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# Legal TAPS

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## **Five questions to ask before a company undertakes an IPO in Malaysia**

Wong Mei Ying  
Lim Wan Yi

## **The Aftershocks in the Housing Development Industry In Malaysia - The Ang Ming Lee Effect!**

Leonard Yeoh  
Caleb Sio

## **The Effects of Malaysia's Minimum Wages Order 2022**

Leonard Yeoh  
Khor Wei Wen

## **Advisory on re-registration of franchises under the Malaysian Franchise Act 1998**

Lee Lin Li  
Chong Kah Yee

## CONTENT

**02** Five questions to ask before a company undertakes an IPO in Malaysia

by Wong Mei Ying & Lim Wan Yi



**08** The Aftershocks in the Housing Development Industry In Malaysia - The Ang Ming Lee Effect!

by Leonard Yeoh & Caleb Sio



**10** The Effects of Malaysia's Minimum Wages Order 2022

by Leonard Yeoh & Khor Wei Wen



**14** Advisory on re-registration of franchises under the Malaysian Franchise Act 1998

by Lee Lin Li & Chong Kah Yee



## Editorial Committee

- Leonard Yeoh
- Lee Lin Li
- Lim Jing Xian

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# 5 questions to ask before a company undertakes an IPO in Malaysia

## 1. What should promoters consider when deciding whether to list their companies?

Promoters should weigh the benefits and drawbacks before deciding whether to undertake an initial public offering (“**IPO**”) and listing exercise for their companies. The key considerations include:

- A public listed company (“**PLC**”) has greater access to capital compared to a private company as a PLC may raise funds from the public.
- A company may incur substantial cost to undertake an IPO exercise and comply with listing obligations and corporate governance practices once the company is listed.
- Certain information about a PLC is required to be announced to the public under the Listing Requirements, which may attract media coverage. Such publicity may affect the PLC’s business and reputation positively or negatively. For example, a PLC is required to announce the acquisition or loss of a contract, franchise or distributorship rights and material litigation under the Listing Requirements.<sup>1</sup>

<sup>1</sup> Paragraph 9.04 of the Main Market Listing Requirements and Rule 9.04 of the ACE Listing Requirements

- A PLC is subject to stricter regulatory regime under listing rules compared to a private company which in turn, increases the credibility and enhances the corporate governance of the PLC.
- Promoters, directors and officers of a PLC, being the “insiders” possessing information not generally available to the public, are subject to insider trading restrictions under the Capital Markets and Services Act 2007. They should consider whether they are accustomed to being subject to restrictions on dealing with their shares. Failure to comply with insider trading provisions is an offence punishable by up to ten years’ imprisonment and a fine not less than RM1 million.<sup>2</sup>
- The public shareholding requirement under the Listing Requirements requires certain percentage of shares in a PLC to be held by the public, which dilutes the promoters’ control over the companies they founded. Shareholders may question directors on how a PLC is managed. Shareholders may vote and decide on matters, which are subject to shareholders’ approval under the Listing Requirements and Companies Act 2016, such as remuneration of directors and certain transactions undertaken by the PLC.
- A PLC may become a target for a takeover by a competitor.
- The success of an IPO exercise depends on the industry outlook and market condition, which should be taken into account in deciding the time for companies to go public.

## 2. Which market should a company choose for listing in Malaysia?

The following are three markets available for

listing in Malaysia, which cater for companies with different profiles and stages of growth.

### Main Market

- Prime market for established companies that have met the standards in relation to quality, size and operations
- Accessible to public

### ACE (Access, Certainty, Efficiency) Market

- Sponsor-driven market for fast-growing companies
- Accessible to public

### LEAP (Leading Entrepreneur Accelerator Platform) Market

- Adviser-driven market for small and medium enterprises
- Only accessible to sophisticated investors, namely accredited investors, high net-worth entities and high net-worth individuals as specified in Part 1 of Schedule 6 or Part 1 of Schedule 7 under the Capital Markets and Services Act 2007.

## 3. What are the preparations for an IPO?

### Preparation to meet the listing criteria

Depending on the market which a company is seeking to list on, certain listing criteria take time to comply with. For examples:

- A Main Market applicant which seeks listing under the profit test must have an uninterrupted profit of three to five full financial years based on audited financial statements prior to submission to the Securities Commission Malaysia (“SC”), with an aggregate after-tax profit of at least RM20 million and an after-tax

<sup>2</sup> Section 188(4), Capital Markets and Services Act 2007

profit of at least RM6 million for the most recent financial year. The applicant or the corporation within the group which is the largest single contributor to the after-tax profits, must have been operating in the same core business over at least the profit track record prior to submission to the SC.

For a Main Market applicant seeking listing under the market capitalisation test, the applicant's ordinary shares must have a total market capitalisation of at least RM500 million upon listing. The applicant or the corporation within the group representing the core business must have been incorporated and generated operating revenue for at least one full financial year prior to submission to the SC.

A Main Market applicant seeking to list under the infrastructure project corporation test must have the right to build and operate an infrastructure project in or outside Malaysia, with project costs of not less than RM500 million and the concession or licence for the infrastructure project must have been awarded by a government or a state agency, in or outside Malaysia, with a remaining concession or licence period of at least fifteen years from the date of submission to the SC.<sup>3</sup>

- A Main Market applicant must have had continuity of substantially the same management at the level of executive directors and senior management for at least three full financial years prior to submission to the SC or for Main Market applicant seeking to list under the market capitalisation test or the infrastructure project corporation test, since

the commencement of its operations, if less than three full financial years.<sup>4</sup> A Main Market applicant must appoint a chief financial officer, finance director, or the individual holding an equivalent position in relation to the applicant's



business, at least six months prior to the submission to SC.<sup>5</sup>

- While there is no minimum operating track record or profit requirement for listing on the ACE Market, an ACE Market applicant is similarly required to have continuity of substantially the

<sup>3</sup> Paragraph 5.02, Part II of the Equity Guidelines

<sup>4</sup> Paragraphs 5.05 and 5.06, Part II of Equity Guidelines

<sup>5</sup> Paragraph 5.06A, Part II of Equity Guidelines

same management at the level of executive directors and senior management for three full financial years before submitting its listing

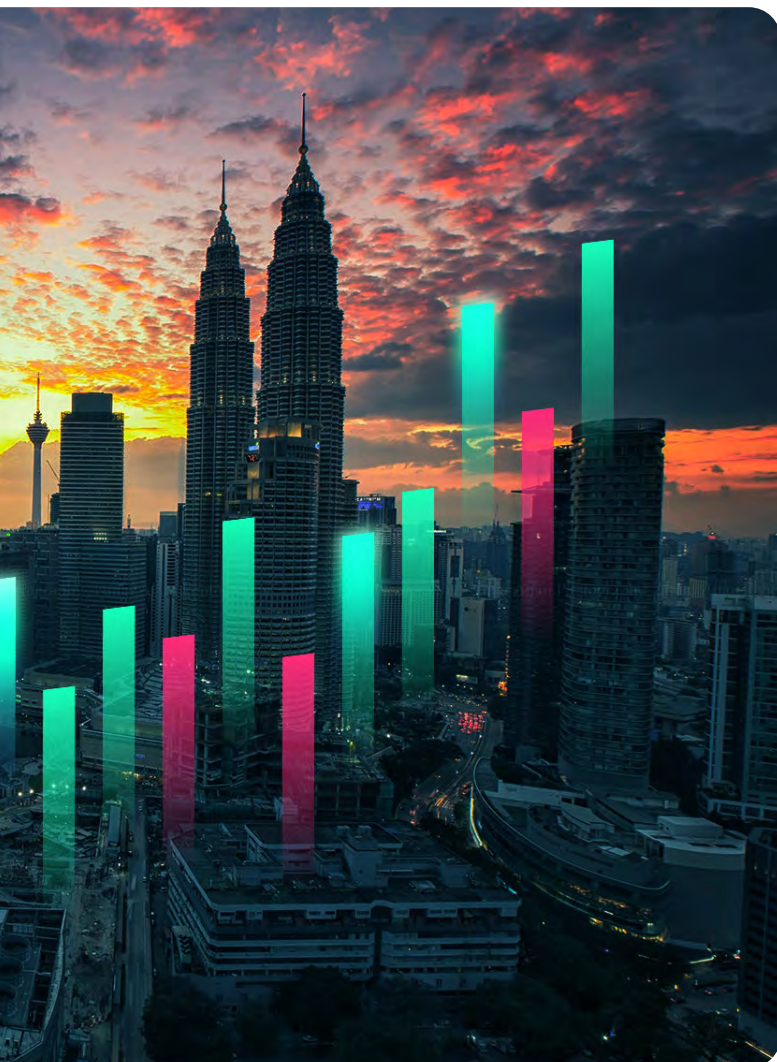


Photo by Zukiman Mohamad from Pexels

application to Bursa Malaysia Securities Berhad or since its incorporation (if less than three full financial years).<sup>6</sup>

### Pre-IPO Restructuring

An applicant may carry out a pre-IPO restructuring exercise prior to it being listed for the following purposes:

- to streamline the business of the listing group which show an identifiable core business of the group and enhance the listing group's valuations to attract investors.
- to exclude companies from the listing group where the business of such companies is not viable or involves non-compliance issues.
- to resolve any conflict-of-interest issues arising from the businesses undertaken by the promoters, substantial shareholders and directors.

### Due Diligence Exercises

An adequate due diligence process also provides a defence for any allegation of false or misleading statement or omission from any prospectus or documents submitted to the SC.<sup>7</sup>

To facilitate the due diligence process, the management of the listing group should establish an effective team to manage the due diligence exercise including responding to requests for information from IPO advisers. The following steps may be taken:

- Proper record should be kept in respect of the documents of the listing group, particularly those in the last three financial years prior to listing. Certain matters such as related party transactions ("RPT"), material contracts and financial information for the said period must be disclosed in the prospectus.<sup>8</sup> It is prudent for the company to keep documents such as price comparisons and quotations obtained from various suppliers or service providers to substantiate that the RPTs were undertaken on arms-length basis.

<sup>6</sup> Rule 3.06 of the ACE Market Listing Requirements

<sup>7</sup> Sections 215 and 250, Capital Markets and Services Act 2007

<sup>8</sup> Paragraph 5.04, Chapter 7 and Chapter 9, Part II, Division 1 of the Prospectus Guidelines

- As various IPO advisers may request for the same documents for their due diligence exercise, having a virtual data room where advisers are granted access to due diligence documents would facilitate the due diligence process. The management of the listing group should keep a list of people who have access to the virtual data room and keep the access secured at all times to ensure confidentiality.

- Where information is provided in a virtual data room, the documents should be properly indexed, labelled and organised to facilitate the review process.

**Determination of Pre-IPO share price**

The applicant must ensure that the exercise price of warrants and options, and the conversion price of convertible securities that are issued prior to or as part of the listing scheme must not be lower than the price of the ordinary shares offered to the general public under the IPO.<sup>9</sup>

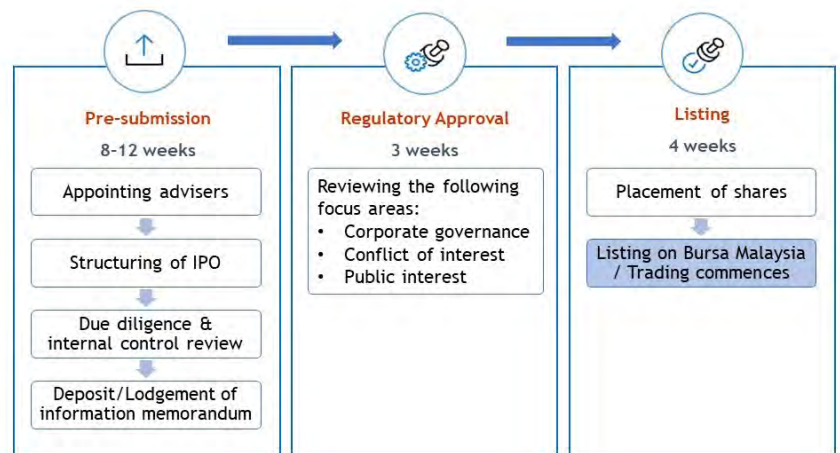
**4. What is the IPO and listing process?**

The IPO and listing process is depicted in the following diagram on Bursa Malaysia’s website:

**Listing Process for Main Market & ACE Market**



**Listing Process for LEAP Market**



Source: [https://www.bursamalaysia.com/listing/get\\_listed/listing\\_process](https://www.bursamalaysia.com/listing/get_listed/listing_process)

<sup>9</sup> Paragraph 5.13, Part II of Equity Guidelines and Rule 3.12(2) of ACE Market Listing Requirements

## 5. What makes a successful IPO and listing?

- The company should have an effective IPO team comprising its senior management and professional advisers. The senior management is responsible for providing information in respect of the listing group and to facilitate the professional advisers in their respective parts of the IPO. The professional advisers include principal adviser/sponsor, solicitors, financial advisers, independent market researcher, reporting accountants and auditors should have the relevant industry knowledge and experience of listing in Malaysia.
- The company should be able to attract investors through its business proposition and position in the market, as well as other non-financial metrics such as brand values, corporate strategies and environmental, social and governance (ESG) efforts.
- The company should make early preparation to ensure that it meets the criteria for listing, engage advisers to carry out assessment of its readiness for listing and have sufficient time to resolve any non-compliance in order to meet the timeline for listing, which should coincide with favourable market outlook.
- A PLC is required to appoint independent directors. As it takes time to assess suitability of director candidates, the process of assessing candidates should start early.
- There should be a realistic timeline for the IPO and listing exercise to ensure the company makes its initial public offering when the market condition is favourable.



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# The Aftershocks in the Housing Development Industry In Malaysia

## The Ang Ming Lee Effect!

In November 2019, the Federal Court's decision in *Ang Ming Lee & Ors v Menteri Kesejahteraan Bandar, Perumahan dan Kerajaan Tempatan & Anor* and other appeals (**AML**) upended the housing development industry. Overnight, housing developers were potentially liable for monumental Liquidated Ascertained Damages (LAD) claims. The Federal Court held that the Controller of Housing (**Controller**)'s power under Regulation 11(3) of the Housing Development Regulations 1989 (**HDR**) was ultra vires of the Housing Development Act 1966 (**HDA**).

Subsequently, in *UE E&C Sanjia (M) Sdn Bhd v Lee Jeng Yuh & Anor* and another appeal, the Court of Appeal further expounded on the principles of AML. The developer attempted to distinguish AML on the fact that the extension of time to deliver vacant possession was obtained before the sale and purchase agreements (**SPA**) were executed.

The Court of Appeal dismissed the developer's argument and held that whether the approval for the extension of time was obtained before the SPAs were executed was irrelevant as the Controller has no power to waive and modify the terms of the SPA in the first place. The SPA was thus void for illegality and parties were entitled to be restored back to the position as if the SPAs were not entered into. This case had been affirmed in the Federal Court after the application for leave to appeal was dismissed.

Are housing developers now left with no alternative but to bite the bullet? That might not be the case as recent Court of Appeal cases appear to provide some leeway.

### Only the Minister allowed to grant extension

In *BluDream City Development Sdn Bhd v Kong Thye & 184 Ors* and 5 other appeals (**Bludream**), the purchasers relied on AML and filed a judicial review against the decision of the Minister in granting an extension of time. The purchasers' judicial review was allowed in the High Court and the developer appealed.

The Court of Appeal distinguished the case of AML and held that the Federal Court's decision dealt with the Controller's power under Regulation 11(3) of the HDR and not the Minister's power under section 24 of the HDA to regulate and prohibit the conditions and terms of the SPA. The Minister retains the power to grant an extension of time for the developer to complete the units.

### Limitation period starts from date of Agreement

Further, in *Obata-Ambak Holdings Sdn Bhd v Prema Bonanza Sdn Bhd* and another appeal (**Obata**), AML was once again distinguished.

In *Obata*, the purchaser relied on AML and sought for LAD. The Court of Appeal dismissed the claim on the basis that it was time-barred.

A legal action to enforce one's rights must be commenced within a certain period. This period is known as limitation period. In Malaysia, limitation period

to commence an action for breach of an agreement is six years.

The SPA was executed in 2012. Vacant possession was delivered in 2017 but the purchaser's action was only commenced in 2020.

Upon a careful examination of the purchaser's claim, the Court of Appeal held that the purchaser's claim was in fact a claim for breach of contract as it was premised on the validity of the amended clauses in the SPA pursuant to the extension of time granted by the Controller. The purchaser's claim was not simply a claim for LAD. Thus, limitation period starts to run at the date of execution of the SPA in 2012. The purchaser's claim was time-barred as the suit was filed in 2020.

The two aforementioned cases are currently pending appeal at the Federal Court. However, these cases may provide some leeway for developers to distinguish AML currently. Crucially, Bludream may allow developers to apply for an extension of time so long as it is approved and signed by the Minister instead of the Controller. Ultimately, a balance must be sought between protecting the rights of purchasers as intended by AML and the rights of the developers, especially where there are cogent reasons for an extension of time.



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# The Effects of Malaysia's Minimum Wages Order 2022

On 1 May 2022, the Malaysian Minimum Wages Order 2022 ("the Order") comes into operation. The Order increases the minimum monthly wage of employees to RM1,500.

The Order applies to all employees except domestic servant. There is a temporary exemption to employers who employ less than 5 employees until 31 December 2022. Such exemption, however, does not apply to employers who carry out professional activities.

In Malaysia, the concept of minimum wage was introduced by the Wages Councils Act 1947, which was applicable to several sectors. It was repealed by the National Wages Consultative Council Act 2011, which established the National Wages Consultative Council to advise and make recommendations on minimum wages.

In 2013, the monthly minimum wage rate was RM900 for Peninsular Malaysia and RM800 for East Malaysia. It was subsequently raised to RM1000 for Peninsular Malaysia and RM920 for East Malaysia. The two different rates in East and West Malaysia were abolished in 2019 when the monthly minimum wage rate was raised to RM1,100. The same was, again,

raised to RM1,200 in 2020 and now to RM1,500.

The increment in minimum wage received a mixed reception. On one hand, it may be a positive development for employees, on the other, it may have a significant effect on the employers. This is particularly so when there is a 25% increase in labour costs for minimum wage workers.

It may be an untimely move as businesses are still in a tough recovery stage. Most of the industries were badly hit by Covid-19 pandemic since 2020. Therefore, to increase the minimum wage at this juncture may jeopardise the efforts of employers in reviving their businesses.

Employers who are unable to recover or sustain their businesses will have to reduce their operating costs, including their manpower costs. Employers may freeze increment, bonuses or recruitment and enforce pay cuts or even retrenchment. Employers may also seek the services of independent contractors instead of hiring employees to reduce costs. In other words, depending on the employers' ability to cope with the current economy and spiralling costs, unemployment rate might increase.

In simple economics, the increase in minimum wage ought to be associated with an increase in productivity, which will lead to an increase in revenue. If it does not, it will raise production costs and lead to spiral inflation. Based on the Q4 2021 report on Labour Productivity by the Department of Statistics Malaysia, the labour productivity merely increased by 1.7% (based on the ratio of value added per employment). Zooming in to the relevant sectors, only manufacturing and services sectors posted an increase of 6.8% and 0.5% respectively. The Agriculture, Mining & Quarrying and Construction sectors recorded a decrease of 4.6%, 3.4% and 8.3% respectively. When labour productivity is unable to correspond with the increment of minimum wages, costs of goods will eventually go up, resulting in higher costs of living. Therefore, higher wages may not improve the quality



Photo by Vlada Karpovich

of life of workers nor increase their purchasing power.

The increase in minimum wages might also result in Malaysia losing its international competitiveness compared to our neighbouring countries. Foreign investors may be more attracted to countries like Vietnam, Thailand, Cambodia, Indonesia, Philippines, Laos and Myanmar, bearing in mind that their minimum wages are lower than Malaysia's by approximately

43.99%, 41.14%, 43.21%, 11.63%, 36.98%, 69.63%, and 90.22% respectively. Lower minimum wages would mean lower operating costs and by extension, higher profits. It comes as no surprise that electric vehicle titan Elon Musk is considering to invest in Indonesia. The diversion of foreign investment will further dampen the recovery of Malaysia's economy.

In conclusion, whilst increasing the minimum wage might be a celebrative cause, it may be an ill-timed move, particularly when most employers are still recovering from the losses caused by the Covid-19 pandemic. Coupled with the global inflationary pressure due to the Russia-Ukraine war and our weakening currency, introducing an increase of the minimum wage at this juncture may do more harm than good



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# Advisory on re-registration of franchises under the Malaysian Franchise Act 1998

The Registrar of Franchise (“**Registrar**”) has issued a circular on 28 July 2022 advising that all franchise registrations will be expiring in conjunction with the coming into force of the Franchise (Amendment) Act 2020 (“**Amending Act**”) on 28 July 2022. We provide below the steps to be taken pursuant to the circular.

## A. Re-registration of franchise

In this connection, all existing franchisors (both local and foreign) who were previously registered under the old system (MyFEX 1.0) (“**existing franchisors**”) are required to re-register their franchise registrations via the new system (MyFEX 2.0) which was officially launched on 28 July 2022. A grace period of 3 years applies to all existing franchisors to complete the re-registration process. The grace period is calculated from 1 August 2022. Failure to re-register franchise registrations may result in the issuance of a notice of suspension, termination and cancellation of franchise registration by the Registrar.

Before applying for re-registration of franchise, existing franchisors are required to submit their franchise business annual reports to the Registrar.

Existing franchisors who have re-registered their franchise registrations under the new system (“**registered franchisors**”) will be required to re-register for each of their franchisee(s) (who were previously registered under the old system) (“**registered franchisee**”).

A registered franchisee who was previously registered as a “master franchisee” under the old system must re-register its franchise registration separately as a master franchisee via the new system (“**registered master franchisee**”) and thereafter re-register for each of its sub-franchisee(s) (who were previously registered under the old system) (“**registered sub-franchisee**”).

While there are prescribed official fees for new applications for registration of franchisor and franchisee/ master franchisee and sub-franchisee under the new system, the prescribed fees will be waived for re-registration of franchisors and franchisees, master franchisees and sub-franchisees previously registered under the old system provided that the process is completed within the grace period.

## B. Renewal of franchise

Following the implementation of the Amending Act and the new system, franchise registration will be effective for a period of 5 years from the date of the Registrar’s approval under the new system. As such, registered franchisors and registered master franchisees must, upon the expiry of their franchise registrations, apply for renewal via the new system with payment of the prescribed renewal fee. There is no separate renewal

process for registered franchisees and registered sub-franchisees.

## C. Next steps

The following steps are recommended to be taken by the franchisor:

1. submit the franchise business annual report, if not already done;
2. re-register its franchise registration under the new system based on the prior registration under the old system;
3. re-register for each of its franchisee(s) under the new system based on prior registration under the old system and/or register for any franchisee(s) who were not previously registered under the old system, if any, to regularize the non-compliance; and
4. if any of its franchisee(s) under step (3) is a master franchisee, re-register as a master franchisee under the new system and thereafter re-register for each of its sub-franchisee(s).



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