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# **Share Capital and Capital Maintenance – Companies Bill 2015**

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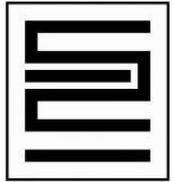
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# 1 Overview

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- Historical background and evolution of Share Capital and Capital Maintenance
  - Key changes made to the Companies Act 1965 (“**CA**”) and the effect of the changes on Share Capital and Capital Maintenance
  - Power of Company to Alter its Share Capital
  - Transitional Provisions Relating to Abolition of Nominal Value
  - Transitional Provisions Relating to Bonus Issue of Shares
  - Practical Issues on Implementation of the Changes



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# **2** HISTORICAL BACKGROUND AND EVOLUTION OF SHARE CAPITAL AND CAPITAL MAINTENANCE

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## BACKGROUND OF SHARE CAPITAL AND CAPITAL MAINTENANCE RULES

- The requirements that a company limited by shares must state its authorised share capital in its memorandum of association and that the shares must be issued with a par or nominal value are concepts found within the common law jurisdiction.
- Any allotment of shares exceeding that authorised in the memorandum of association is void – *Bank of Hindustan, China & Japan Ltd v Alison* (1871) LR 6 CP 222.
- The decision of the court in *Ooregum Gold Mining Co of India v Roper* [1892] AC 125, which was later codified into statute, sets out that issuance of shares shall not be made at discount, unless certain conditions are met.
- Both concepts are reflected in the CA.



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## BACKGROUND OF SHARE CAPITAL AND CAPITAL MAINTENANCE RULES (CONT'D)

The concepts of par value and share capital maintenance is intended to protect:

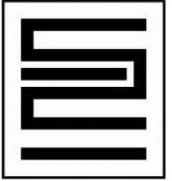
- Creditors –
  - (i) Subscribed share capital may not be repaid to shareholders without the sanction of the court. This acts as a protection of solvency for the business of a company.
  - (ii) Help lenders and/or creditors to assess the adequacy of capital of a company.
  
- Shareholders –
  - (i) Placing limitations on the issue of new shares and the repurchasing of shares to mitigate the possibility of dilution of the shareholding of existing shareholders.



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## CONCEPT OF PAR VALUE OF SHARES

- There is nothing inherent in the nature of shares which makes it necessary for shares to be ascribed a nominal value in monetary terms.
- On issue of shares at a discount, see earlier.
- The nominal value of shares can be used as a measure of a shareholder's liability towards the company. A shareholder would have discharged his obligation to contribute, once the shareholder has paid the company a sum equal to the nominal value of his shares, plus premium, if any.



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## CONCEPT OF PAR VALUE OF SHARES (cont'd)

Beyond being the measure of a shareholder's liability, the nominal value of shares is useful in:

- **declaring dividends:**

*Oakbank Oil Co Ltd v Crum [1882] 8 App Cas 65* sets out that dividends must be paid proportionately to the nominal value, not the paid up value, of the shares (Notwithstanding, Table A of CA provides that, subject to the special rights as to dividend (if any), all dividends shall be paid according to the amounts paid on the shares); and

- **determining voting rights at shareholders' meeting:**

The articles sometimes may make voting rights proportionate to the nominal value of the company's shares. Section 55 of the CA sets out that, each share (which is not a preference share) confer the right at a poll at any general meeting to one vote only for each ringgit or part of a ringgit that has been paid up on that share.



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## CONCEPT OF PAR VALUE OF SHARES (cont'd)

- The Companies Bill 2015 (“**Bill**”) introduced the no par value (“**NPV**”) regime.
- With the NPV regime, Clause 81 of the Bill sets out that, unless otherwise provided in the constitution, a company may pay dividends in proportion to the amount paid up on each share where a larger amount is paid up on some shares than on others.
- Clause 293 of the Bill provides that, (i) on a vote on a written resolution or (ii) a vote on resolution on a poll taken at a meeting, every member shall have one vote in respect of each share held by him.



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## CONCEPT OF PAR VALUE OF SHARES (cont'd)

- In a system of par value, it is usual to state the share capital in such manner:
  - *“The share capital is RM100 divided into 100 ordinary shares of RM1.00 each”*
- In a no-par system, the share capital will be represented as:
  - *“The share capital is RM100 divided into 100 ordinary shares”*



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## CONCEPT OF SHARE CAPITAL MAINTENANCE

- The doctrine of share capital maintenance is a long standing principle within company law.
- It was first demonstrated in the case of *Trevor v Whitworth* (1887) 12 App Cas 409, 57 LJ Ch 28, 36 WR 14, which said:  
*“What is the meaning of the distinction thus drawn between a company without limit of liability of its members, and a company where the liability is limited, but in the latter case to assure to those dealing with the company that the whole of the subscribed capital, unless diminished by the expenditure upon the objects defined by the memorandum, shall remain available for discharge of its liabilities? The capital may no doubt be diminished by expenditure upon and reasonably incidental to all the objects specified. Of this all persons trusting the company are aware and take the risk. But I think they have a right to rely and were intended by the legislature to have a right to rely on the capital remaining undiminished by any expenditure outside of these limits.”*



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## CONCEPT OF SHARE CAPITAL MAINTENANCE (cont'd)

- The consequences of capital maintenance are that:
  - a company with a share capital should receive proper consideration for its issued shares; and
  - no part of the share capital may be returned to the shareholders, unless expressly allowed.



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## CONCEPT OF SHARE CAPITAL MAINTENANCE (cont'd)

- This concept underpins the legal rules in the following areas:
  - Subsidiary holding shares in its holding company (Section 17 of the CA);
  - Reduction of share capital (Section 64 of the CA);
  - Redemption of preference shares (Section 61 of the CA);
  - Financial assistance (Section 67 of the CA);
  - Purchase of a company's own shares (Section 67A of the CA);
  - Restrictions on dividend distributions (Section 365 of the CA);
  - The creation of quasi capital reserve accounts (share premium account (Section 60 of the CA) and capital redemption reserve (Section 67A of the CA)) found in the current CA but not the Bill), such accounts being subject to restrictions on usage.



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## OTHER JURISDICTIONS

- Some commonwealth countries adopted the NPV regime when reforming their respective corporate legislations, such as:
  - Australia
  - Canada
  - New Zealand
  - Singapore



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## OTHER JURISDICTIONS (cont'd)

- Although UK Companies Act 2006 did not adopt the NPV regime, its capital maintenance rules have been relaxed. For example, the new procedure introduced by the UK Companies Act 2006 enables companies to reduce its share capital by a special resolution supported by a solvency statement given by all directors without the court's approval.
- UK has yet to adopt the NPV regime, as the Second Company Law Directive of the European Parliament was said to be a hindrance.
- Since the UK has left the European Union, will the UK move to adopt the NPV regime?
- Similarly, the Bill has introduced the NPV regime and some changes to the capital maintenance rules.



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## POSITION IN MALAYSIA

- The Bill, which introduces the NPV regime, has passed the first and second reading, but the Royal Assent has yet to be obtained.
- The Bill abandons the principles of requiring a company to (i) state its authorised share capital in its memorandum (Section 18 of the CA) and that (ii) shares issued must have a par or nominal value (Section 54 of the CA).
- The Bill also revises the current rules on capital maintenance.



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## POSITION IN MALAYSIA (cont'd)

- The rationale for abolishing such requirements as set out in the Consultative Document on Capital Maintenance Rules and Share Capital by the Corporate Law Reform Committee (“**Consultative Document**”) are as follows:
  - Simplifying the workings of company law so that conduct of business in Malaysia remains competitive
  - Simplify company operations by reducing compliance costs (e.g. no application for raising capital)
  - Promote corporate governance by enhancing transparency of the company’s financial accounts



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# **3** KEY CHANGES MADE TO THE COMPANIES ACT 1965 AND THE EFFECT OF THE CHANGES ON SHARE CAPITAL AND CAPITAL MAINTENANCE

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- **Introduction of NPV Regime**
    - Dispensation of the authorised share capital, share premium account and capital redemption reserves
  
  - **Extended use of the Solvency Test**
    - Redemption of Preference Shares
    - Reduction of Share Capital
    - Financial Assistance
    - Share Buy back
    - Dividends



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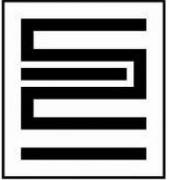
## INTRODUCTION OF NPV REGIME

- The Corporate Law Reform Committee (“**CLRC**”) which was set up by the Companies Commission Malaysia to review the CA proposed that this concept should be abandoned after taking into consideration the current law reform exercises in various Commonwealth countries.
- This concept was intended to protect shareholders’ and creditors’ rights. However, this concept can lead to a misleading perception that the nominal value of the share is the real value of the share.



## **INTRODUCTION OF NPV REGIME (cont'd)**

- Based on the consultation's responses, most bodies like General Insurance Association of Malaysia, Malaysian Accounting Standards Board, Malaysian Institute of Accountants and Securities Commission, generally supported the recommendations made by the CLRC and acknowledged the need to bring our company law in line with business needs.



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## INTRODUCTION OF NPV REGIME (cont'd)

The Australian Companies and Securities Law Review Committee suggested the following:

- The arguments for abolition of the concept of nominal value:
  - to simplify the company's accounts as share premium accounts and capital redemption reserves are not required;
  - to enable the company to undertake capital raising exercises with greater flexibility; and
  - to clarify the misleading perception that the nominal value is the real value of the share.
  
- The arguments against the abolition of the concept of nominal value:
  - investors who are commercially astute are rarely misled in assessing the value of shares by the existence of nominal value; and
  - nominal value is a means to measure liability to pay any unpaid amount of the capital subscribed.



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## INTRODUCTION OF NPV REGIME (cont'd)

- There are concerns on the setting of issue price of shares after the abolition of par value and whether there is a need to provide legislative measure against arbitrary or manipulated setting of the issue price of shares by the directors.
- This is because directors may appear to have a wider discretion in setting the issue price of shares.
- It was suggested by the minority in the Gedge Committee of 1954 (UK) that giving directors power over ancillary matters, such as the price of issue of no par value shares, would permit unscrupulous directors to defraud shareholders, whom it was claimed lack sufficient time, money and experience to make full use of their rights.



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## INTRODUCTION OF NPV REGIME (cont'd)

- Singapore has not legislated to regulate the valuation of shares.
- Section 47 of the New Zealand Companies Act 1993 requires the board to resolve that in its opinion the consideration and terms of issue are fair and reasonable to the company and to all existing shareholders, and for all directors who vote in favour of that resolution to sign a certificate to that effect (*Walter Woon on Company Law – Revised Third Edition*).
- In Malaysia, Clause 75 of the Bill provides that directors may allot shares (subject to certain exceptions) if the prior approval of the company by way of resolution had been obtained.
- However, if such approval granted by the company is general in nature, it may be open to the directors to determine the issue price of such shares and possibly defrauding shareholders.



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## INTRODUCTION OF NPV REGIME (cont'd)

- Although the abolition of par value has removed the minimum price at which shares may be issued, this does not give directors a completely free hand in setting the issue price as the directors would still have an overriding fiduciary duty to the company to set the price in good faith.
- However, the fiduciary duties of the directors are owed to the company, not the shareholders – *Brunninghausen & Anor v Glavanics (1999) 32 ACSR 294*. It is possible that directors may issue shares at a price which may be in the best interest of the company, but detrimental to the shareholders.
- The courts have been generally reluctant to inquire into the question of whether an act is bona fide in the interest of the company as demonstrated in *Re Smith and Fawcett Ltd [1942] Ch D 304*.



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## DISPENSATION OF AUTHORISED SHARE CAPITAL AND NOMINAL VALUE OF SHARE

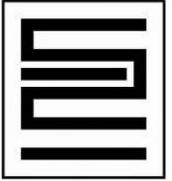
- Currently, the CA requires the authorised share capital to be included in the memorandum of every company.
- However, under the Bill, companies are no longer required to state their authorised share capital and nominal value of shares.
- This is a natural consequence of the introduction of a NPV regime.



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## DISPENSATION OF AUTHORISED SHARE CAPITAL AND NOMINAL VALUE OF SHARE (cont'd)

- The statutory quasi capital reserve accounts, namely the share premium account and the capital redemption reserve, are found in the current CA.
- Under the par value system, when shares are issued at a premium, the premium received by a company whether in cash or in other forms of consideration will be transferred to the share premium account (Section 60(2) of the CA).
- The share premium account can be utilised for certain limited purposes stated in Section 60(3) of the CA but would otherwise be subject to approval by the court and a special resolution in a manner similar to a capital reduction under Section 64 of the CA.



## **DISPENSATION OF AUTHORISED SHARE CAPITAL AND NOMINAL VALUE OF SHARE (cont'd)**

- Pursuant to Section 61(5) of the CA, where redeemable preference shares are redeemed out of distributable profits (other than proceeds of a fresh issue), a sum equal to the nominal amount of the shares redeemed will be transferred to the capital redemption reserve.
- The capital redemption reserve account may only be used for paying up unissued shares to be issued to members of the company as fully paid bonus shares (Sections 106 and 67A(4) of the CA).



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## **DISPENSATION OF AUTHORISED SHARE CAPITAL AND NOMINAL VALUE OF SHARE (cont'd)**

- Under the Bill, with the introduction of an NPV regime, there will be no requirement to maintain the share premium account and the capital redemption reserve.
- A “share capital account” may be used to hold the entire amount that the shareholders have paid for shares.
- Distributable profits currently transferable to the capital redemption reserve in relation to the redemption of redeemable preference shares will also be transferred to this share capital account.



Accounting entries in a PV and an NPV environment for the issue of 1,000 ordinary shares at RM5 each by way of cash (RM2,000) and capitalisation of RM3,000 property, plant and equipment (“PPE”) followed by the writing off of expenses in connection with the issue of shares of RM1,000 are illustrated in the diagram below. (Note: Extracted from the Consultative Document)

PV environment (assume PV = RM1)			NPV environment			
	(I) Issue of shares for cash and non-cash considerations	After (I) and writing-off the expenses against Share Premium		(I) Issue of shares for cash and non-cash considerations	After (I) and expenses Contributed Capital	writing-off against Income Statement
	RM	RM		RM	RM	RM
PPE	3,000	3,000	PPE	3,000	3,000	3,000
Cash	2,000	1,000	Cash	2,000	1,000	1,000
	<u>5,000</u>	<u>4,000</u>		<u>5,000</u>	<u>4,000</u>	<u>4,000</u>
<b>Share Capital</b>	1,000	1,000	<b>Contributed Capital</b>	5,000	4,000	5,000
<b>Share Premium</b>	4,000	3,000	<b>Accumulated Losses</b>	-	-	(1,000)
<b>Shareholders' Funds</b>	<u>5,000</u>	<u>4,000</u>	<b>Shareholders' Funds</b>	<u>5,000</u>	<u>4,000</u>	<u>4,000</u>
No of Shares (RM1)	1,000	1,000	No of Shares	1,000	1,000	1,000
<u>Accounting entries</u>			<u>Accounting entries</u>			
Dr PPE	3,000		Dr PPE	3,000		
Dr Cash	2,000		Dr Cash	2,000		
Cr Share Capital		1,000	Cr Contributed Capital			5,000
Cr Share Premium		4,000				
Dr Share Premium	1,000		Dr Contributed Capital	1,000		
Cr Cash		1,000	Cr Cash			1,000
			<i>(write-off against Contributed Capital)</i>			
			Dr Expenses - Income Statement	1,000		
			Cr Cash			1,000
			<i>(write-off against Income Statement)</i>			



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## EXTENDED USE OF THE SOLVENCY TEST

- Under the CA, the solvency test is only used by companies to purchase its own shares.

*“ Section 67A. Purchase by a company of its own shares, etc.*

*(1) Notwithstanding the provisions of section 67, a public company with a share capital may, if so authorized by its articles, purchase its own shares.*

*(2) A company shall not purchase its own shares unless -*

*(a) it is solvent at the date of the purchase and will not become insolvent by incurring the debts involved in the obligation to pay for the shares so purchased.”*

- The solvency test is a device used to protect creditors, in particular. However, the CA uses other devices to protect creditors as well, including, the use of the statutory quasi capital accounts.



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## EXTENDED USE OF THE SOLVENCY TEST (cont'd)

- The Bill applies the solvency test as a tool for capital maintenance much more widely and supplants or augments existing tools with this test.
- The solvency test is set out in Clauses 112 and 132 of the Bill. It applies to:
  1. redemption of redeemable preference shares (Clause 112(1));
  2. reduction of capital (Clause 112(1));
  3. financial assistance (Clause 112(1));
  4. share buyback (Clause 112(2)); and
  5. Dividends (Clause 132).
- This test for (1) to (3) above is satisfied if the companies:
  - can pay its debt in full immediately after any transactions mentioned above and/or within the twelve-month period after any transactions made; and
  - have more assets than liabilities at the date of transaction.



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## REDEMPTION OF REDEEMABLE PREFERENCE SHARES

- Pursuant to Section 61(3) of the CA, fully paid up shares shall be redeemed out of distributable profits or proceeds of issue of new shares made for the redemption purpose. Where there is a premium payable on redemption (if any), profits or share premium account can be used for the premium payment before the shares are redeemed.
- The capital maintenance principle is maintained here by allowing redeemable preference shares to be redeemed only out of distributable profits or a fresh issue of shares and in the case of premium, only out of share premium account or distributable profits.
- Under the current Bill, the capital maintenance rules have been modified, capital of the company can be used for redemption so long as the solvency test is satisfied and a solvency statement is made by all the directors of the company (Section 72(4)(c) of the Bill).



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## REDUCTION OF CAPITAL

- Under Section 64(1) of CA, share capital of a company can be reduced by a special resolution subject to the court's confirmation.
- With the Bill, a company may reduce its share capital by a special resolution with confirmation of court or a solvency statement by all directors of the company (Clause 115 of the Bill).
- The introduction of this alternative capital reduction procedure has been widely supported as it simplifies and facilitates the capital reduction exercises without need of confirmation by the court.



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## REDUCTION OF CAPITAL (cont'd)

- Some safeguards were recommended by CLRC in the Final Report on Review of the CA as follows:
  - Creditors can object to the capital reduction exercise with reasonable grounds within four weeks after a special resolution is passed (Clause 118 of the Bill)
  - Directors will be criminally liable for making a solvency statement without having reasonable grounds (Clause 114 of the Bill).
- Our current Bill does not provide for selective capital reduction as Australia does. Under the Corporations Act 2001, there are two types of capital reduction exercises, namely equal reduction and selective reduction. An ordinary resolution is required for equal reduction while a special resolution is required for selective reduction exercises (Section 256C).



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## FINANCIAL ASSISTANCE

- Generally, no company shall give any financial assistance in whatever form for the purpose of or in connection with purchase or subscription for its shares or shares in its holding company (Section 67(1) of the CA).
- A number of exceptions are set out in Section 67(2) of the CA as follows:-
  - “(2) *Nothing in subsection (1) shall prohibit--*
    - (a) *where the lending of money is part of the ordinary business of a company, the lending of money by the company in the ordinary course of its business;*
    - (b) *the provision by a company, in accordance with any scheme for the time being in force, of money for the purchase of or subscription for fully-paid shares in the company or its holding company, being a purchase or subscription by trustees of or for shares to be held by or for the benefit of employees of the company or a subsidiary of the company, including any director holding a salaried employment or office in the company or a subsidiary of the company; or*
    - (c) *the giving of financial assistance by a company to persons, other than directors, bona fide in the employment of the company or of a subsidiary of the company with a view to enabling those persons to purchase fully-paid shares in the company or its holding company to be held by themselves by way of beneficial ownership.”*



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## FINANCIAL ASSISTANCE (cont'd)

- Under the Bill, the provision in relation to financial assistance is:

*“Clause 123 of the Bill*

*123. (1) Unless otherwise provided in this Act, a company shall not give any financial assistance, whether directly or indirectly and whether by means of a loan, guarantee or the provision of security or otherwise, for the purpose of or in connection with a purchase or subscription made or to be made by any person of or for –*

- (a) any shares in the company; or*
- (b) in the case where the company is a subsidiary, any shares in its holding company, or in any way purchase, deal in or lend money on its own shares.*

*(2) Unless otherwise provided in this Act, a company shall not give financial assistance directly or indirectly for the purpose of reducing or discharging the liability, if –*

- (a) a person has acquired in the company or its holding company; and*
- (b) the liability has been incurred by any person for the purpose of the acquisition of the shares.”*



## FINANCIAL ASSISTANCE (cont'd)

*“Clause 125 of the Bill*

*Section 123 shall not prohibit—*

- (a) The lending of money by the company in the ordinary course of its business if the lending of money is part of the ordinary business of a company;*
- (b) the provision by a company, in accordance with any scheme for the time being in force, of money for the purchase of or subscription for fully-paid shares in the company or its holding company, being a purchase or subscription by trustees of or for shares to be held by or for the benefit of employees of the company or a subsidiary of the company, including any director holding a salaried employment or office in the company or a subsidiary of the company;*
- (c) the giving of financial assistance by a company to persons, other than directors, bona fide in the employment of the company or of a subsidiary of the company with a view to enabling those persons to purchase fully-paid shares in the company or its holding company to be held by such persons by way of beneficial ownership; or*
- (d) the making of a loan or the giving of a guarantee or the provision of security in connection with one or more loans made by one or more other persons by a company in the ordinary course of its business where the activities of that company are regulated by any written law relating to banking, insurance or takaful or which are subject to the supervision of the Securities Commission and where—*
  - (i) the lending of money or the giving of guarantees or the provision of security in connection with loans made by other persons, is done in the course of such activities; and*
  - (ii) the loan that is made by the company, or, where the guarantee is given or the security is provided in respect of a loan, such loan is made on ordinary commercial terms as to the rate of interest or returns, the terms of repayment of principal and payment of the interest or returns.”*



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## FINANCIAL ASSISTANCE (cont'd)

- Clause 123(1) of the Bill is largely based on Section 67(1) of the CA.
- It has not taken into account some important developments in major Commonwealth company law jurisdictions (will be discussed later). Among others, the difficulties arising from *Belmont Finance Corpn Ltd v Williams Furniture (No. 2) [1980] 1 All ER 393, CA*.
- The general exceptions to financial assistance by a company in dealing in its own shares are set out in Clause 125 of the Bill.



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## FINANCIAL ASSISTANCE (cont'd)

- The “whitewash” procedures are introduced in the Bill to permit financial assistance not exceeding ten per centum of the shareholders’ fund be given for the purpose of the acquisition of a share or for the purpose of reducing or discharging a liability incurred for such an acquisition (Clause 126(2) of the Bill).
- New Zealand only allows companies to give financial assistance not exceeding 5% of the shareholders’ fund. Other commonwealth countries like Australia, UK and Singapore do not have similar provisions in their companies act to limit the amount of financial assistance given.
- Clause 126(1) of our Bill provides that financial assistance can be given if the solvency test is satisfied by the Company and a special resolution is passed by its shareholders together with the solvency statements. However, companies whose shares are on stock exchange are not allowed to give any assistance.



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## FINANCIAL ASSISTANCE (cont'd)

### United Kingdom

- Under the Sections 678 and 679 of the Companies Act 2006 (UK), it is not lawful for a company or its subsidiary to give financial assistance directly or indirectly for the purpose of the acquisition of shares in a public company or private company or for the purpose of reducing or discharging the liability incurred for such an acquisition .
- The word of “acquisition” used in the Companies Act 2006 includes but not limited to purchase and subscription of shares (Section 658).



## FINANCIAL ASSISTANCE (cont'd)

There are more exceptions found in Sections 681 and 682 of the Companies Act 2006 as compared to our Bill as follows:-

### **“Section 681 Unconditional exceptions**

*This section has no associated Explanatory Notes*

- (1) *Neither section 678 nor section 679 prohibits a transaction to which this section applies.*
- (2) *Those transactions are—*
  - (a) *a distribution of the company's assets by way of—*
    - (i) *dividend lawfully made, or*
    - (ii) *distribution in the course of a company's winding up;*
  - (b) *an allotment of bonus shares;*
  - (c) *a reduction of capital under Chapter 10 of Part 17;*
  - (d) *a redemption of shares under Chapter 3 or a purchase of shares under Chapter 4 of this Part;*
  - (e) *anything done in pursuance of an order of the court under Part 26 (order sanctioning compromise or arrangement with members or creditors);*
  - (f) *anything done under an arrangement made in pursuance of section 110 of the Insolvency Act 1986 (c. 45) or Article 96 of the Insolvency (Northern Ireland) Order 1989 (S.I. 1989/2405 (N.I. 19)) (liquidator in winding up accepting shares as consideration for sale of company's property);*
  - (g) *anything done under an arrangement made between a company and its creditors that is binding on the creditors by virtue of Part 1 of the Insolvency Act 1986 or Part 2 of the Insolvency (Northern Ireland) Order 1989 (S.I. 1989/2405 (N.I. 19)).”*



## FINANCIAL ASSISTANCE (cont'd)

### ***“Section 682 Conditional exceptions***

*This section has no associated Explanatory Notes*

- (1) *Neither section 678 nor section 679 prohibits a transaction to which this section applies—*
  - (a) *if the company giving the assistance is a private company, or*
  - (b) *if the company giving the assistance is a public company and—*
    - (i) *the company has net assets that are not reduced by the giving of the assistance, or*
    - (ii) *to the extent that those assets are so reduced, the assistance is provided out of distributable profits.*
- (2) *The transactions to which this section applies are—*
  - (a) *where the lending of money is part of the ordinary business of the company, the lending of money in the ordinary course of the company's business;*
  - (b) *the provision by the company, in good faith in the interests of the company or its holding company, of financial assistance for the purposes of an employees' share scheme;*
  - (c) *the provision of financial assistance by the company for the purposes of or in connection with anything done by the company (or another company in the same group) for the purpose of enabling or facilitating transactions in shares in the first-mentioned company or its holding company between, and involving the acquisition of beneficial ownership of those shares by—*
    - (i) *bona fide employees or former employees of that company (or another company in the same group), or*
    - (ii) *spouses or civil partners, widows, widowers or surviving civil partners, or minor children or step-children of any such employees or former employees;*
  - (d) *the making by the company of loans to persons (other than directors) employed in good faith by the company with a view to enabling those persons to acquire fully paid shares in the company or its holding company to be held by them by way of beneficial ownership.”*



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## FINANCIAL ASSISTANCE (cont'd)

### Australia

- Looking at the provisions of the Corporations Act 2001 (Australia), Australian companies are generally permitted to financially assist a company to acquire shares in another company so long as:-
  - the interests of the company or its shareholders or the company's ability to pay its creditors are not materially prejudiced (Section 260A(1)) ; or
  - the assistance is approved by shareholders (Section 260(1)); or
  - the assistance falls within the general exemptions (Section 260C).



## **FINANCIAL ASSISTANCE (cont'd)**

General exemptions based on ordinary course of commercial dealing are set out in Section 260C Corporations Act 2001:-

- (1) Financial assistance is exempted from Section 260A if it is given in the ordinary course of commercial dealing and consists of:
  - (a) acquiring or creating a lien on partly-paid shares in the company for amounts payable to the company on the shares; or
  - (b) entering into an agreement with a person under which the person may make payments to the company on shares by instalments.

Special exemptions for financial institutions

- (2) Financial assistance is exempted from Section 260A if:
  - (a) the company's ordinary business includes providing finance; and
  - (b) the financial assistance is given in the ordinary course of that business and on ordinary commercial terms.

Special exemptions for subsidiaries of debenture issuers

- (3) Financial assistance is exempted from Section 260A if:
  - (a) the company is a subsidiary of a borrower in relation to debentures; and
  - (b) the financial assistance is a guarantee or other security given by the company for the repayment by the borrower
  - (c) the borrower is a borrower in relation to the debentures because it is or will be liable to repay the money; and
  - (d) the guarantee or security is given by the company in the ordinary course of commercial dealing.



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## FINANCIAL ASSISTANCE (cont'd)

Special exemption for approved employee share schemes

- (4) Financial assistance is exempted from section 260A if it is given under an employee share scheme that has been approved by:
- (a) a resolution passed at a general meeting of the company; and
  - (b) if the company is a subsidiary of a listed domestic corporation--a resolution passed at a general meeting of the listed domestic corporation; and
  - (c) if paragraph (b) does not apply but the company has a holding company that is a domestic corporation and that is not itself a subsidiary of a domestic corporation--a resolution passed at a general meeting of that holding company.

Other exemptions

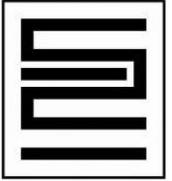
- (5) The following types of financial assistance are exempted from Section 260A;
- (a) a reduction of share capital in accordance with Division 1 of Part 2J.1;
  - (b) a share buy-back in accordance with Division 2 of Part 2J.1;
  - (c) assistance given under a court order;
  - (d) a discharge on ordinary commercial terms of a liability that the company incurred as a result of a transaction entered into on ordinary commercial terms.



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## SHARE BUY BACK

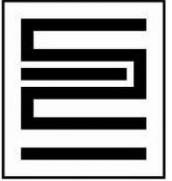
- Under Section 67A(1) of the CA, a public company may purchase its own shares , if authorised by its articles.
- Section 67A(2) sets out that:  
*“A company shall not purchase its own shares unless-*
  - (a) it is solvent at the date of the purchase and will not become insolvent incurring the debts involved in the obligation to pay for the shares so purchase;*
  - (b) the purchase is made through the stock exchange on which the shares of the company are quoted and in accordance with the relevant rules of the stock exchange; and*
  - (c) the purchase is made in good faith and in the interests of the company.”*



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## SHARE BUY BACK (cont'd)

- Under the Bill (Clause 112 of the Bill), companies are required not only to show that it is solvent at the date of solvency statement, but also during the six-month period after the share buy back.
- Under the share buy back provisions, the declaration of solvency should be made by a majority of directors, not all directors as required by the capital reduction exercises and redemption of preference shares.



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## SHARE BUY BACK (cont'd)

- Under the Clause 127(3) of the Bill, a company may purchase its own shares otherwise than through a stock exchange if the purchase is (a) permitted under the relevant rules of the stock exchange; and (b) made in accordance with such requirements as may be determined by the stock exchange.
- This addition was not provided for in the CA and this will allow flexibility to companies intending to purchase its own shares.



## SHARE BUY BACK (cont'd)

- Under the CA and the Bill, only a public listed company may purchase its own shares.
- Corporations Act 2001 (Australia) and Companies Act 2006 (UK) do not appear to impose such restriction.



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## DIVIDENDS

- Section 365 of the CA provides that dividends shall be payable to shareholders out of profits.
- However, under Clause 131 of the Bill, companies are required to show that they are solvent before a distribution is made.
- The solvency test for distribution is the company is able to pay its debts as and when the debts become due within twelve months immediately after the distribution is made.



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# 4 POWER OF COMPANY TO ALTER ITS SHARE CAPITAL

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## POWER OF COMPANY TO ALTER ITS SHARE CAPITAL

The relevant provision under the CA is set out as follows:-

### ***“62. Power of company to alter its share capital***

- (1) *A company if so authorized by its articles may in general meeting alter the conditions of its memorandum in any one or more of the following ways:*
- (a) *increase its share capital by the creation of new shares of such amount as it thinks expedient;*
  - (b) *consolidate and divide all or any of its share capital into shares of larger amount than its existing shares;*
  - (c) *convert all or any of its paid-up shares into stock and re-convert that stock into paid-up shares of any denomination;*
  - (d) *subdivide its shares or any of them into shares of smaller amount than is fixed by the memorandum, so however that in the subdivision the proportion between the amount paid and the amount, if any, unpaid on each reduced share shall be the same as it was in the case of the share from which the reduced share is derived; or*
  - (e) *cancel shares which at the date of the passing of the resolution in that behalf have not been taken or agreed to be taken by any person and diminish the amount of its share capital by the amount of the shares so cancelled.”*



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## POWER OF COMPANY TO ALTER ITS SHARE CAPITAL (cont'd)

- However, Section 21(1A) of the CA provides that a company, may by special resolution, alter or delete a provision of the memorandum of a company if the provision could lawfully have been contained in the articles of the company, unless the memorandum itself prohibits the alteration or deletion of the provisions.
- The inter-relationship between Section 62 and Section 21(1A) of the CA has created some confusion.



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## POWER OF COMPANY TO ALTER ITS SHARE CAPITAL (cont'd)

### ***“Clause 84 of the Bill***

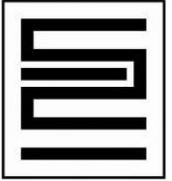
- (1) *Unless otherwise provided in the constitution, a company may alter its share capital in any one or more of the following ways by passing a special resolution to—*
- (a) *consolidate and divide all or any of its share capital, the proportion between the amount paid and the amount, if any, unpaid on each subdivided share shall be the same as it was in the case of the share from which the subdivided share is derived;*
  - (b) *convert all or any of its paid-up shares into stock and may reconvert that stock into paid-up shares; or*
  - (c) *subdivide its shares or any of the shares, whatever is in the subdivision, the proportion between the amount paid and the amount, if any, unpaid on each subdivided share shall be the same as it was in the case of the share from which the subdivided share is derived.”*



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# **5** TRANSITIONAL PROVISIONS RELATING TO ABOLITION OF NOMINAL VALUE

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## TRANSITIONAL PROVISIONS RELATING TO ABOLITION OF NOMINAL VALUE

- Clause 618 of the Bill aims to provide transitional period relating to abolition of nominal value.
- It is set out in Clause 618 that, inter alia:
  - where a share is issued before the commencement of Clause 74, the amount paid on the share shall be the sum of all amounts paid to the company at any time for the share, but not including any premium; and
  - any amount standing to the credit of a company's share premium account and capital redemption reserve shall become part of the company's share capital.



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## TRANSITIONAL PROVISIONS RELATING TO ABOLITION OF NOMINAL VALUE (cont'd)

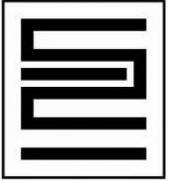
- It is also set out in Clause 618 that:
  - a company may, within 24 months upon the commencement of Clause 74, use the amount standing to the credit of:
    - its capital redemption reserve account to pay up shares which were unissued before that date and which are to be issued to members of the company as fully paid bonus shares;
    - its share premium account to:
      - (a) provide for the premium payable on redemption of debentures or redeemable preference shares issued before the commencement of Clause 74,
      - (b) pay up in whole or in part the balance unpaid on shares issued before the commencement of Clause 74 to members of the company; or
      - (c) pay dividends declared before the commencement of Clause 74, if such dividends are satisfied by the issue of shares to members of the company.



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## **TRANSITIONAL PROVISIONS RELATING TO ABOLITION OF NOMINAL VALUE (cont'd)**

- Upon the commencement of Clause 74, for the purpose of interpreting and applying a contract (including the constitution of the company) entered into before such date or a trust deed or other document executed before such date, Clause 618 also seeks to provide clarification/interpretation on any reference to:
  - the par or nominal value of a share;
  - a right to a return of capital on a share; and
  - aggregate par or nominal value of the company's issued share capital.



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# **6** TRANSITIONAL PROVISIONS RELATING TO BONUS ISSUE OF SHARES

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## TRANSITIONAL PROVISIONS RELATING TO BONUS ISSUE OF SHARES

- In the context of bonus issues and the utilisation of reserve accounts under Clause 618 of the Bill, consider Regulation 107 of Table A and other similar articles which provides that whenever directors of a company in general meeting resolve to capitalise its distributable profits or any amount standing credit of the company's reserve accounts, they shall
  - make all appropriations and applications of the undivided profits resolved to be capitalised;
  - make all allotments and issues of fully paid shares;
  - do acts or things required to give effect thereto; and
  - authorise any person to enter on behalf of all the members entitled thereto into an agreement with the company providing for the allotment to them respectively.



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# **7** PRACTICAL ISSUES ON IMPLEMENTATION OF THE CHANGES

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## PRACTICAL ISSUES

- The need for companies and their directors and officers to understand the new regime.
- The need for new procedures, documentation and software.
- Awaiting the new regulations and understanding how they work.
- Awaiting the new SSM software and understanding how they work.
- Others.



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# Q&A

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These slides and the matters discussed in connection with it are general in nature and do not constitute the provision of any legal or professional advice or the creation of any solicitor-client relationship. The information is merely a generic overview of some of the changes introduced by the Bill and it does not purport to be comprehensive or exhaustive. If you require assistance in connection with a particular matter, you should seek appropriate legal or professional advice from a qualified professional.



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