



TAY & HELEN WONG
LAW PRACTICE • AMALAN GUAMAN

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CHARGOR, WATCH OUT!

Chargor who waits till the last moment to reach settlement with the chargee in order to postpone the scheduled auction faces the risk of the application for postponement rejected by the authority resulting in the auction being carried out and the charged property sold off !

That sums up the lesson to be learnt following the decision in *Koperasi Pembangunan Kampung Tradisional (Pekatra) Tasek Bhd v Pentadbir Tanah, Daerah Kubang Pasu, Kedah darul Aman & Anor; Shahezan Wali Mohamed (Intervener)*ⁱ. In that case, the applicant /chargor charged a piece of property to the 2nd respondent as security for a banking facility. Defaults took place and on the application by the 2nd respondent under the National Land Code (NLC), the 1st respondent (Land Administrator) made an order for sale of the propertyⁱⁱ. The auction was fixed on 28.7.2003. Pursuant to discussion held on 22.7.2003, the 2nd respondent issued a letter on 23.7.2003 to state its agreement to adjourn the scheduled auction on the condition that an amount of RM200,000 was to be paid by 25.7.2003 and the balance by monthly instalments of RM100,000 each. The amount of RM200,000 was indeed paid on 25.7.2003.

The 2nd respondent however only orally applied to the 1st respondent on the morning of 28.7.2003 to postpone the scheduled auction on the ground that the applicant had made payments to the 2nd respondent. The 1st respondent rejected the application. The auction proceeded and the intervener successfully bid for the property. The applicant then filed the suit to nullify the auction sale and invalidate any registration made on the land title consequent to the sale on the ground that the 1st respondent had erroneously exercised his discretion in rejecting the 2nd respondent's application for postponement of the auction and in proceeding with the auction since both chargor and chargee had reached an agreement to postpone the said auction and this was notified to the 1st respondent. Reliance was placed on S.264(3) of NLCⁱⁱⁱ.

The learned Judicial Commissioner dismissed the applicant's suit. In his view, the effect of S.264(3) of NLC had been considerably watered down by the new provision in S.264A which came into force in 2002. Under S.264A, any application for postponement of an order for sale (auction) must be submitted to the land administrator not less than seven days before the date of the sale and must be made by the chargee with the concurrence of the chargor in the prescribed form. In the instant case, no such formal application was made. The oral application was only made in the morning of the auction date. Thus, the court held that the 1st respondent had correctly exercised his discretion as the applicant had not complied with the provisions in S.264A of NLC. The auction sale was valid and the intervener's interest on the property is indefeasible.

The consequence is the chargor lost its property, although it had managed to reach an agreement with the chargee to postpone the auction. It is not clear whether the chargor has taken or will be taking any action against the chargee for breach of agreement as in the case of *Wong Yuen Hock v Ban Hin Lee Bank Berhad*^{iv}. The chances of the chargor succeeding in such action depend upon the wordings of the letter issued by the 2nd respondent on 23.7.2003. It is however clear that one must not take the land administrator for granted or assume that as long as both parties to the charge, ie. chargor and chargee, reach a settlement, the land administrator will agree to the request or application made to postpone the auction. It must not be forgotten that the land administrator is guided by statutory provisions and is not at all subservient to any party's act. It is therefore advisable to comply with statutory provisions in taking any action or carrying out any act.

ⁱ [2007] 3 CLJ 725

ⁱⁱ Presumably under S.263 of the National Land Code pursuant to an enquiry held.

ⁱⁱⁱ S.264(3) NLC reads: "The Land Administrator may, if he thinks it expedient to do so, from time to time postpone any sale ordered under S.263."

^{iv} [1999] MLJU 236; [1999] 1 LNS 313.

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CONTRACT

AGENT LIABLE FOR CONTRACTS ENTERED ON BEHALF OF PRINCIPAL

Ordinarily, an agent is not personally bound by or liable for a contract entered into by him on behalf of his principal. However, an agent will be found personally liable if the contract is made by the agent for the sale of goods for a merchant who is resident abroad.ⁱ The presumption of personal liability arises when the elements in the proviso (a) of Section 183 of the Contracts Act 1950 are fulfilled.

This point was well illustrated in the recent case of *George Wong Sui Cheng v Amcan Sdn Bhd*ⁱⁱ in which the Court of Appeal held that a managing director (the Appellant) of a company based in Brunei was personally liable for the contract entered into by him on behalf of the company with a local company. The Appellant, the managing director of Pembinaan Menjaya Sdn Bhd [a company registered in Brunei], ordered goods from the Respondent with the express instruction to deliver the goods to Unieast Building & Civil Engineering Sdn Bhd in Brunei (Unieast). The Respondent duly delivered the goods but was not paid, hence the suit against the Appellant. The Appellant attempted to strike out the Respondent's claim by relying on the fact that he was not an agent of Pembinaan Menjaya and that the goods were actually ordered by Unieast.

The issues before the Court of Appeal were:-

- (i) whether a managing director of a company could be deemed as an agent of the company; and
- (ii) whether Pembinaan Menjaya and Unieast fall within the exception of "merchant resident abroad".

The Appellant's contention was that as the managing director of the Pembinaan Menjaya, he was not "employed" by the company but rather could be removed or appointed by way of ordinary resolution. The

contention was rejected by the court because as a managing director, he was regarded *ipso facto*ⁱⁱⁱ as an agent of the company.

It was further argued that Pembinaan Menjaya and Unieast were at all material times building contractors and as such could not be considered as "merchants" within the meaning of s.183 (a) of the Contracts Act 1950. The court did not agree with the argument and held that both Pembinaan Menjaya and Unieast fall within the meaning of "merchants". The court therefore dismissed the appeal by the Appellant to strike out the Respondent's statement of claim.

This case serves as a good reminder for a managing director or, in our view, any director or person who can be regarded as an agent of a foreign registered company (the said foreign principal) in going about their daily jobs. It will be in the interests of these people to bear in mind that they will be, *prima facie*, personally liable for breach of a sale and purchase agreement made by them as agent of the said foreign principal. It is not enough to prove that the sale and purchase agreement was in fact the contract of the said foreign principal and the agent has merely acted as agent because such proof would merely trigger the operation of the statutory presumption in the proviso (a) of s 183 of the Contracts Act 1950. The only way to get rid of such personal liability would be, as laid down in the earlier Supreme Court case of *Medicon Plastic Industries Sdn Bhd v Syarikat Cosa Sdn Bhd*^{iv}, either by express words or impliedly by a necessary inference from documents, evidence and surrounding circumstances showing that the agent has in fact contracted out of such statutory presumption.

ⁱ S. 183 (a) Contracts Act 1950

ⁱⁱ [2007] 3 AMR 184

ⁱⁱⁱ in itself or by the fact

^{iv} [1993] 2 MLJ 416

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EMPLOYMENT LAW

DIGEST

1. Fixed term contract unaffected by provisions akin to permanent employment

The Industrial Court in the case of *Captain Robert H Haywood v Malaysian Airlines System Bhd* laid down the above principle. In that case, it was the contention of the claimant that due to the presence of provisions on annual increments, bonuses and allowances in his contract of employment, it was not a genuine fixed term contract but a contract which was of a permanent nature dressed up as a fixed term contract. It was also a fact that his contract had been renewed several times during the various durations of the fixed term contracts. The court however held that the same benefits could still be granted to and enjoyed by employees in fixed term contracts without affecting the character and nature of such contracts. It was also the company's normal practice to employ expatriates on a fixed term contract basis.

Essentially, whether a contract is a genuine fixed term, contract or not depends on the facts of each case. If it were a genuine fixed term contract, the Industrial Court would have rightly disposed of the matter without having to go into the further (and irrelevant) question of whether there was a dismissal without just cause or excuse.

2. Running errands for the company president's wife

An employee is not duty bound to attend to the needs of the company president's wife or family in the absence of clear stipulations in his contract of employment. The general descriptions like "other functions", "to perform as and when required by the company" would not entitle the president to instruct and expect the employee to perform errands for the former's wife or family. The fact that the employee obliged such performance of tasks in the past does not mean that it has become his bounden duty to continue performing such functions forever. Such previous acts could not be read back retrospectively into the employee's contract of employment and be converted into implied contractual obligations when they had not been

there in the first place. The court thus held that the claimant in *Airod Sdn Bhd v Doraiyah Munusamy*ⁱⁱ was not contractually bound to attend to the personal needs of the president, his wife or family.

3. Probationer to be given sufficient opportunities and guidance

The Industrial Court decision in *Chan Weng Sze v OSK Securities Berhad*ⁱⁱⁱ is of concern to employers. In that case, the claimant (holding a Diploma in Computer Studies) was employed as an Analyst Programmer and put on probation but she was not confirmed at the end of the six-month probation period. In the appraisal conducted a few days before the termination of her services, the claimant was given an average grading. The company's main grouse against her was that she made numerous errors in her work and failed to complete her assignments on time, without close supervision from a superior.



The Industrial Court however held that there was no evidence that the claimant had done the kind of work that she was appointed to do and it was the first time that she had been exposed to it. There was no evidence that the immediate head of the claimant had given her a fair and reasonable opportunity to prove herself or that he had told the claimant how to overcome her shortcomings.

The claimant being a probationer and inexperienced certainly could not be expected not to make mistakes in the first six months of her new job. The burden was on the company to show that the claimant had been given

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support and a reasonable amount of time to improve. Her average rating appraisal meant that she had met with the job requirement and the company could not contend that she was a below average performer. If the company had expected a high standard of its probationary employees, then it should have made the same known to the employees at the outset and provided opportunities for them to achieve such high standards.

4. Sexual misconduct unaffected by outcome of criminal cases

Pursuant to two police reports lodged, the claimant was charged in the Magistrate's Court for allegedly outraging the modesty of two colleagues. The claimant was subsequently given a discharge not amounting to an acquittal (DNAA). A domestic inquiry was held and he was found guilty of the two charges of sexual misconduct and was dismissed from the company. Does the DNAA in the Magistrate Court have any bearing on the case of wrongful dismissal under S.20(3) of the Industrial Relations Act 1967? This was one of the issues posed in *Colgate-Palmolive (M) Sdn Bhd v Yap Shyan Meng*^{iv}. It was held that a DNAA in a criminal case did not mean a verdict of not guilty. DNAA was normally

ordered when the prosecution was either unable to produce the necessary witnesses or adduce sufficient evidence to secure a conviction, but it did not estop the prosecution from charging the claimant again for the same offence at a later date should the prosecution be able to secure the attendance of witnesses in court or find sufficient evidence. Thus, the criminal proceedings should have no bearing on the instant case and the Industrial Court could decide the case independently of the criminal case. On the evidence, the company had discharged its burden on a balance of probabilities that the claimant's acts tantamount to sexual harassment at the work place, which was a serious misconduct and punishable by dismissal.

ⁱ [2007] 1 ILR 577
ⁱⁱ [2007] 1 ILR 644
ⁱⁱⁱ [2007] 2 ILR 121
^{iv} [2007] 2 ILR 313

LAND LAW / BANKING

CHARGE RENDERED DEFEASIBLE BY SOLICITOR'S FRAUD

The Court of Appeal decision in *Abu Bakar bin Ismail & Anor v Ismail bin Husin*ⁱ serves as a reminder to banks to exercise prudence in appointing solicitors firm to act for it in any loan transaction.

In that case, the registered proprietors of three lots of land (subject property) entered into a sale and purchase agreement with the 1st defendant. The agreement was prepared by the 2nd defendant who was a partner in the 3rd defendant firm of solicitors. After initial payment of less than 3% of the total purchase price, the registered proprietors deposited the

title deeds together with a signed memorandum of transfer in blank with the 3rd defendant firm. It was later discovered that the subject property was fraudulently charged to the 4th defendant bank to secure a loan granted to the 5th defendant, the instrument of charge being a forged document. A sum of RM10 million had been disbursed to the 5th defendant whose manager absconded with the money. The registered proprietors therefore commenced legal proceedings against all the five defendants to recover the subject property.

The High Court made a finding that the 1st and 2nd defendants were parties to the fraud but absolved the 4th defendant lender. The 2nd defendant was in fact held to be the central figure in planning the whole scheme with the 1st defendant and the representatives of the 5th defendant. It was also held that the 3rd defendant firm was retained by the 4th defendant lender to prepare the necessary loan documentation. The 2nd and 3rd defendants thus were in law regarded as the agents of the 4th defendant lender.

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Although the High Court found that the 4th defendant lender was neither a party nor privy to the fraud, the Court of Appeal by majority held that the 4th defendant's charge was defeasible due to the fraud perpetrated by the 2nd defendant who was the agent of the 4th defendant. Section 340(2)(a) of the National Land Code entitles the plaintiffs to defeat the title of the registered chargee (the 4th defendant lender) by showing that the registered chargee's agent was party or privy to the fraud. The findings that the 2nd and 3rd defendants were the agents of the 4th defendant lender and the 2nd defendant was a party to the fraud fit into this scenario.

The upshot was that the 4th defendant lender's charge was declared to be null and void. It was unfortunate that though the bank was itself faultless, its security was jeopardized due to the its solicitor's fraud in the transaction in question !!

In terms of legal principles, the Court of Appeal expressed doubts that the common law exception that notice of an agent is not to be imputed to the principal where there has been fraud on the part of the agent in the matter is applicable to the provision in the said Section 340(2)(a). The Court of Appeal construed the clear wordings of the said Section 340(2)(a) and set aside the bank's charge by virtue of its solicitors' involvement in the fraud although on the findings of evidence, the bank was not a party to the fraud at all.

ⁱ [2007] 3 AMR 257

PUBLIC UTILITIES / TORT / CONTRACT

CURBING POWERS OF PUBLIC UTILITY AUTHORITIES

Public utility authorities should exercise restraint and refrain from exercising their powers or act in a manner which is arbitrary, coercive and unlawful. This is basically the warning emanated from two recent High Court decisions involving Tenaga Nasional Berhad, the national supplier of electricity in Malaysia.

Firstly, whilst it may not be often for any one to dispute the amount billed in electricity bills, it does not mean that one must accept the estimated sum (as opposed to actual sum for actual amount of electricity consumed) stated in the bills without question. In *Kamalanathan Ponnambalan v. Tenaga Nasional Bhd*, the High Court held that the bill for electricity consumed by the plaintiff must be based on the actual meter reading as required by s 32 of the Electricity Supply Act 1990 (the Act). The acts of the defendant repeatedly

sending notices and seeking payment of an estimated sum and then having received no payment from the plaintiff, proceeding to disconnect the electricity supply were clearly in breach of the contract with the plaintiff and wrongful.



The notices of disconnection and the acts of disconnecting the electricity supply at the plaintiff's premises a number of times were defamatory. The court remarked that the proper course that the defendant ought to have adopted was for it to sue the plaintiff in court for the amount allegedly owed. The repeated

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acts of arbitrarily disconnecting the electricity supply despite the plaintiff's protests were therefore wilful and in wanton disregard of the statutory provisions and the court awarded exemplary damages.

Secondly, the public utility provider ought not to make use of statutory provisions which empower them to disconnect electricity supply for a purpose not provided for in the said provisions. In *Kejuruteraan Enweld Sdn Bhd v Tenaga Nasional Bhd*ⁱ, the High Court found that the reason for the disconnection of the electricity supply by the defendant was not because of any existing defect in any installation which could cause danger pursuant to s 49 of the Act.

The disconnection was to ease the other authorities (namely Jabatan Tanah and Galian and Dewan Bandaraya Kuala Lumpur) to destroy the plaintiff's premises on the land which had been acquired by the government. The plaintiff's claim for breach of contract between the plaintiff and defendant was thus allowed.

ⁱ [2007] 3 CLJ 83

ⁱⁱ [2007] 3 MLJ 89

approved payment of allowances and other benefits.

The plaintiff claimed that these losses were caused by breaches of the defendant-firm (auditor)'s contractual obligations and duty of care of the express and implied terms of the audit contract. Such breaches occurred in relation to the audits carried out for FY 1999, FY 2000 and FY 2001 on which financial statements the defendant had expressed an unqualified opinion. The plaintiff's case was that, *inter alia*, the defendant had failed to bring to the plaintiff's attention material weaknesses in the system of accounting and internal control that came to the defendant's notice. In one of the audits conducted, the defendant was unable to obtain the employment contract of R but sought confirmation, at R's suggestion, on R's remuneration package by securing the approval of the other director (C) through C's signature on the draft financial statements.

TORT / CONTRACT / COMPANIES

WHY DIDN'T AUDITORS FIND THE FRAUD?

Companies and organizations that are hit with employee's fraud, including embezzlement, asset misappropriation and financial statements manipulation are often surprised that the incident occurred. Even more surprising to executives and boards of directors is the fact that their auditors didn't find the fraud sooner, or didn't find it at all. After all, isn't that what auditors are supposed to do?

In the Singaporean case of *JSI Shipping (S) Pte Ltd ("JSI") v Teofoongwonglcloong*^j, the special audit report of the plaintiff had revealed that one of its directors (R) had misappropriated company funds totaling \$1.808m over the period covering FY 2001 and FY 2002. The misappropriations comprised personal expenses charged to director's benefits without board approval, unsubstantiated traveling expenses, doubtful charges, fictitious payments to a company controlled by R and issuance of cash cheques for spurious transactions. It was also discovered that for the period covering FY 1999 and FY 2000, there was overpayment of R's salary and non-



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The High Court of Singapore held that the duties of an auditor were governed by the contract of engagement in the light of sections 205 and 207 of the Companies Actⁱ. In fulfilling his duties under s 207, the auditor had to use reasonable skill, care and caution. What amounts to reasonable skill depended on the circumstances of each case. An auditor's role was to verify and not to detect. It was his duty to take care that errors were not made. To do so, an auditor needed to have an inquiring mind, not one suspicious of dishonesty but one suspecting that someone may have made a mistake somewhere. On the facts of the case, the defendant was entitled to rely on R's representation in seeking verification of R's remuneration package. The defendant did obtain C's signature on the director's report. The defendant was entitled to rely on the directors' statement in the absence of evidence of dishonesty or fraud. Moreover, the defendant was seeking to rely on the directors' statements to confirm only an aspect of the audit and not the entire audit.

However, another High Court judge arrived at a different decision in the case of *Gaelic Inns Pte Ltd v Patrick Lee PAC*ⁱⁱ. Here, the plaintiff company alleged that the defendant (auditor) had failed to detect cash misappropriations by the plaintiff's former group finance manager ("Denise") during the audit of the accounts for FY 2001, FY 2002 and FY 2003. It was the plaintiff's contention that the defendant acted in breach of the duty of care owed to the plaintiff as an auditor of the company. Had the defendants alerted the plaintiff of Denise's misdeeds, further misappropriations would have been averted.

Whilst the case of *JSI Shipping* was cited for the principle that generally, an auditor who adhered to the accounting standards to convey a true and fair view of the financial statements has a better chance of defending criticisms in the conduct of the audit as compared to an auditor who departs from them, the judge in *Gaelic Inns Pte Ltd* case departed from *JSI Shipping* case on one material aspect. *JSI Shipping* adopted the same test for auditors as that for doctors in *Bolam v Friern Hospital Management Committee*^{iv} namely, the court would be guided by accepted professional practice so that an auditor would commit no breach of duty if he had acted in accordance with a practice

accepted as proper by a body of skilled and responsible auditors. However, *Gaelic Inns Pte Ltd* held that it was ultimately the court that has to decide whether, on the facts and circumstances of the case, a *prima facie* case of breach of duty has occurred. It was for the province of the auditing profession itself to determine the legal duty of auditors or what reasonable skill and care required to be done, although what others did or what was usually done was relevant. If the auditing profession or most of them fail to adopt some step which despite their practice was reasonably required of them, such failure did not cease to be a breach of duty just because all or most of them did the same^v. In this respect, the judicial approach in *Gaelic Inns Pte Ltd* echoes the new approach laid down by the Malaysian Federal Court in a medical negligence case of *Foo Fio Na v Dr Soo Fook Mun & Anor*^{vi}. The courts would adjudicate on what was the appropriate standard of care. It is not to be determined by the practice followed or supported by a responsible body of opinion in the relevant profession or trade.

Whilst an auditor was not expected to be a detective, the duty to audit carried with it an incidental duty to warn the management of fraud or irregularities uncovered during the course of the audit. A breach of the duty would have occurred if, in the course of the audit, the auditors uncovered matters which reasonably required them to take further steps that would have uncovered or led them to uncovering the fraud and they omitted to take such further steps. On the facts of the case, the Court held that the defendant's negligence in failing to examine the irregularities and failing to inform the plaintiff's senior management of Denise's misappropriations was a breach of his duty of care owed to the plaintiff company.

Recently in Malaysia, the duties and functions of auditors hogged the limelight following irregularities detected in the Transmile Group Bhd's financial statements and records. Their actual losses for FY 2005 and 2006 were reportedly higher than the losses in the earlier audited reports. A special audit carried out uncovered substantial irregularities, including overstatement of revenue and transactions that were said to have been fabricated to transfer trade receivables to asset accounts. Whether the auditors could be held accountable for breach

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of duty expected of an auditor remains to be seen.

It is however comforting to note that efforts are being taken to beef up our laws to safeguard against the exploitation of accounting system and to enhance controls. The onus will soon fall on auditors of public-listed companies to 'blow whistle'. This is with regards to the proposed Companies (Amendment) Act 2007 where auditors of a public listed company will soon be obliged to report any fraud and dishonesty committed by any officer of a public-listed company. Under the proposed amendments which have yet to come into operation, auditors would not be liable to be sued or be subject to any crime or disciplinary proceedings for reports done in good faith. Further, once an auditor ceases his

service to the firm, he must provide a written explanation to the Registrar of Companies or Bursa Malaysia on his resignation^{vii}.

ⁱ [2007] 1 SLR 821

ⁱⁱ The relevant provision in Malaysian Companies Act 1965 is Section 174.

ⁱⁱⁱ [2007] 2 SLR 146

^{iv} See paragraph 69 in [2007] 1 SLR page 843.

^v See paragraph 11 in [2007] 2 SLR 152.

^{vi} [2007] 1 MLJ 593, please refer to our Law Update Issue 5/2006.

^{vii} See article on The Star 3 July 2007, StarBiz section page 1.

TORT / CONTRACT

NO LIABILITY FOR INDUCING BREACH OF VOIDABLE CONTRACT WITH ROONEY

Do you know that Wayne Rooney (yes, the Manchester United and England star striker) at the age of 15 years old had already entered into a representation agreement (the 2000 agreement) by which he appointed a sports management company (the plaintiff) to act as his agent and to carry out all the functions in respect of personal representation on his behalf as a professional footballer? In other words, Rooney employed the plaintiff to represent him exclusively in contract negotiations and transfers. At that time, Rooney was already with Everton Football Club that provided him with training and was registered with the Football Association Premier League on a scholarship agreement. Under the Football Association Rules, Rooney as a person not in full-time education was not able to sign a professional contract until he was 17.

The 2000 agreement lasted only for two years. Three days after its expiry on 11 December 2002, Rooney entered into another representation agreement with the 1st

defendant. 1½ months later, Rooney entered into a Football Association Premier League professional contract with Everton Football Club. The plaintiff subsequently sued the 1st defendant and a director of the 2nd defendant for unlawful interference with and/or the procuring of a breach of the 2000 agreement. It was a fact that the 1st defendant entered into agreements with Rooney in July and September 2002 although it was in dispute whether both the agreements were ever acted upon by the defendants.

This was the brief factual background of the case of *Proform Sports Management Ltd v Proactive Sports Management Ltd & Anor*¹, a decision of the High Court (Chancery Division) in United Kingdom. It must be highlighted that Rooney was still a minor when he entered into the 2000 agreement. In English law, the only contracts that are binding on a minor are contracts for necessities, contracts for the minor's benefit particularly contracts of apprenticeship, education and service. Other than these, a minor's contract is voidable at his option, ie. not binding on the minor but binding on the other party.

The defendants applied for summary judgment against the plaintiff on the ground that the plaintiff had no real prospect of succeeding on the claim and there was no other compelling reason to go for trial. The court concurred with the defendants that the plaintiff had no reasonable prospect of succeeding in establishing that the 2000

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agreement fell within the class of contracts analogous to contracts of necessities, contracts of employment, apprenticeship or education which were enforceable against a minor.

Rooney was already with a football club at the time of the 2000 agreement and the plaintiff did not undertake matters essential to the player's training or livelihood, nor did they enable Rooney to earn a living or advance his skills as a professional footballer. The 2000 agreement was therefore voidable. There

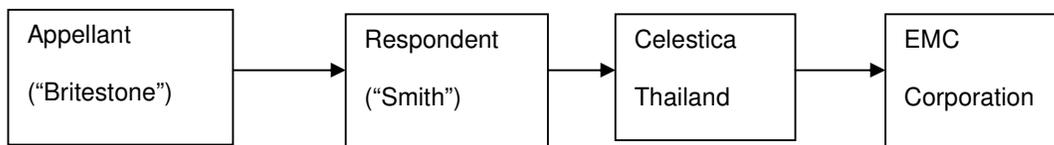
could be no liability for inducing or facilitating the breach of a voidable contract with a minor. The fact that the contract could be avoided should in principle be a defence to any claim for the tort of wrongful interference with, or wrongfully procuring a breach of, the contract. Thus, the defendants' application for summary judgment succeeded.

ⁱ [2007] 1 All ER 542.

COMMERCIAL TRANSACTIONS / DAMAGES

DAMAGES CLAIMABLE IN SUB-SALES

Despite the normal rule that sub-sales are not taken into account when computing damages arising directly and naturally from a breach of contract, the High Court of Singapore in *Smith & Associates Far East Ltd v Britestone Pte Ltd*^d decided otherwise.



A chain of events occurred as above when Smith purchased some electronic components from Britestone and re-sold them to CTL. After receiving the components, CTL installed them onto printed circuit boards for its customer EMC. It was subsequently discovered that the components supplied from Britestone to Smith were counterfeit goods. As a result, the components had to be removed and replaced with genuine products.

EMC claimed for damages against CTL who in turn held Smith responsible for that amount. It was later agreed that Smith would pay CTL the sum of USD300,000 in full and final settlement of CTL's claim against Smith ("settlement sum"). Smith then commenced proceedings against Britestone for the settlement sum paid to CTL including a sum of profit or, alternatively, damages to be assessed.

Both parties agreed to a consent judgment, under which Britestone accepted liability for breach of contract for Smith's loss of profits. However, the Assistant Registrar ruled that Smith was also entitled to be paid the settlement sum. On appeal, Britestone's questioned its liability to pay Smith the settlement sum that Smith paid to CTL.

The High Court judge opined that the loss suffered by Smith with respect to the settlement sum concerned a sub-sale to CTL and as such, not taken into account when computing damages arising from a breach of contract. However, section 54 of the *Sales of Goods Act*^f provides as follows:-

*"Nothing in this act affects the right of the buyer or the seller to recover interest or special damages in any case where by law interest or special damages may be recoverable..."*ⁱⁱⁱ

IMPORTANT

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The learned judge explained that section 54 left room for the application of the second branch of the rule in *Hadley v Baxendale*^{iv} :-

"[I]f the special circumstances under which the contract was actually made were communicated by the plaintiffs to the defendants, and thus known to both parties, the damages resulting from the breach of such a contract, which they would reasonably contemplated, would be the amount of injury which would ordinarily follow from a breach of contract under these special circumstances so known and communicated."

Smith and Bristestone had traded with each other for a long time and Bristestone was aware that when Smith ordered the components, they were for its customers. Although there was a chain of contracts involved, this did not affect Smith's claim. There were no material differences in relation to the warranty complained of in any of the contracts in the chain, and there was nothing in the chain of contracts that affected the original warranty given by Bristestone to Smith, which was broken because the components that had been supplied were counterfeit goods.

The damages due from Smith to CTL, which flowed from Bristestone's breach of warranty, would reasonably be supposed to have been in the contemplation of both Smith and Bristestone when they made the contract, and were the probable result of the breach in question. The Bristestone's contentions that it was not bound to pay to Smith the entire settlement sum on the grounds that Bristestone was not involved in the negotiations between Smith and CTL, that the settlement sum was unreasonable as Smith had not properly verified the claims of CTL and EMC and that Smith's general counsel lacked the technical knowledge to effectively conduct negotiations with CTL were rejected. The learned judge instead regarded the length of negotiations lasting nine months and the exclusion of CTL's own costs in purging the printed circuit boards which left only EMC's costs to be claimed from Smith as showing the settlement sum was reasonably arrived at, particularly in the absence of any evidence offered by Bristestone as to what was the reasonable cost of purging the counterfeit goods from the printed circuit boards. On this reasoning, Bristestone's appeal was dismissed.

ⁱ [2007] 1 SLR 958

ⁱⁱ Cap 393, 1999 Rev Ed

ⁱⁱⁱ The Malaysian equivalent is section 61 of the Sale of Goods Act .

^{iv} (1854) 9 Exch 341; 156 ER 145

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