

**Class Actions in Malaysia:
An Update on the Country Report**

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Introduction

This is an update to the country report that was submitted for the Globalization of Class Actions Conference held in Oxford, England from 12 to 14 December 2007.¹

While the procedural principles and applicable rules concerning class action remain unchanged in Malaysia, an important development that warrants mention is in the area of corporate law and corporate litigation. Recent amendments to the Malaysian Companies Act 1965² in 2007³ amongst others introduced sections 181A to 181E into the Companies Act 1965. These entirely new sections relate to an important aspect concerning class action in corporate litigation, namely a derivative action. This was followed by the release of the Final Report by the Corporate Law Reform Committee in 2008. This Report reviewed and made copious recommendations to the Companies Act 1965.⁴ Of interest to us are those recommendations relating to derivative actions and class actions.

This update will highlight and comment on the new sections 181A to 181E of the Companies Act 1965. It will then draw attention to the recommendations made by the Malaysian Corporate Law Reform Committee in its Final Report concerning derivative actions and class actions in corporate litigation. The Final Report provides us with a glimpse of what can be expected in terms of changes that may (or may not) be introduced in the area of corporate litigation. Finally, this update also discusses recent decisions of the courts in Malaysia concerning derivative actions and class actions.

The Common Law Derivative Action

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¹ . This report is available at http://www.globalclassactions.stanford.edu/PDF/Malaysia_National_Report.pdf.

² . Act 125.

³ . See the Companies (Amendment) Act 2007, Act A1299. This Act came into effect on 15 August 2007.

⁴ . See the report of the Corporate Law Reform Committee at www.ssm.com.my/clrc/.

In our country report, we noted that the procedural rules governing civil litigation do not contain any specific provision relating to the applicable procedure for a derivative action under common law. Be that as it may, the majority decision of the Court of Appeal in *Tang Kwor Ham & Ors v Pengurusan Danaharta Nasional Bhd & Ors*⁵ refused to allow the absence of such a specific provision or rule to thwart any attempt by a group of shareholders in a company from commencing a derivative action. According to the Court of Appeal in that case, a derivative action may be commenced in Malaysia by invoking the general provision concerning representative actions, namely Order 15 rule 12 of the Rules of the High Court 1980. Gopal Sri Ram JCA gave an account of how the procedure concerning representative action in Order 15 rule 12 of the Rules of the High Court 1980 had developed and opined that the rule should not be applied in a rigid manner but its application should remain as flexible as possible. This includes permitting or recognising a common law derivative action to be pursued under the general provision of Order 15 rule 12 of the Rules of the High Court 1980.⁶

Despite the positive approach taken by the majority decision of the Court of Appeal in *Tang Kwor Ham & Ors v Pengurusan Danaharta Nasional Bhd & Ors*, the application of the common law derivative action is fraught with problems and obstacles. As a result it is an unattractive remedy for a minority shareholder. One of its main problems relates to the issue of costs. In most cases, the costs of the proceedings must be borne by the individual or minority shareholder who commences the action.⁷ Costs can be crippling as the minority shareholder has to satisfy that he has the *locus standi* to sue in a preliminary hearing before he can proceed to the main action. Hence the shareholder may be reluctant to bring an action as he will have to use his own funds to proceed. Furthermore, any damages awarded by the court will go to the company for the benefit of the whole body of shareholders.

Another problem which creates a disincentive for a shareholder to use this remedy concerns the requirement of having to establish “fraud”. To commence a derivative action, an attendant requirement is that the shareholder who brings the action must show that there is “fraud on the minority” as explained in the leading common law cases.⁸ Case law demonstrates that the courts have given a restrictive and at times, ambiguous definition of fraud on the minority, thus making it difficult for a prospective complainant to satisfy this requirement.

⁵. [2006] 5 Malayan Law Journal 60.

⁶. Order 15 rule 12 of the Rules of the High Court 1980 is based on the English Rules of Supreme Court 1965 that applied prior to the 1999 reforms and the introduction of the Group Litigation Order in the Civil Procedure Rules 1998 in England and Wales.

⁷. However it may be possible for the shareholder to obtain an indemnity from the company if the court gives a judgment in favour of the company.

⁸. See *Estmanco (Kilner House) Ltd v Greater London Council* [1982] 1 WLR 2; [1982] 1 All ER 437.

In addition, another difficulty relates to a situation where there is a ratification by the general body of shareholders of the wrongdoing. At common law, ratification by the general body of shareholders regarding a wrong done to a company may amount to a decision not to sue in respect of that wrongdoing. Thus an effective ratification of a wrongdoing may adversely affect a derivative action by members regarding that wrongdoing. Apart from clear cases of expropriation or abuse of the company assets⁹ or of members' property,¹⁰ case law has not laid down a firm principle as to what type of wrongdoing can be ratified by the shareholders.¹¹

The New Statutory Derivative Action

To overcome the setbacks of the common law derivative action, the Malaysian High Level Finance Committee on Corporate Governance and the Corporate Law Reform Committee recommended that a statutory derivative action (as implemented in other jurisdictions) be introduced in Malaysia. In August 2007, the Companies (Amendment) Act 2007 inserted new sections 181A to 181E into the Companies Act 1965 which creates a new statutory derivative action for the benefit of shareholders and other complainants listed out in section 181A(4).¹²

The salient features of this new statutory derivative action are as follows. First, an action under section 181A can only be instituted with the leave of the court. Under section 181A, a complainant must also demonstrate that he is a complainant within the meaning of section 181A(4). The procedure for obtaining the leave of court is set out in section 181B. It provides that the application for leave shall be made by originating summons and no appearance need be entered.¹³ In addition, the complainant must give thirty days notice in writing to the directors of his intention to apply for leave and where leave has been granted by the court, the complainant must commence the action within thirty days of the grant of leave.¹⁴ Section 181B(4) is a key provision. It provides that the court in deciding whether or not leave shall be granted shall take into account whether the complainant is acting in good faith and whether it appears *prima facie* to be in the best interest of the company that the application be granted.

It may be noted that in developing this new statutory action, the legislature attempts to redress the setbacks of the common law derivative action. An

⁹. See *Cook v Deeks* [1916] 1 AC 554.

¹⁰. See *Brown v British Abrasive Wheel Ltd* [1919] 1 Ch 290.

¹¹. Although at present it is commonly believed that negligent acts or omissions against the company can be ratified – see *Pavlidis v Jensen* [1956] 2 All ER 89.

¹². Section 181A(4) provides that a “complainant” means:

- (i) a member or person entitled to be a member of the company
- (ii) a former member if the application relates to circumstances in which the member ceased to be a member
- (iii) any director of the company; or
- (iv) the Registrar in the case of a company which is under investigation under Part IX of the Companies Act 1965

¹³. See section 181B(1) of the Companies Act 1965.

¹⁴. See section 181B(2) and (3) of the Companies Act 1965.

example of this is found in section 181D which deals with the effect of a ratification of the wrongdoing. Under section 181D(a), a ratification by the shareholders *will not prevent*¹⁵ a complainant from bringing a statutory derivative action with the leave of the court under the new provisions.¹⁶ Another example of the legislature's intention to overcome the difficulties of the common law derivative action is section 181E. This section provides that the court, in granting leave under section 181A, may make appropriate orders including an order requiring the company to pay reasonable legal fees and disbursements incurred by the complainant in connection with the action and also an order as to indemnification for costs.¹⁷ This will go a long way to encourage shareholders' actions against their company's wrongdoers.

Finally, it must be noted that the common law derivative action appears to be preserved by the new section 181A(3) which states:

The right of any person to bring, intervene in, defend or discontinue any proceedings on behalf of a company at common law is not abrogated.

To date, there is only one reported case which deals with this new statutory derivative action, namely *Mohd Shuaib Ishak v Celcom (Malaysia) Bhd*,¹⁸ a decision of the Malaysian High Court. In this case, the plaintiff, a former member of the defendant company (Celcom), successfully applied for leave to bring a statutory derivative action under section 181A in respect of certain business decisions taken by the directors of Celcom. At the outset, the court was satisfied that the plaintiff fell within the meaning of a "complainant" under section 181A(4) as the plaintiff was a former member of Celcom and the application related to matters and circumstances in which he ceased to be a member of Celcom. Thus the plaintiff had the *locus standi* to bring this action on behalf of Celcom. The court was also satisfied that the plaintiff had complied with the procedural requirement specified in section 181B(2), namely that thirty days notice in writing had been given to the directors of Celcom of the plaintiff's intention to apply for the leave of court. The main issue which required the court's deliberation was whether or not the requirements of section 181B(4) was satisfied, namely that (i) the plaintiff was acting in good faith and (ii) it appears *prima facie* to be in the best interest of the company that the application for leave be granted. After a detailed scrutiny of local and foreign authorities, the court expressed a view that section 181B(4) would be satisfied as long as the complainant could demonstrate "that there was a reasonable basis for the complaint and that the proposed action was legitimate and arguable, in that it had some semblance of merit". The court emphasised that at leave stage, which is the threshold stage, the court is not to

¹⁵. This is the position even if the wrongdoing is ratifiable at common law, for example, cases of negligence.

¹⁶. It may be noted however that under section 181D(c), the court may take into account the ratification in determining what order it would make.

¹⁷. See section 181E(1) (d) and (e) of the Companies Act 1965.

¹⁸. [2008] 1 LNS 314.

go into substantial issues on merits and that all the plaintiff had to show was that there was some substance in the grounds supporting the application. The learned High Court judge, Ramly J explained the above in the following terms:

It is to be stressed that at this stage the threshold requirement or guiding principles for leave to bring an action on behalf of the company under section 181A of the Companies Act, 1965 should not be narrowed down to an extreme edge so as to not to impose or place an undue burden or shackles on a Plaintiff to such an extent that it may eventually frustrate the object of procedural rules for seeking leave.

This case demonstrates that the Malaysian courts are willing to take a broad and liberal approach in interpreting the new provisions on the statutory derivative action. It is hoped that the courts will continue to take this approach so as to encourage legitimate actions by minority shareholders against wrongdoers who are in control of the company.

Review of the Companies Act 1965 – Final Report by the Corporate Law Reform Committee

A number of recommendations made by the Corporate Law Reform Committee in its Final Report concern derivative actions and class actions in the environment of company law.

The Statutory Derivative Action

One of the recommendations of the Corporate Law Reform Committee is for the introduction of a statutory derivative action. The Report categorically recommends that the statutory derivative action should be made applicable to all types of companies.¹⁹ The rationale for this recommendation is premised on the belief that a statutory derivative action “will be able to resolve the difficulties faced by members who want to bring an action on behalf of the company under the common law”.²⁰ As we have noted in the foregoing section, the Companies (Amendment) Act 2007 has already introduced a statutory derivative action which is now provided for under section 181A of the Companies Act 1965. However, as highlighted in the Final Report, the Corporate Law Reform Committee strongly recommends that the common law derivative action *be replaced* by the statutory derivation action on the ground that such an approach will provide certainty and clarity to the law.²¹ Despite the clear recommendation by the Corporate Law

¹⁹. See Recommendation 2.40 of the Final Report by the Corporate Law Reform Committee on the Review of the Companies Act 1965.

²⁰. See Chapter Two, para 13.01 of the Final Report by the Corporate Law Reform Committee on the Review of the Companies Act 1965.

²¹. See Recommendation 2.41 and Chapter Two, para 13.02 of the Final Report by the Corporate Law Reform Committee on the Review of the Companies Act 1965.

Reform Committee, the new section 181A that codifies the common law derivative action continues to preserve the right of any person to bring, intervene in, defend or discontinue any proceedings on behalf of a company at common law.²²

Besides the above notable difference between the recommendation of the Corporate Law Reform Committee in relation to the statutory derivative action and section 181A of the Companies Act 1965, other recommendations had been incorporated into the new sections 181A to 181E of the Companies Act 1965. Some of these recommendations include extending the statutory derivative action to allow an action to be brought by “any member or director of the company or any person who at the discretion of the court, is a proper person” to make an application under section 181A of the Companies Act 1965, putting into place certain safeguards to ensure that the section is not abused, and addressing issues relating to costs of the proceedings and indemnity as well as orders that the court may make. Happily, these recommendations have been incorporated into the Companies (Amendment) Act 2007.

Class Action

Although the Corporate Law Reform Committee recommended for the introduction of a statutory derivative action, it decided against making a recommendation for the introduction of a class action remedy under the Companies Act 1965. In its Consultative Document 6 entitled “Members’ Rights and Remedies”, the Corporate Law Reform Committee considered the question of whether a statutory provision should be included in Malaysian company legislation to allow a class or representative action by shareholders.²³ The Corporate Law Reform Committee acknowledged that class action is another alternative to the shareholders protection mechanism. In para 5.01 of its Consultative Document 6, it reports as follows:

The relevance of a class action to minority shareholders is that there may be cases where several minority shareholders are affected by the conduct of the directors or majority shareholders. Pooling their resources may provide a better outcome for the minority shareholders in terms of reducing the costs of bringing separate proceedings and/or increasing the amount of compensation/damages that they may obtain.

Further down in para 5.03, the Corporate Law Reform Committee acknowledges that there are indeed several shortcomings under Order 15 rule 12 of the Rules of the High Court 1980 in relation to its use by the minority shareholders. For example, where the relief requested is for damages, it will still be necessary for the persons represented to bring a separate action to establish the damage suffered by each of them. Second, since the representative persons and those

²². See section 181A(3) of the Companies Act 1965.

²³. See <http://www.ssm.com.my/clrc/cd6.pdf>.

represented are not parties to the proceedings, the court has no power to order any represented person to make discovery of documents. Third, the represented persons are not liable for costs. Hence, this would discourage many potential plaintiffs from undertaking the role of the representative plaintiff.

The Corporate Law Reform Committee also considered section 173 of the New Zealand Companies Act 1993 which provides that where a shareholder of a company brings proceedings against the company or a director, and there are other shareholders who have the same or substantially the same interest in relation to the subject-matter of the proceedings, the court may appoint that shareholder to represent all or some of the shareholders having the same or substantially the same interest. In addition, the court may also make such orders in relation to, the conduct of the proceedings, the costs of the proceedings and the distribution of any amount ordered to be paid by the company or director.

Despite the having stated the above in its Consultative Document 6, the Corporate Law Reform Committee is still of the view that there is no necessity to introduce a provision for class action under the Malaysian Companies Act 1965. The reluctance is based on the conviction that first, the provisions in section 181²⁴ and sections 181A to 181E will resolve the above problems.

Recent Decisions

The decision of the Court of Appeal in *Tunku Dato Seri Shahabudin bin Tunku Besar Burhanuddin & Ors v Lee Tak Suan & Anor*,²⁵ is significant because it reiterated the very important point that a derivative action as a procedural device is not available in every action. While it is trite that a derivative action originated from the sphere of company law, with its origins in *Foss v Harbottle*,²⁶ and thus can be invoked in an action, for example, by a group of shareholders against the directors of the company, the Court of Appeal explained that its application has over time been extended to a trade union²⁷ and a co-operative society²⁸.

Where an action involves an unincorporated society, as in the present case, the Court of Appeal refused to allow the action to be continued as a derivative action. In this case, the plaintiffs/respondents, as ordinary members of a club that was registered under the Societies Act 1966 had initiated a derivative action against the defendants/appellants, who were the committee members of the club alleging

²⁴. Section 181 of the Companies Act 1965 is a general provision which provides protection and a variety of relief to minority members of a company in cases of oppression, unfair discrimination, prejudice or acts in disregard of members' interests.

²⁵. [2008] 2 Malayan Law Journal 700.

²⁶. [1843] 2 Hare 461.

²⁷. *Edwards v Halliwell* [1950] 2 All ER 1964, *Cotter v National Union of Seamen* [1929] 2 Ch 58 and *Taylor & Anor v National Union of Mineworkers (Derbyshire Area) & Ors* [1985] BCLC 237 were cited by the Court of Appeal.

²⁸. The Court of Appeal referred to *Hui Huat v Datuk Khoo Eng Choo* [1993] 3 Current Law Journal 777 and section 9 of the Co-operative Societies Act 1993.

inter alia breach of trust, breach of fiduciary duty and negligence. The issue before the Court of Appeal was whether the plaintiffs' action should have been commenced by derivative action or representative action. The Court of Appeal easily answered the question by holding that the plaintiffs should have instituted a representative action instead of a derivative action. The Court of Appeal did not strike out the plaintiffs' action but set aside the derivative action and substituted it with a representative action.²⁹

Another recently reported decision that dealt with an unincorporated association is *Chin Mee Keong & Ors v Pesuruhjaya Sukan*.³⁰ The Court of Appeal noted that since an association cannot sue in its own name, an action should be commenced by its registered public officer. If none is registered as such, James Foong JCA said that it is then permissible for any office bearer of the association to mount a claim for and on behalf of its members. According to James Foong JCA, this would put the office bearer on the same footing as a representative for others having the same interest in the proceedings. In other words, the office bearer is deemed to have commenced a representative action under Order 15 rule 12 of the Rules of the High Court 1980. In this case, it was argued that only six out of the ten committee members brought the action. The Court of Appeal rejected the objection and held that even a single member could represent the other members.

Conclusion

It is commendable that the Malaysian legislature, on the recommendation of the Corporate Law Reform Committee, has taken steps to implement a statutory mechanism for derivative actions. What remains to be done is for the courts to interpret these statutory provisions in a broad and liberal manner so as not to stifle actions by minority shareholders against the company's wrongdoers.

It is also hoped that the changes introduced in the sphere of company law will serve as a catalyst for future reforms to promote class actions in other specific areas such as consumer protection, unfair commercial practices, competition law and environmental law.

Finally, as have been noted in our country report, there is a dire need to address a number of procedural obstacles that are found in the present Order 15 rule 12 of the Rules of the High Court 1980. These obstacles are further compounded when the government or a public authority is a defendant in a class action. Hence, we would repeat our urgent call for the regime under Order 15 rule 12 and Order 53 of the Rules of the High Court 1980 to be reviewed.³¹

²⁹. However, the parties were ordered to bear their own costs at the Court of Appeal and at the High Court below.

³⁰. [2007] 5 Current Law Journal 363.

³¹. Order 53 of the Rules of the High Court 1980 is the procedure for Judicial Review.