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Dispute Resolution

Land Law – Indefeasibility : Meaning of ‘good faith’

Introduction

In Peninsular Malaysia, the law governing land matters is embodied in the National Land Code 1965 (“NLC”). The NLC provides for the Torrens system of title by registration – it is the act of registration that confers title to or interest in land.

Section 340 of the NLC deals with the indefeasibility of a registered title to and interest in land. The term ‘indefeasible’ though used in Section 340 of the NLC, is not defined in the NLC. By a judge-made decision, this term ‘indefeasible’ has been judicially defined to mean ‘immune from attack by adverse claim to the land or interest in respect of which he is registered’.

Section 340(2) of the NLC sets out the circumstances under which a registered title to or interest in land can be rendered defeasible and set aside. Section 340(3) of the NLC provides that a subsequent registered title to or interest in land – which is acquired from a preceding owner of registered title or holder of registered interest who gets onto the register by means of one or more of the vitiating methods as specified in Section 340(2) of the NLC – shall be protected if the subsequent registered title to or interest in land is acquired ‘in good faith and for valuable consideration’ (pursuant to the proviso thereto).

To illustrate, if A acquires his title / interest by fraud, A’s title / interest is defeasible and can be set aside under Section 340(2)(a) of the NLC. But, if A subsequently transfers the title / interest to B, B’s title / interest is also defeasible and can be set aside, unless B’s title / interest is acquired ‘in good faith and for valuable consideration’. In other words, B’s title / interest is protected and cannot be set aside if B’s title / interest is acquired ‘in good faith and for valuable consideration’. The successors in title / interest of B are also protected. This is legally known as the doctrine of deferred indefeasibility of title or interest – which is so deeply embedded in the NLC.

The focus of this write-up is the meaning of ‘good faith’ in the proviso to Section 340(3) of the NLC. ‘Good faith’ is used synonymously with the Latin phrase ‘bona fide’.

A recent Apex Court case

In a recent case of *T Sivam A/L Tharamalingam v Public Bank Berhad* [2018] MYFC 11, the Federal Court (the apex court in Malaysia) had an opportunity to consider and revisit the meaning of ‘good faith’ in Section 340(3) of the NLC. The dispute was about the competing claims on a same piece of land between two parties, namely the original registered owner of the land and a chargee bank (who was a subsequent holder of interest in the land) – both were affected by the fraud of a third party. The crux of the dispute is whether or not the registered interest of the chargee bank (a subsequent holder of interest in the land) is protected under the proviso to Section 340(3) of the NLC.

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In *T Sivam*, the deceased was the original registered owner of a piece of agricultural land. One of the deceased's sons fraudulently transferred the land to himself. A common solicitor handled the transfer of the land (purportedly from the deceased) to the son.

After having been registered as the owner of the land, the son (as the registered owner) obtained a loan from a bank where a charge over the land was created and registered in favour of the bank as collateral for the loan – legally speaking, the bank (as the registered chargee) was the subsequent holder of interest in the land (who can claim protection under the proviso to Section 340(3) of the NLC). The same common solicitor handled this loan transaction for the son (a customer of the bank) and the bank – therefore, both the son and the bank are the clients of the solicitor.

Later on (after the loan transaction was completed), the deceased (the original registered owner) discovered the fraudulent transfer and the creation of the charge. The deceased then commenced two separate legal actions (one after another) to set aside the fraudulent transfer and the charge respectively. The transfer was then set aside by the Court. In seeking to set aside the charge, the deceased claimed that the charge was defeasible and not valid on the ground that the charge was created following the fraudulent transfer.

High Court's Decision

The High Court set aside the charge on the ground that the chargee bank was an immediate acquirer / holder of interest in the land and therefore, could not claim protection under the proviso to Section 340(3) of the NLC. It is important to note that the High Court made a finding that the chargee bank acquired the interest in the land in good faith.

Court of Appeal's Decision

Upon the chargee bank's appeal, the Court of Appeal reversed the decision of the High Court. The Court of Appeal held that the chargee bank was a subsequent – and not immediate – acquirer / holder of interest in the land in good faith and for valuable consideration and therefore, enjoyed the protection under the proviso to Section 340(3) of the NLC.

The Court of Appeal found that as a matter of evidence, the same common solicitor (who handled the transfer and then, the loan transaction) did not inform the chargee bank of the allegation that the land was fraudulently acquired by the deceased's son. In this regard, the Court of Appeal held that the solicitor's knowledge of fraud or the allegation of fraud could not be imputed to the chargee bank (the client) – therefore, the chargee bank had no notice of the allegation of the fraudulent transfer.

Federal Court's Decision

Leave to appeal was granted to the deceased. The Federal Court agreed with the decision of the Court of Appeal that the chargee bank was a subsequent holder of interest in the land. The crux of the appeal is whether the chargee bank (as a subsequent holder of interest in the land) acquired the interest in the

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land in good faith – if this is so, then the charge was indefeasible; but if not, then the charge was defeasible and can be set aside. Therefore, the key to the determination of this appeal centers on the meaning of ‘good faith’ in the context of Section 340(3) of the NLC.

Meaning of ‘good faith’

The Federal Court held that the existence of good faith or otherwise would depend on the particular facts of each case and emphasised that the overriding consideration is ‘the particular circumstances of each case’. In illustrating this point, the Federal Court referred to two cases.

First, the Federal Court case of *Datuk Jagindar Singh & Ors v. Tara Rajaratnam* [1983] 2 MLJ 196 where it was held that mere knowledge of fraud would suffice to negate good faith – in that case, a purchaser who has knowledge that his predecessor’s title is tainted with fraud, cannot claim protection under the proviso to Section 340(3) of the NLC (even though he himself is not guilty of any fraud).

Second, the Court of Appeal case of *Au Meng Nam & Anor v. Ung Yak Chew & Ors* [2007] 5 MLJ 136 where Raus Sharif JCA (as His Lordship then was) held that a purchaser in good faith did not include a purchaser who was careless or who had been negligent.

Adopting the principle underlying the above cases, the Federal Court laid down the elements required to prove the existence of good faith, as follows :-

- (a) good faith does not simply mean absence of fraud, deceit or dishonesty; it also requires acting honestly, reasonably or fairly – this includes taking ordinary precautions that ought to be taken;
- (b) the elements of good faith are not closed; it must in all cases depend upon the circumstances;
- (c) it is not enough for a purchaser to merely show absence of fraud, deceit or dishonesty; knowledge of a dispute as to the ownership of property and knowledge of fraud allegation, for example, could vitiate good faith;
- (d) an element of carelessness and negligence negates good faith.

In allowing the deceased’s appeal (reversing the decision of the Court of Appeal), the Federal Court set aside the charge and held that the chargee bank did not acquire the interest in the land in good faith – on the grounds that :-

- (i) the knowledge of the (same common) solicitor (who handled the transfer for the son and then, the loan transaction for the chargee bank) that there was a serious dispute as to the ownership of the land, and of the allegation that the son (the customer of the chargee bank) obtained title to the land by fraud – the aforesaid knowledge of the solicitor was acquired in the earlier (the first) transaction (namely, the transfer of the land purportedly from the deceased to the son) – is regarded and treated by the law as the knowledge of the chargee bank (as the client of the solicitor);

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- (ii) in other words, the aforesaid knowledge of the solicitor must be imputed to the chargee bank in the course of acting for the chargee bank (in creating and registering the charge). This is so despite the fact that (even if) the solicitor was unwilling to and did not reveal the aforesaid knowledge to the chargee bank;
- (iii) the two transactions (the transfer of the land to the son and then, the loan transaction) were immediately consequent on one another, and were very closely connected that the first (transaction) must obviously have been still present in the solicitor's mind – the solicitor could not claim to have forgotten the aforesaid knowledge/information;
- (iv) in the light of the fraud allegation (which the chargee bank is regarded as knowing, by imputation), there was a real necessity for the chargee bank to conduct further investigative work;
- (v) in the face of suspicious and uncertain circumstances under which the transaction (of the transfer of the land) was transacted (which the chargee bank is regarded as knowing, by imputation), the chargee bank failed to make further inquiries before creating the charge and disbursing the loan.

The Federal Court clarified that the general rule is that the knowledge of a solicitor is regarded by law as the knowledge of the client – except where the solicitor is complicit in fraud.

Conclusion

The above decision of the Federal Court in *T Sivam*, as it stands, represents the current legal position on the meaning of good faith under the proviso to Section 340(3) of the NLC.

Accordingly, when acquiring title to or interest in land, an acquirer of title to or interest in land should act honestly and take ordinary precautions that ought to be taken – in doing so, he should be careful not to act carelessly and negligently. Further, the acquirer should conduct further investigative work and make further inquiries when the circumstances are such that he is (or should be) put on inquiry.

Keeping in mind that the knowledge of a solicitor is regarded by law as the knowledge of the client (by imputation), it is prudent to engage a solicitor (a law firm) who is not privy to any previous dealings with the land.

Epilogue

With all due respect, it is respectfully submitted that the approach of the Court of Appeal in *Au Meng Nam* holding that a purchaser in good faith does not include a purchaser who is careless or negligent – which is adopted by the Federal Court in the above case of *T Sivam* – ought to be construed to apply only to the facts peculiar to that case (*Au Meng Nam*) and should not be construed as authority for the blanket proposition that carelessness or negligence negates good faith under the proviso to Section 340(3) of the NLC. Probably, the Court of Appeal in *Au Meng Nam* had to take that approach in order to avert injustice spawned by a decision of the Federal Court in *Adorna Properties Sdn Bhd v. Boonsom*

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Boonyanit [2001] 1 MLJ 241 which was at that time binding on the Court of Appeal, but was later on overruled by the Federal Court in *Tan Ying Hong v. Tan Sian San & Ors* [2010] 2 MLJ 1.

Bearing in mind that 'good faith' has often been judicially defined at least since two decades ago to mean 'absence of fraud, deceit or dishonesty', the perimeter of 'good faith' should not be expanded to include absence of carelessness or negligence. It is therefore submitted that carelessness or negligence should not be taken into consideration when deciding on the issue of good faith in the context of indefeasibility of title or interest under Section 340(3) of the NLC.

It is hoped that an opportunity will soon arise for the Federal Court to revisit the meaning of good faith under the proviso to Section 340(3) of the NLC. For that, only time will tell; we shall await another decision of the Federal Court.

Should you have any queries, please contact our team members below.

Contacts



Heng Yee Keat
Partner

D +60 3 2267 2723
F +60 3 2273 8310
yee.keat.heng@christopherleeong.com



Diana Chang Kuok Eng
Associate

D +60 3 2267 2659
F +60 3 2273 8310
diana.chang@christopherleeong.com

Our Regional Contacts

RAJAH & TANN | *Singapore*

Rajah & Tann Singapore LLP

T +65 6535 3600
F +65 6225 9630
sg.rajahtannasia.com

CHRISTOPHER & LEE ONG | *Malaysia*

Christopher & Lee Ong

T +60 3 2273 1919
F +60 3 2273 8310
www.christopherleeong.com

R&T SOK & HENG | *Cambodia*

R&T Sok & Heng Law Office

T +855 23 963 112 / 113
F +855 23 963 116
kh.rajahtannasia.com

RAJAH & TANN NK LEGAL | *Myanmar*

Rajah & Tann NK Legal Myanmar Company Limited

T +95 9 7304 0763 / +95 1 9345 343 / +95 1 9345 346
F +95 1 9345 348
mm.rajahtannasia.com

RAJAH & TANN 立杰上海 SHANGHAI REPRESENTATIVE OFFICE | *China*

Rajah & Tann Singapore LLP Shanghai Representative Office

T +86 21 6120 8818
F +86 21 6120 8820
cn.rajahtannasia.com

GATMAYTAN YAP PATACSIL GUTIERREZ & PROTACIO (C&G LAW) | *Philippines*

Gatmaytan Yap Patacsil Gutierrez & Protacio (C&G Law)

T +632 894 0377 to 79 / +632 894 4931 to 32 / +632 552 1977
F +632 552 1978
www.cagatlaw.com

ASSEGAF HAMZAH & PARTNERS | *Indonesia*

Assegaf Hamzah & Partners

Jakarta Office

T +62 21 2555 7800
F +62 21 2555 7899

Surabaya Office

T +62 31 5116 4550
F +62 31 5116 4560
www.ahp.co.id

RAJAH & TANN | *Thailand*

R&T Asia (Thailand) Limited

T +66 2 656 1991
F +66 2 656 0833
th.rajahtannasia.com

RAJAH & TANN LCT LAWYERS | *Vietnam*

Rajah & Tann LCT Lawyers

Ho Chi Minh City Office

T +84 28 3821 2382 / +84 28 3821 2673
F +84 28 3520 8206

RAJAH & TANN | *Lao PDR*

Rajah & Tann (Laos) Sole Co., Ltd.

T +856 21 454 239
F +856 21 285 261
la.rajahtannasia.com

Hanoi Office

T +84 24 3267 6127
F +84 24 3267 6128
www.rajahtannlct.com

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