation to land must be properly attested and the power of attorney must be filed in the Land Office concerned.

Question 2

The “true” or “false” questions, naming the various courts and the criteria for obtaining an offshore banking license, were the favourite among candidates. The weakest section was on stating the criteria for obtaining a license. 79% of the candidates passed this question.

2. (a) (i) The superior courts comprise the Federal Court, the Court of Appeal and the High Court.
(ii) The subordinate courts are the Sessions Courts and the Magistrates’ Courts.
- (b) (i) False
(ii) True
(iii) False
(iv) True
(v) True
- (c) **General Entry Criteria to Conduct Offshore Banking Business**
It is a policy of the Labuan Offshore Financial Services Authority (LOFSA), the statutory body solely responsible for the supervision of the offshore financial industry in Labuan, that an application for an offshore banking licence can only be considered provided the applicant meets the following criteria:
- (i) Applicant is a well established bank of international standing in the top 200 range with minimum tier-1 capital of US\$1 billion for international banks and US\$500 million for regional or domestic banks
(ii) Has good rating by established international rating agencies
(iii) Has excellent track record of financial performance
(iv) Demonstrates high expertise in international finance and foreign exchange
(v) There is no adverse report or announcement in any reliable news sources
(vi) Applicant is effectively supervised by a strong home monetary authority
(vii) Applicant is committed to a functional full-fledged operation in Labuan
- (d) (i) True
(ii) False
(iii) False
(iv) True
(v) False

Question 3

Understanding of concepts was average. Candidates were weak in certain areas, such as duties owed by agents to principals.

3. (a) An agent's acts are binding on the principal if they are done within the agent's authority. If an agent does an act which exceeds that authority so given, the principal is not bound unless he adopts and ratifies the unauthorised act.

Actual (Express or Implied) Authority

An agent's authority may be actual or apparent. Actual authority is authority expressly given by the principal (orally or in writing), or implied from the express authority given, from the circumstances of the case, custom or usage of trade, and the conduct of parties.

In *The Firm of T.A.R CT v The Firm of SV.K.R* the Privy Council decided that an agent who had authority to part with the firm's money had, in the circumstances of the case, a necessary implied authority to receive repayment for the firm.

Apparent or Ostensible Authority

Apparent or ostensible authority is that which is not expressly given by the principal but which the law regards the agent as possessing although the principal has not consented to his exercising such authority.

In *The Firm of T.A.R CT v The Firm of SV.K.R*, the Privy Council decided that an agent who had authority to part with the firm's money had, in the circumstances of the case, a necessary implied authority to receive repayment for the firm.

Secret or private restrictions on the authority of the agent do not affect a third party who does not know of such restrictions and who has acted in good faith in relying on the agent's apparent authority.

(b) **Duties of an Agent**

- (i) An agent has to obey his principal's instructions
- (ii) The agent has a duty to exercise reasonable care
- (iii) The agent has to keep proper accounts and produce them when required
- (iv) The agent has a duty to keep his principal informed
- (v) The agent has a duty not to take any secret profit or bribe
- (vi) Right of the principal to secret dealings made by the agent
- (vii) The agent has a duty to avoid a conflict of interest
- (viii) The agent has a duty to pay to his principal all sums received on his behalf
- (ix) The agent must keep his principal's affairs confidential
- (x) The agent has a duty not to delegate his authority
- (xi) Non-liability of employer of agent to do a criminal act

(c) Where a power of attorney is not expressly stated to be irrevocable, such power of attorney is revocable. Powers of attorney may be revoked by:

- (i) notice of revocation by the donor
- (ii) notice of renunciation by the donee
- (iii) death of the donor or the donee
- (iv) donee's insanity, *or*
- (v) the donor adjudicated bankrupt

Question 4

Generally, a well attempted question by most candidates.

4. (a) Offshore banks are expected to exercise due diligence in the opening of new accounts. The Act specifically states that no licensed offshore bank shall open an account for a customer whose identity is not known to the bank. LOFSA has also issued and recommended several preventive measures to be followed in order to ensure that the offshore bank does not get involved, whether unintentionally or otherwise, in money laundering activities. The core principles on the prevention of money laundering activities are:

(i) **Know Your Customer**

Be familiar with the identity and business of the customer. Section 15(2) of the OBA prohibits an offshore bank from opening an account for a customer whose identity is not known to the offshore bank. A lot of verification work is involved in this area. This means that a potential customer with documents identifying his identity and business may not automatically be allowed to open an account.

Most offshore banks have strict standards in place with respect to the opening of accounts and for ascertaining the identity of customers, beneficial owners and the source of funds deposited into an account. Some of the standards could include customer referrals or recommendations, information regarding clients' affairs, interviews and sight of original documents, e.g. passports.

(ii) **Comply with Legislation and Co-operate with Law Enforcement Agencies**

An offshore bank should ensure that business is conducted in conformity with high ethical standards and local laws and regulation pertaining to financial transactions. Offshore banks should also co-operate fully with national law enforcement authorities to the extent permitted without breaching customer confidentiality.

(iii) **Maintain Records**

An offshore bank should keep records and have adequate procedures for maintaining internal records. For example, they should maintain, for at least 5 years, all necessary records on transactions to enable them to comply swiftly with information requests from regulatory authorities. Such records must be sufficient to permit reconstruction of individual transaction or audit trails so as to provide, if necessary evidence for prosecution purposes. Essential information would be records on customer identification (e.g. copies of official identification like passports, driving licences or similar documents), account files and business correspondences.

(b) (i) **Maintenance of Strict Secrecy**

Other duties and responsibilities to be observed by an offshore bank include the maintenance of strict secrecy over the affairs of its customers. Worldwide, this is the generally accepted hallmark or selling point of offshore banking business. It is also the most important duty of the offshore bank to its customer.

Confidentiality of relations and dealings between the offshore banker and its customers is paramount not only in maintaining the banker's reputation but also in complying with legal requirements. But this is slowly being eroded in the face of mounting global demand for more transparency in banking transactions. The rising demand for more transparency arose mainly as a result of global vigilance against money laundering activities.

Importance of Confidentiality

The importance of confidentiality in offshore banking business is highlighted in Section 21 of the OBA, which says, "Nothing in this Act shall authorise the Minister or the Authority to inquire into the identity, accounts and affairs of any particular customer of the offshore bank".

It is also provided in the Act that no director or officer of any offshore bank shall divulge information relating to the affairs of a customer unless it is authorised by the customer. Moreover, it is normally encoded in the individual offshore bank's code of good practice for its employees that the employees are not allowed either during or after employment with the bank to provide information to third parties about the activities of the bank's customers.

Customer confidentiality is so important that although the Authority is empowered to conduct an examination of the offshore bank, such examination is limited to just verifying the accuracy of information submitted regularly by the bank to the Authority.

(ii) **Disclosure of Information**

An offshore bank may, however, be compelled to disclose information under certain specific circumstances, such as when the disclosure is in the interest of the internal security of Malaysia. Disclosure of customers' information, however, can be effected by way of an order of the High Court. The order can be applied by:

- an interested party if a customer is dead, bankrupt or in the case of a company, being wound up;
- public officer in the course of investigating an offence; and
- the Authority, supported by a certificate given by the relevant Minister that the disclosure is in the interest of financial or economic well-being of Malaysia or internal security of Malaysia.

Question 5

Understanding of concepts was fair. Benefits of creating offshore trusts was a weak area amongst most candidates.

5. (a) The Companies Act 1965 of the Labuan Trust Companies Act 1990 govern the setting up of Labuan trust companies.
- (b) No, a Labuan trust company must be a domestic company.
- (c) Under Section 2 of the Labuan Trust Companies Act 1990 "carrying on business" in relation to a trust company means carrying on any economic activity as a trustee, agent, executor or administrator pursuant to the objects of the trust company and, without limiting the generality of the foregoing, includes:
- (i) establishing or using a share transfer office or share registration office
 - (ii) administering, managing or otherwise dealing with property as an agent, legal personal representative or trustee, whether by servant or agent or otherwise
 - (iii) maintaining an agent for the purpose of soliciting or procuring business, whether or not the agent is continuously resident in Labuan
 - (iv) maintaining an office, agency or branch, whether or not that office, agency or branch is also used for any purpose by another company
 - (v) the provision of
 - management and accounting services to, *or*
 - directors, secretaries and registered offices for,offshore companies incorporated under the Offshore Companies Act 1990 and foreign offshore companies registered under the Act, *and*
 - (vi) incorporating or registering companies under the Offshore Companies Act 1990 and generally acting as a lodging agent for any document required to be lodged by a company or person under that Act.

- (d) (i) A settlor (grantor) is a person who makes a settlement (creates a trust) of property.
- (ii) A trustee is a person to whom legal title (legal ownership) to property is transferred (to hold such property in trust) for the benefit of the beneficiaries - the beneficial ownership of such property is for the beneficiaries.
- (iii) A beneficiary is the person entitled to benefit under the trust.
- (iv) A protector is a person (who supervises the trustee) whose consent is sometimes required before certain specified powers are exercised by the trustee under the terms of the trust; a protector may have the power to remove a trustee or appoint a new or additional trustee.

(e) **Why Offshore?**

This question can be simply answered - to get away from "onshore". The right offshore jurisdiction will offer a legal regime and infrastructure which, while sensibly regulated, permits family and commercial ventures greater flexibility, privacy and a nil or reasonably taxed environment.

Benefits of Offshore Trust

(i) **Taxation**

- The local tax jurisdiction usually cannot easily cope with offshore assets or offshore structure
- The coordination of assets in a low tax and offshore environment is simpler and cheaper
- The use of double tax treaties to reduce or remove withholding tax or other levies on profits and gains
- Pre-emigration tax planning
- The situation of international families

(ii) **Avoidance of local laws and restrictions**

- Use of structures not available locally
- Absence of exchange control
- Fixed succession regimes
- Avoidance of banking secrecy
- Restrictions of ownership of real property

(iii) **Asset protection**

- Safe haven for assets, free from political change
- Avoiding consequences of business failure and litigation (aggressive jurisdictions)
- Protection against spendthrift family members
- Better coordination of assets
- Secured succession to businesses

Uses of Offshore Trust

(i) **Estate Planning**

- By properly settling a trust prior to an individual's death, the assets should not form part of the estate. Therefore, it may substantially reduce, if not eliminate, estate tax payable to the government. This may thus minimise inheritance tax, death tax and capital transfer tax. Estate planning include:
 - Ensuring succession of assets to family members. The transfer of wealth to the next generation is secured.
 - Restricting or placing conditions on receipts of gifts (e.g. entering university)
 - Eliminating or reducing estate administration cost
 - Appointing a professional to manage the assets rather than a family member with no business acumen
 - Preferring privacy

- (ii) **Tax planning**
A properly structured offshore trust often can invest the trust property in stocks and shares for instance, and accumulate wealth on a reduced tax, if not, tax free basis, depending on the trust investments selected.
- (iii) **Asset protection**
Protective trust is a trust that, in order to protect the settlor's interest and intention, may make the interest of the beneficiaries in the trust property, or in any income or capital of such property, be terminated or restricted from being alienated or disposed.

Besides protecting the settlor from the beneficiaries, there is also preservation of the assets from future creditors. Under some asset protection laws, professionals who may be the target in a civil law suit, or individuals such as directors facing claimant or bankruptcy charges, may opt to go to those jurisdictions to set up offshore trusts.
- (iv) **Immigration planning**
As the business world become increasingly global, more individuals will physically relocate from their jurisdictions or country and emigrate to another country. By setting up an offshore trust, he would be able to take some opportunities that arise and could shelter his assets from taxation at his new home.
- (v) **Minimise legal complication**
As opposed to having a death will, the settlor may transfer the assets during his lifetime to a trust and such assets could pass without going through a court probate, thus saving costs, and facilitating quicker distribution of the assets to his intended beneficiaries. This is especially useful if there are assets in different countries.
- (vi) **Confidentiality**
A trust is a private agreement between a client and the trustee. As such, there is confidentiality as to the terms and professional discretion exercised with respect to the distributions to the beneficiaries. Confidentiality is not secrecy.
- (vii) **Continuity in management**
By transferring his assets to the trustee during his lifetime, the trustee can keep the necessary records in order to guard his assets. Furthermore, the trustee may be informed as to which one of his family members should manage his businesses, while at the same time protecting the interests of the other members of his family.

Question 6

Understanding was weak among candidates.

6. (a) **Definition of Negligence**
Lord Wright in *Lochgelly Iron and Coal Co. v Mc.Mullan* defined negligence as a tort which consists of a legal duty of care towards the plaintiff and there is a breach of this duty of care by the defendant, thereby causing damage to the plaintiff.
- Elements of Negligence**
The elements of negligence are:
- (i) A legal duty on the part of the defendant towards the plaintiff to exercise care in such conduct of the defendant as falls within the scope of his duty
 - (ii) Breach by the defendant of that duty, *and*
 - (iii) Consequential damage suffered by the plaintiff
- (i) **Duty of Care**
Before a person can claim for negligence, it is necessary to show that the defendant owed a duty of care to the plaintiff. The significance of the element of duty of care is that it determines whether the type of loss suffered by the plaintiff in the particular manner of which it had occurred, could be actionable.

The test for the existence of a duty of care owed by the defendant to the plaintiff is laid down by the 'neighbour' principle, which is the test of reasonable foresight.

Under this test, a duty of care exists if it was reasonably foreseeable that the plaintiff would be injured as a consequence of the defendant's acts or omissions. This test laid down by Lord Atkin in the case of *Donoghue v Stevenson*, when it was stated that:

"...You must take reasonable care to avoid acts or omissions which you can reasonably foresee would likely to injure your neighbour. Who, then, in law is my neighbour? The answer seems to be – persons who are so closely and directly affected by my act that I ought to reasonably have them in contemplation as being so affected..."

In *Haley v London Electricity Board*, it was held that a plaintiff need not be identifiable specifically by the defendant. It is sufficient if the plaintiff is one of a class of persons within the area of foreseeable injury.

Breach of Duty

The second element, which must exist in order to raise the tort of negligence, is the fact that the defendant has breached the duty of care owed by him to the plaintiff.

(ii) **Standard of care**

The standard of the care, which is expected of a defendant, is that of reasonable person. This was laid down by Alderson B. in *Blyth v Birmingham Waterworks Company*:

"Negligence is the omission to do something which a reasonable man, guided upon those considerations which ordinarily regulate the human conduct of human affairs, would do, or something which a prudent and reasonable man would not do".

Reasonable man

A 'reasonable man' refers to the any ordinary or lay person on the street, who should rightly be of prudent or reasonable mentality or reasoning.

Possessing special skills or belonging to specific professions

However, where the defendant is exercising special skills or belongs to a specific profession, the defendant has to conform to the standards of a reasonable person possessing those special skills or of a reasonable member in that profession. This was so held in the case of *Philips v Whiteley*.

Reasonable foresight

The standard of what is 'reasonable' is based on objective and impartial standards.

Test for reasonable foresight

Judges decide what a reasonable man would have in contemplation in the circumstances of each case and accordingly what the defendant ought to have foreseen – *Glasgow Corporation v Muir*. In other words, would a reasonable man, in similar circumstances as applicable to the defendant, have foreseen that his actions would cause the plaintiff to suffer damage? Hence, reasonable foreseeability of a consequence is determined by the knowledge and experience, which is attributed to a reasonable man, in the given circumstances.

In the case of *Roe v Minister of Health*, a case of medical negligence, the question of whether the defendant did conform to what would have been done by a reasonable body of medical opinion was asked.

It was held that in such situations, different doctors may have different views about what should be done and therefore, it was decided that a single right or wrong answer would not necessarily be available in the circumstances.

In short, for every case where a duty of care exists, in considering whether this duty was breached by the defendant, the court must consider:

- the magnitude of the risk, that is the likelihood that injury will occur and the seriousness of the injury that is risked – see *Bolton v Stone*.
- the importance of the object to be obtained, that is to balance the risk against the consequences of not taking it. See *Daborn v Bath Tramsways*.
- the practicability of precautions, that is the risk must be balanced against the measures necessary to eliminate it and the practical measures, which the defendant could have taken. See *Latimer v A.E.C.*

(iii) **Damage suffered by the plaintiff must not be too remote**

In order to establish negligence, the third element to satisfy is that the damage suffered by the plaintiff must have been caused by the defendant's breach of duty owed to the plaintiff, and such damage must not be too remote. See *Barnett v Chelsea and Kensington Hospital Management Committee*.

Remoteness deals with whether the tort is legally, relevant to the injury. In the case of *The Wagon Mound*, the Privy Council held that consequences are too remote if a reasonable man would not have foreseen them. Hence, a defendant will only be liable for damages of which is reasonably foreseeable.

In assessing damages for libel, the courts would take into consideration the following:

- the position and standing of the plaintiff
- the nature of the libel
- the mode and extent of the publications
- the absence of any retraction or apology, *and*
- the whole conduct of the defendant from the time when the libel was published, down to the very moment of verdict – See *Ng Cheng Kiat v Overseas Chinese Banking Corporation*.

- (b) (i) True
- (ii) True
- (iii) False
- (iv) False
- (v) True

- (c) (i) 18 years
- (ii) (1) contracts for necessities
- (2) contracts of scholarship
- (3) contracts of insurance
- (iii) Gaming contracts are void