

CHAPTER III

Legal Environment

Introduction

It is of interest to note that the Companies Act, 1965 which is based on the Companies Ordinances of United Kingdom and Australia is enforced since April, 1966.

The trust companies are registered in accordance with the Companies Ordinance, 1948. In 1957, there was no specialised Ordinance to control the activities of these trust companies. In United States the specialised act, Investment Company Act of 1940 is directed towards the trust companies. Below is a summary of the more important clauses of the ^{Investment} Companies Act.

(1) Management - The law ensures independent and honest management which may prevent excessive commissions and self-aggrandizement by underwriters, etc. The Security Exchange Commission which administers this Act can take legal action against any person for misconduct such as embezzlement. A bank will act as custodian for the portfolio of the trust company.

(2) Investment policies - Trust companies are to file with the Security Exchange Commission a statement outlining the investment policies in clear and specific writing and such policies may not be changed without the consent of the shareholders.

(3) Shareholders participation - At least 2/3 of the

directors must be elected by the shareholders and 40 of the directors may not be officers of the companies. The shareholders will ratify the selections of accountants. Should there be any default in payment of dividends the preferred shareholders will have a right to vote.

(4) Capital - \$100,000 is the minimum capital required. With regard to investment trusts the capital structure is limited. At least 50 per cent of which must be common shares at the time of issuance. They can only issue one class of preferred stock and one class of bonds. unit trusts may issue only common shares.

(5) Distribution - All sales of securities must be in compliance with the Securities Act of 1933.

Doubtless to say, trust companies must provide the investors with complete and accurate financial reports. The investors, if they want to, can always find out what he is buying and can find out the past performance of the company, the present portfolio holdings and from these can use to determine other things such as forecasting future income.

In Australia, the trust companies operate under the Australian Companies Ordinance, Victoria, 6839/1961.

Since the drafting up of the Malaysian Companies Act of 1965 is based on the Companies Ordinances of United Kingdom and Australia, it is not surprising that the Companies Act is quite identical to the two.

The trust companies are governed by the Companies Ordinance, 1948. In compliance with the Ordinance, the trust companies must follow the Memorandum and Articles of Association. Now that the Companies Act has replaced the Companies Ordinance, new companies will be registered according to the Companies Act.¹

Legal Environment - Unit Trust

The unit trust operates within the confinement of the Companies Ordinance, now the Companies Act. Whereas the unit trust in Australia is governed partially by the Trustee Law and Division V of the Companies Act, the unit trust in Malaysia is not partially governed by any other ordinance, not even the Trustee Investment Act, 36/1965.

In fact, it is wholly governed by the Companies Act, Division V of Part IV.

Here the term company is taken to mean a public company and must follow the Seventh Schedule of the Companies Act which means that the company must furnish certain types of information as specified by the Schedule in Appendix I.

There is no legal restriction on the financial position of the company that may act as trustee but the trustee is normally of good financial standing. Section 87(1) of the

1. It would be noticed that the trust companies are not governed by the Trust Companies Ordinance 33/1949. This Trust Companies Ordinance is meant to govern the activities of the trustee companies.

Companies Act reads as follows:

"The Minister on the recommendation of the Bank Negara Malaysia, subject to such terms and conditions as he thinks fit, grant his approval to a company acting as trustee or representative for the purpose of a deed."

In pursuance of the provisions of this clause, it is usual for the trustee to be a trustee company or an insurance company of high standing or the nominee of a bank. The high financial standing of the trustee will ensure the safety of the investment for the investors.

A unit trust is brought into existence by the execution of a Trust Deed. The investment trust operates under the Memorandum and Articles of Association which lays down the objects of the company and the rules under which it shall operate. The Trust Deed for a unit trust is very similar to a Memorandum and Articles of Association and incorporates provisions for its operations much along the same line as would be found in the Memorandum and Articles of Association of an investment trust. The Trust Deed sets out the objects of the trust and it names the manager as well as the trustee. The manager and trustee between them discharge the duties which a trustee under a normal trust instrument would perform and the Deed clearly defines the respective duties of both the trustee and the manager. The manager, in addition to being charged with the responsibility of managing the investments, is also required to raise the necessary funds for the

trust. The trustee holds the investments, receives the income from these investments and distributes such income periodically to the unit-holders by means of a cheque from the trustee. This ensures that the investments of the trust are safe-guarded by an independent trustee on behalf of the investing public and that the income from these investments is similarly protected.

With a view to protecting the public investors in the unit trusts, certain clauses in the Companies Act have been enacted to control their operations and the organisations managing such trusts. The ultimate effect is to give the investors maximum protection for their investments in the unit trust. The important requirements with which the trustee and the managers of the unit trusts are by law required to comply, are as follows:

(i) The management company must be a public company and thus it must make available its Balance Sheet and Accounts.

(ii) The units in a trust can only be offered to the public if there is a Deed, the approval of which by the Registrar of Companies is subject to Section 86(1) which reads as follows:

"Where a deed makes provisions for the appointment of a company as trustee for or representative of the holders of interests issued or proposed to be issued by a company the Registrar may grant his approval to the deed".

provided the deed complies with the requirements of Division V of Part IV and

"makes provision for such other matters and things as are required by or under the regulations to be included in the deed." 86(2).

The Trustee or representative named in the Deed in Section 86 must be approved by the Minister on the recommendation of Bank Negara Malaysia.

The Deed contains covenants which:

- (a) binds the management company to use its best endeavours to carry on and conduct its business in a proper and efficient manner.
- (b) binds the management not to sell any interest to which the deed relates other than at a price calculated in accordance with the provisions of the deed and that the management will at the request of the unit holder purchase the interest at the calculated price in accordance with the provision of the deed.
- (c) requires the trustee to exercise all due diligence and vigilance in carrying out its functions and duties in watching the rights and interest of the unit holders, that it will keep proper books of accounts which shall be audited at the end of the financial year and shall send by post a copy of these accounts to each unit holder once a year.

There are also other covenants required from the trustee and manager which prohibit the management company or the trustee from lending monies of the trust, and also that neither the management company nor the trustee may exercise a vote in respect of any shares held on behalf of the unit holders in so far as that vote would extend to voting at a meeting in regard to an election of the directors, except under conditions which the Companies Act renders impossible of performance. Therefore, the trustee is disenfranchised

in such an instance. Also a prospectus must be lodged with the Registrar before inviting the public to subscribe for the purchase of any interest. Such prospectuses must comply with all the rules of law to the issue of prospectuses and must contain certain information and reports as required by the Seventh Schedule of the Companies Act.

Legal Environment - Investment Trust

The regulations governing the policies and practices of an investment trust is the Companies Act. The Memorandum and Articles of Association are drawn up in conformity with the Companies Ordinance of 1948 now replaced by the Companies Act.

The investment trust is managed by a board of directors or trustee-managers. There are certain limitations on the freedom of action but the "trustees" are nevertheless vested with wide discretionary powers. Upon the specific restrictions imposed by the Articles (and Memorandum) of Association, the directors may among other things, issue shares of stocks. The directors may purchase and sell securities and other investments and act as transfer agents for the registration of the company's securities. They appoint and fix the salaries of the officers and clerks. They may institute, defend, compromise or settle any legal action, on behalf of the company. The negotiation of the company's interests with those of other companies is done by the directors.

These are some of the discretionary powers which the directors possess. However, the directors are subject to Section 143-153 of the Companies Ordinance.

Conclusion

It may be said that when the Companies Act comes into force, it would "provide the investing public with more protection through a better legal framework for the operation of the companies."²

2. Bank Negara, Annual Report, 1965, p.45.