



Firasat Newsletter

Dear clients and friends,

I had the opportunity to visit Robben Island during the firm's recent global network Lawworld meeting held in Cape Town, South Africa in early April. These words were placed at the walls of the prison where Mr Mandela was held captive as a prisoner for more than 20 years. It reads "The greatest glory in living lies not in never falling but in rising every time we fall". I suppose that those words will apply to all of us be it in our social or professional working life to continue striving amidst all the challenges. In this global world with the recent TPPA and downward trend of oil prices, one has to continue to innovate to remain relevant. It is with this in mind that we at MRCO hopes to continue to think outside the box to deliver the effective business solution to our clients. I am also pleased to note that with your support, MRCO was nominated in a number of deals at the recent ALB law awards held at the Intercontinental Kuala Lumpur. We were nominated for finalist in Real Estate Law Firm of the Year, Boutique Law Firm of the Year and M&A Deal of the Year. For this month's edition, our associate Najwa will be deliberating on a very important topic in corporate law being related party transaction. We hope you will find it useful in your decision making.

*Yours truly,
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RELATED PARTY TRANSACTIONS (RPT): HOW RELATED IS THE RPT?

"Related party transactions have been a feature of a number of financial scandals in recent years, many of which have had in common the dominance of the company by a powerful chief executive who was also involved with the related parties" - Sir David Tweedie, Chairman, International Accounting Standards Board United Kingdom.

It is prevalent for related party transactions to be part of business because cultural and political forces lead to a relationship-based system in the economy. Sir David Tweedie's statement portrays the reality of the situation and it can be worse throughout the years if there is no good governance in practice to underpin the good conduct and good judgment of a company. A good governance practice will ensure a company places a policy or process for managing Related Party Transactions to reduce corporate risk and protect members' interests.

As a basic understanding of the concept, Related Party Transaction is defined as a transaction entered into by a company or its subsidiaries which involve the interest, direct or indirect, of a related party. Related Party refers to director, major shareholder or persons connected with such director or major shareholder.

For this month's newsletter, our aim is to illustrate situations where Related Party Transactions may arise and the requirements of which parties need to comply to avoid illegal and void transactions being entered into. We will explain via hypothetical situations where related party transactions may happen.

Company ABC Berhad is a listed company and the Company's nature of business is property development with core business in development and real estate with development potential. The shareholders of the Company are Company DEF Sdn Bhd (40%), Company GHI Sdn Bhd (30%) and Company JKL Sdn Bhd (30%). The Directors of Company ABC Berhad are Encik Ali, Encik Lim and Encik Ramu. Audited Financial Statements for the Financial Year ended 31 March 2016 shows the net assets of Company ABC Berhad is RM6,000,000.00.

One day Company ABC Berhad decides to develop a new project in Setia Alam, Shah Alam and they are looking for a parcel of land in Setia Alam, Shah Alam for the development of the project.

Encik Ali proposes to Company ABC Berhad to acquire a parcel of Land in Setia Alam, Shah Alam which belongs to his stepson, Encik Saiful for the development of the project. Encik Ali convinces the other Directors of Company ABC Berhad, Encik Lim and Encik Ramu about the acquisition of the Land from Encik Saiful. Eventually Company ABC Berhad and Encik Saiful had a discussion on the terms and conditions of the acquisition of the land. They come into an arrangement for consideration price of RM2,000,000.00 for the acquisition of the said land.

First, we need to see whether the parties, Company ABC Berhad and Encik Saiful are related to each other within the concept of Related Party Transaction? Under Section 122A of Companies Act 1965, a person shall be deemed connected with a director if he is a member of that director's family. Section 122A (2) of Companies Act 1965 has further defined that stepchildren shall be considered to be part of director's family. In view of this section, Encik Saiful is deemed to be connected/related with Encik Ali, one of the directors Company ABC Berhad.

Section 132E of Companies Act 1965 provides a company shall not carry any transaction where a person connected with such a director dispose of his non-cash assets of the requisite value to the Company. The transaction shall be void unless the transaction has been approved by resolution of the company at a general meeting. Encik Ali being "related" to the seller, Encik Saiful should also abstain from voting during the Board of Directors meeting.

Second, whether the action of acquiring the Land by the Company from Encik Saiful is a type of transaction that falls within concept of Related Party Transaction? Since Company ABC Berhad is a listed company, Clause 10.2 (I)(i) of Chapter 10 Listing Requirements list out that the act of acquiring asset by company is part of the definition of 'transaction' under Related Party Transaction.

Third, we need to ask what is the percentage ratio of the transaction involved? The valuation for the percentage ratio of acquisition of asset is calculated from the value of the assets compared to the net assets of Company ABC Berhad. We can refer to the consideration of the transaction or refer to the value stated in the valuation report to establish the value of the Land.

If the percentage ratio is calculated to be 0.25% or more, the Company is required to make an announcement of the transaction to Bursa Malaysia Berhad as soon after the terms of transaction have been agreed unless the value of the consideration is less than RM500,000.00 or it is a Recurrent Related Party Transaction.

If the percentage ratio is 5% or more, the Company is required to (i) announce the transaction to Bursa Malaysia Berhad as soon after the terms of the transaction have been agreed (ii) issue a circular to its shareholders and obtain shareholders' approval in general meeting and (iii) appoint an independent adviser who is a corporate finance adviser within the meaning of the Security Commission's Principal Adviser Guidelines before the terms of transaction are agreed upon.

If the percentage ratio is more than 25%, in addition to the above requirements, Company ABC Berhad is required to appoint a main adviser, who is a Principal Adviser before the terms of transaction are agreed upon.

When the Company is a property developer with core business in development and real estate with development potential, there will be an additional requirement which is to submit to Bursa Malaysia Berhad two (2) copies of the valuation report on the Land concerned and a copy of the valuer's undertaking letter immediately after the Company announces the transaction or at least 1 month before submitting the draft circular.

The above given hypothetical situation involves the acquisition of acquiring asset. There are many other possible transactions which could be entered by parties such as Disposal and Leasing of assets, establishment of Joint Ventures, the provision of Financial Assistance, the provision or Receipt of Service or any business transaction or arrangement entered into by company or its subsidiaries with a Related Party which the list of transactions can be referred to in Chapter 10 Transactions. Each transaction may have a different method in calculating the percentage ratio as per Clause 10.03.

From the above we can see Related Party Transactions are not totally prohibited in business as long as the interested parties and details of transactions are properly disclosed. It is the time for every company to ensure they are applying the highest possible standards of ethical, moral and legal business conduct, and at the same time ensuring that the interests of all shareholders are protected and the directors maintain their duty in good faith and act in the best interest of the company.

Readers need to be aware that it is not just the role of the Directors to achieve good and coherent corporate governance in Malaysia. Each company must ensure their employees understand the policies and procedures that need to be adhered to identify and treat Related Party Transactions to ensure compliance with the Companies Act 1965, the Main Market Listing Requirements and other applicable laws.

Najwa Aqilah Mansor
Associate

Chapter 10 Transactions, Part B Definitions , Clause 10.04 (3) (a) of Listing Requirements

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