

CFL2

Offshore Legislation

8 MAY 2002

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) List any **five** matters that come under the High Court's civil jurisdiction. [5]
- (b) What are void contracts? [2]
- (c) State any **five** types of contracts or agreements that are void. [5]
- (d) (i) Briefly explain the term "right of restitution". [2]
- (ii) What is the rationale for the right stated in (i) above? [1]
- (e) State the instances where specific performance may be granted. [3]
- (f) What is a "mandatory injunction"? [2]
- (Total:20 marks)

2. (a) Answer "**True**" or "**False**" for each of the following:
- (i) A tort is a civil wrong that is committed against the Courts. [1]
- (ii) The test for professional negligence is judged by the test of the highest skilled expert. [1]
- (iii) *Ex turpi causa non oritur action* is a remedy that is available for the tort of conversion. [1]
- (iv) The only remedy for the tort of defamation is damages. [1]
- (v) The law of tort in Malaysia is governed by the Civil Law Act 1956. [1]
- (b) (i) Explain the process of "authentication of a power of attorney". [3]
- (ii) State the requirement of powers of attorney in relation to land laws in Labuan. Include in your answer, the relevant statutory provisions, if any. [3]
- (iii) What does section 4 of the Powers of Attorney Act 1949 provide for? [2]
- (c) What is a mandate? [3]
- (d) What is the difference between the terms "damage" and "damages"? [4]
- (Total:20 marks)

3. (a) Fill in the blanks with the correct answers for each of the following:
- (i) An application to the Court for a new trial or to set aside a judgement after a trial is known as an _____. [1]
- (ii) An action for the recovery of immovable property whereby the amount may exceed RM250,000.00 will be heard and determined by the _____ Court. [1]
- (iii) The _____ hears and determines civil appeals from the decision of the High Court where the amount or value of the subject matter of the claim is above RM250,000.00. [1]
- (iv) **One** of the methods used in the settlement of disputes, which can be defined as "a settlement of dispute by an appointment of a person which is agreed to by the parties to the contract", is known as _____. [1]
- (v) Judge-made law is more properly referred to as _____. [1]

- (b) Answer the following questions in relation to the duties of an offshore bank in Labuan in the conduct of its business:
- (i) State any **three** of the duties of an offshore bank in the conduct of its business. [3]
 - (ii) State any **five** of the prohibited activities. [5]
- (c) What are the core principles on the prevention of money laundering activities? Your answer should also include relevant examples of how these principles are implemented. [7]
(Total:20 marks)
4. (a) Explain how a trust becomes an offshore trust in Labuan. [8]
- (b) What are the forced heirship rules? [2]
- (c) Describe briefly the asset protection provisions. [5]
- (d) Name any **five** types of offshore trusts provided for by the Labuan Offshore Trusts Act 1990. [5]
(Total:20 marks)
5. (a) Banks must observe a strict duty of confidentiality in relation to information about their customers.

State **four** exceptional circumstances permitted by law when a bank may disclose such information. [4]
- (b) Answer “**True**” or “**False**” for each of the following:
- (i) The Code of Good Banking Practice is not binding on offshore banks in Labuan. [1]
 - (ii) The provisions of the Banking and Financial Institutions Act 1989 do not apply to licensed offshore banks including those which are owned by Malaysian banks. [1]
 - (iii) The profits of offshore banks are taxed at 3% of chargeable profits or RM20,000 a year, elected at the bank’s choice. [1]
 - (iv) The statute that governs “powers of attorney” for offshore bankers in Labuan is the Offshore Banking Act 1990. [1]
 - (v) The Labuan Offshore Limited Partnerships Act 1997 governs that residents of Malaysia are allowed to form an offshore limited partnership for any lawful purpose. [1]
- (c) Explain how the agency of ratification can arise and the effects of ratification. In your answer, include the conditions to be satisfied leading to ratification. [11]
(Total:20 marks)
6. (a) Ani, Peggy and Shila want to form an offshore limited partnership in Labuan but are not too familiar with the requirements for this process. Ani is a retired engineer from Iceland and Peggy comes from Timbuktu while Shila is currently residing in Labuan. The trio has decided that Shila should be appointed as the general partner while Ani and Peggy will act as the limited partners. They now seek your advice on the following:
- (i) How do they form an offshore limited partnership? What are the types of partnerships that can be established in Labuan? They would also like you to suggest the type of offshore partnership that they should establish and your reasons as to why that would be best suited for them. [6]
 - (ii) Shila wants to know if there are any acts she is not authorised to carry out as the general partner. [3]

- (iii) Ani and Peggy also want to know their rights as limited partners. They especially want to know under what circumstances can they be held liable as general partners. [8]
- (b) Some years have now passed since Ani, Peggy and Shila came to see you. They were happy with the information you provided the last time and are now back for some more advice. Ani, Peggy and Shila now want to dissolve the limited partnership and need your expert guidance again.

Advise Ani, Peggy and Shila on how a limited partnership can be dissolved. [3]
(Total:20 marks)

- END OF QUESTION PAPER -

OUTLINE ANSWERS

Question 1

This was a very poorly answered question as candidates were unfamiliar with the concepts of void contracts, right of restitution and mandatory injunction.

As for the High Court's civil jurisdiction, candidates merely wrote "any matter above RM250,000" or "matters on appeal from the Session Court", when these are the High Court's monetary and appellate jurisdictions respectively.

1. (a) The civil jurisdiction of the High Court includes the following (any **five**):
 - Bankruptcy and companies;
 - Admiralty matters;
 - Divorce and matrimonial causes;
 - Appointment and control of guardians of infants;
 - Appointment and control of guardians of mentally disabled persons and persons of unsound mind; and
 - Probate and administration of the estate of the deceased persons.
- (b) A void contract is an agreement that is not enforceable by law because the consideration or object of that agreement is unlawful.
- (c) Contracts/agreements that are void (any **five**):
 - agreements without consideration;
 - an agreement in restraint of marriage;
 - an agreement in restraint of trade;
 - an agreement in restraint of legal proceedings;
 - an agreement with uncertain meaning; and
 - an agreement by way of wager.
- (d) (i) When an agreement is discovered to be void or when a contract becomes void, any person who has received any advantage under such an agreement or contract is bound to restore it or to pay adequate compensation for the same to the person from whom he received it.

(ii) The rationale for the right of restitution is founded upon the doctrine of unjust enrichment.
- (e) 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 monetary compensation;
 - where it concerns executory contracts; and
 - where actual damage cannot be ascertained.
- (f) A Mandatory Injunction is a court order requiring something to be done. A party can use the remedy of this interlocutory injunction to maintain the status of the subject matter in an ongoing suit.

Question 2

Candidates had weak understanding of a “mandate” and also the difference between “damage” and “damages”. Some candidates wrote all they knew about “power of attorney” but this did not answer the question.

2. (a) (i) False
(ii) False
(iii) False
(iv) True
(v) False
- (b) (i) A power of attorney must be made by deed. It must be signed by the donor in the presence of a witness attesting to his signature or is signed at his direction in his presence and the presence of two witnesses who attest to his signature. This process is called the authentication of a power of attorney.
- (ii) The Sabah Land Ordinance governs Land laws in Labuan. Section 98 of the SLO requires that all powers of attorney in relation to land must be properly attested by the relevant person (i.e. an Advocate and Solicitor for documents signed in Sabah/Sarawak or Commissioner of Oaths if signed elsewhere). Also the power of attorney must be filed in the Land Office concerned.
- (iii) S. 4 of the Powers of Attorney Act requires all powers of attorney made within Peninsular Malaysia to be deposited in the High Court.
- (c) A “mandate” is a letter written by a customer authorising a certain person to operate his bank account. A person so authorised is called the “mandate-holder” and becomes the “agent” of the customer. (He may or may not hold a power of attorney.)
- (d) The term “damage” refers to loss or injury that a plaintiff suffers as a result of the defendant’s breach of the duty of care owed to the plaintiff. “Damages” is the compensation granted by the court to the plaintiff if all the elements of negligence on the part of the defendant are successfully proven.

Question 3

One weakness of the candidates was that they listed the duties of a bank instead of an offshore bank. The question on the prevention of money laundering activities was well answered.

3. (a) (i) appeal
(ii) Sessions
(iii) Court of Appeal
(iv) Arbitration
(v) common law
- (b) (i) An offshore bank is permitted to do any of the following (any **three**):
- Transact business only in currencies other than Malaysian Ringgit;
 - Deal with Malaysian residents subject to the Exchange Control Regulations and other restrictions;
 - Submit its regular statistics and information relating to its business in Labuan to LOFSA;
 - Appoint an auditor annually;
 - Submit its financial statements together with the auditor’s report to LOFSA within three months after the close of each financial year; and
 - Maintain strict secrecy over the affairs of its customers.

- (ii) The prohibited activities of an offshore bank are as follows (any **five**):
- Not permitted to carry on business in Malaysia other than from Labuan;
 - Shall not open offices in any place in Malaysia except Labuan; (must seek permission to have marketing offices in Kuala Lumpur);
 - Not allowed to open offices in Labuan without the prior consent of LOFSA;
 - Prohibited from dealing or transacting any business in Malaysian Ringgit; (exceptions being purchase and sale of foreign currency);
 - Not permitted to operate checking accounts for its customers;
 - Not allowed to undertake foreign exchange transactions, including remittances, with or on behalf of residents that are not authorised banks; and
 - Prohibited from opening an account for a customer whose identity is not known to the offshore bank.

- (c) Offshore banks are expected to exercise due diligence in the opening of new accounts to ensure that they do not unintentionally or otherwise get involved in money laundering activities.

The core principles of the prevention of money laundering activities are:

- **Know your customer**

Section 15(2) of the Offshore Banking Act, 1990, prohibits an offshore bank from opening an account for a customer whose identity is not known to it. Banks need to be familiar with the customer's identity and business. This area needs a lot of verification work. (Note: Due diligence is required of offshore banks)

Strict standards must be adhered to with respect to the opening of accounts and also to ascertain the identity of potential customers, beneficial owners and the source of funds to be deposited in the accounts. Some of these include customer referrals or recommendations, information regarding clients' affairs, interviews and sight of original documents certifying the customer's identity and identifying the nature of business.

- **Comply with legislation and co-operate with law enforcement agencies**

An offshore bank needs to ensure that it conducts its business in conformance with high ethical standards and local laws and regulations pertaining to financial transactions. Offshore banks should also co-operate fully with national law enforcement authorities to the extent permitted without breaching customer confidentiality.

- **Maintain Records**

An offshore bank should keep records and have adequate procedures for maintaining internal records. An example would be maintaining all necessary records on transactions for at least five years. This would enable them to comply with information requests from regulatory authorities. It is vital that the records maintained are sufficient to permit reconstruction of individual transaction or audit trails so as to provide evidence for prosecution purposes, if necessary. Essential information would include account files, business correspondences and customer identification. (e.g. copies of official identification documents such as passports, driving licenses or other similar documents.)

Question 4

Candidates gave satisfactory answers on how a trust becomes an offshore trust in Labuan. However, some candidates listed the benefits of an offshore trust or wrote on the registration requirements, which were irrelevant.

None of the candidates were able to answer the questions on forced heirship rules and asset protection provisions. All candidates who attempted this question assumed the term “asset protection” meant that assets were protected for the beneficiaries’ sake.

4. (a) A trust becomes an offshore trust in Labuan if it meets the following requirements.

- **Settlor**

The settlor must be a qualified person i.e. a non-resident of Malaysia at the time of the creation of the trust.

The Exchange Control Act 1953 provides the following definitions:

– A resident of Malaysia includes:

- A citizen of Malaysia;
- A non-citizen of Malaysia who has obtained permanent resident status of Malaysia and is residing permanently in Malaysia; or
- A person who has established a place of business and is operating in Malaysia

– A non-resident of Malaysia includes:

- Any person other than a resident;
- A Malaysian citizen who has obtained permanent resident status of a territory outside Malaysia and is residing outside Malaysia; or
- An offshore company or a foreign offshore company established under the Offshore Companies Act, 1990.

- **Trust Property**

The property cannot involve any immovable property in Malaysia, unless approved by the relevant authorities and law.

- **Beneficiaries**

- They are all non-residents at the time of creation of the trust. If the beneficiaries subsequently become residents of Malaysia when they become entitled to be beneficiaries, the trust remains as an offshore trust; or
- They are all non-residents at the time any one or more of them become entitled to be beneficiaries. This means that at the time of creation of the trust, residents may be named as the beneficiaries provided that when one or more of them come of age and/or become entitled to be beneficiaries, they have to be non-residents.

- **Trustees**

There are no restrictions imposed on the number of trustees that may be provided for in a trust instrument. However, at least one of the trustees must be a Labuan trust company appointed by the settlor.

A Labuan trust company, which may be the sole trustee must be a company incorporated under the Companies Act 1965, and registered under the Labuan Trust Companies Act 1990.

- (b) Forced heirship is a means by which the state authority imposes control over an individual's power to make testamentary dispositions. This usually occurs when an individual's spouse or children are entitled by law to at least a fixed share of his estate upon death.
- (c) The provisions on assets protection are found in the Labuan Offshore Trusts Act, 1996 (LOTA). A creditor can rely on these provisions when a settlor has created an offshore trust with the principal intent to defraud the creditor, or where the disposition to the trust has rendered the settlor insolvent or without property which could satisfy the creditor's claim. LOTA puts the burden of proof beyond reasonable doubt on the claiming creditor.

However, a disposition shall not be fraudulent as against a creditor if the creation or the disposition of the property:

- took place before the creditor's cause of action accrued or had arisen;
- took place after the expiration of two years from the date the creditor's cause of action accrued; or
- took place before the expiration of two years from the date, which the creditor's cause of action accrued but he fails to commence such action before the expiration of one year from the date of such creation, disposition or registration.

In determining whether an offshore trust or disposition has rendered the settlor insolvent or without property which could satisfy the creditor's claim, the fair market value of the settlor's property at the time immediately after the creation of the trust must be taken into consideration. If the fair market value exceeds the value of the creditor's claim, at the time, then the trust or the disposition shall be deemed not to have been created with the principal intent to defraud.

- (d) The various types of trusts are as follows (any **five**):

- Purpose Trust
- Charitable trust
- Trading Trust
- Finance Trust
- Personal Trust
- Protective Trust
- Discretionary Trust

Question 5

Candidates could not fully explain agency of ratification and the effect of ratification. The answers given were too brief and not detailed enough.

5. (a) A bank may disclose information about their customers when:
- it is legally compelled to disclose;
 - there is a duty to the public to disclose;
 - the interests of a bank require disclosure; or
 - the disclosure is made at the request or with the consent of the customer.
- (b) (i) True
(ii) True
(iii) True
(iv) False
(v) True
- (c) Agency by ratification can arise in either of the following two ways: where an agent who was duly appointed has exceeded his authority; or where a person who has no authority to act for the principal has acted as if he has the authority.

When either of these scenarios occur, the principal concerned can choose to either reject or accept the contract so made. When the principal accepts and confirms such a contract, the acceptance is called ratification. Ratification may be expressed or implied. The effect of ratification is to render the contract as binding on the principal as if the agent had been properly authorised beforehand. Ratification is retrospective i.e. it dates back to the time when the original contract was made by the agent and not from the date of the principal's ratification.

However there are certain conditions that must be satisfied before a contract can be ratified:

- The act or contract must be unauthorised;
- The agent must, at the time of the contract, be expressly acting as an agent for the principal. He must not allow the third party to think that he is the principal;
- The agent must have a principal, who actually exists or is capable of being ascertained;
- The principal must have contractual capacity at the time when the contract is being made and at the time of ratification;
- The principal must, at the time of ratification, have full knowledge of all material facts, unless it is shown that he intends to ratify the contract whatever the facts may be and assume responsibility for them;
- The principal must ratify the whole act or contract; and
- The ratification must not injure a third party.

Question 6

This was a scenario-based question with several questions relating to the scenario. Instead of answering the specific parts of this question, most tended to write what they knew about limited partnerships. Most candidates suggested the right answer but gave the wrong rationale.

6. (a) Ani, Peggy and Shila are advised as follows.

The Labuan Offshore Limited Partnerships Act, 1997 (LOLPA) allows for three types of offshore limited partnerships to be established:

- **An offshore professional partnership** which can only be formed by a professional who carries on practice in accounting, actuarial science, engineering or law. The professional who forms the partnership must have in force professional indemnity insurance cover for not less than the prescribed amount with an insurer approved by LOFSA;
- **An offshore project partnership** that shall be established solely for the purpose of undertaking the project or business specified in the partnership agreement. The agreement of the partnership shall provide that the partnership be dissolved after the completion of the project and all the partners must be a body corporate; and
- **An offshore general limited partnership** that may be formed by any person for any lawful purpose.

Ani, Peggy and Shila are advised that they will not be able to establish either of the first two types of partnerships. This is because neither Peggy nor Shila are professionals, and as Ani is retired he will not be able to satisfy the requirement of the professional indemnity insurance cover needed for an offshore professional partnership.

Furthermore as all three of them are individuals they would not be allowed to establish an offshore project partnership, which requires that all partners be a body corporate.

Therefore, it is recommended that the type of partnership that they should establish is an offshore general limited partnership. It is unclear whether Shila is a resident of Malaysia or

not. However LOLPA allows even residents of Malaysia to form an offshore limited partnership for any lawful purpose.

- (b) Shila as the general partner of this offshore limited partnership has no authority to:
- do any act that makes it impossible for the partnership to operate;
 - possess property or dispose any right of the partnership other than that of the partnership's purpose; and
 - admit a person as general or limited partner unless provided for in the partnership agreement.

- (c) Ani and Peggy are advised that as the limited partners, their rights include:

- having access to full information on the affairs of the partnership;
- making inspections on the partnership;
- making demands for return of their contribution:
 - upon dissolution of the partnership;
 - at the time specified in the partnership agreement;
 - after they have given 6 months' notice; or
 - not being liable to creditors of the partnership.

Ani and Peggy are hereby advised that as limited partners, they are not liable as general partners unless they participate in the management of the partnership. However they may partake in any one of the following acts as these do not amount to participation 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; and
 - transactions in which the general partners have conflict of interest with the limited partners.

- (d) The **three** persons are advised as follows. Shila as the general partner can dissolve the offshore limited partnership by filing a notice of dissolution with the Authority. However they also need to be aware that an automatic dissolution would take effect upon the death, bankruptcy, legal incapacity or withdrawal of the sole or general partner i.e. Shila.

In such an event, the limited partners could avoid automatic dissolution if they elect one or more general partners within 60 days of the event. A partnership may also be dissolved by an order of the court, upon the application by a partner. In granting an order to dissolve the partnership, the court must be satisfied of any of the following:

- the partnership has been conducted contrary to the terms of the agreement;
- the partnership has been conducted in a manner that is "oppressive" to the limited partner; or
- that it is equitable to dissolve the partnership.