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Dr. Sharifah Suhanah Syed Ahmad
Executive Editor

Reforming the Capital Maintenance Doctrine in the Context of China: From the Guiding Cases Perspective

Gao Fei*

Abstract

The doctrine of capital maintenance is an important principle of company law. Since the 20th century, a number of crucial changes relating to the rules of capital maintenance have been adopted in several jurisdictions. This has resulted in the deregulation and relaxation of a number of measures. China has followed this trend and has relaxed the regulations on corporate capital in recent years. However, the rules on capital maintenance have remained largely unchanged. This has elicited a heated debate on whether China should abolish the doctrine of capital maintenance altogether. This article argues that instead of abolishing the capital maintenance doctrine, it should be modified to make creditor protection more effective. The article suggests that, the guiding cases released by the PRC Supreme People's Court play an important role in the development of company law in China, and there are influential cases in modifying the rules of capital maintainance. The paper also suggests that the mandatory capital maintenance rules under Chinese company law should be further relaxed. The court should not mechanically follow existing capital maintenance rules but should improve it through guiding cases.

Keywords: Capital Maintenance Doctrine, China, Guiding Case, Reform.

I. INTRODUCTION

Chinese company law was reformed by the Standing Committee of the National People's Congress on 28 December 2013, taking effect from 1 March 2014.[1] This reform repealed the minimal registered capital requirement and simplified the procedure for starting a company. At the same time, the State Council also promulgated the Scheme for the Registration System Reform of Registered Capital (the Scheme), which was implemented concurrently with the amendment to the company law.[2] The Scheme changed the requirement for an annual inspection[3] on the enterprise to an annual report, which requires

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1 "*The Decision on Amending the Marine Environmental Protection Law and Other Seven Legislations of the Sixth Session of the Standing Committee of the Twelfth National People's Congress"*, http://www.npc.gov.cn/npc/xinwen/2013-12/30/content_1821988.htm. Site accessed on 14 December 2017.

2 *"The Notice of the State Council on Issuing the Scheme for the Registration System Reform of Registered Capital"*, http://www.gov.cn/zhengce/content/2014-02/18/content_8642.htm. Site accessed on 14 December 2017.

3 The annual inspection required all enterprises summit materials related to corporate registration and finance to the administration of industrial and commercial bureau, and the bureau shall, in accordance with law and on the basis of the submitted materials, conduct a supervision of periodic inspection.

enterprises to submit its annual report through the National Enterprise Credit Information Publicity System.[4] The annual report will include among others, information concerning subscribed capital and paid-up capital, equity change, administrative penalties. As one of the supporting measures, the Interim Regulation on Enterprise Information Disclosure (the Regulations) was promulgated by the State Council on 7 August 2013, which took effect from 1 October 2014.[5] These measures began the reforms on corporate capital (the 2013 reform) in China.

The purpose of the 2013 reform was to reduce the cost of starting a company and to encourage investment. According to the National Report on the Development of Market Participants released by the State Administration for Industry and Commerce (SAIC), since the implementation of the 2013 amendments to company law, there has been more than 10 million new market participants. Amongst which were nearly three million enterprises, an increase of 53.99%, with an average of 10,400 new enterprises per day.[6] This suggests that the 2013 amendments has played an important role in promoting the development of the Chinese economy.

The doctrine of capital maintenance has always been a fundamental principle of company law in many jurisdictions such as United Kingdom, Germany and Japan.[7] Local Chinese academia and judicial practices however, commonly interprete capital maintenance as a doctrine that requires the company to retain assets equivalent to the contributed capital in order to protect creditors.[8] The reform on corporate capital brings millions of jobs and benefits the market economy. However, it also elicites a heated discussion on creditor protection. If there is no minimal registered capital requirement, would capital still matter in protecting creditors?[9] Should China abandon the capital maintenance doctrine?

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4 There are some differences between annual inspection and annual report: (1) The purpose of annual inspection is for supervision, while the purpose of the annual report is just reporting, so the enterprises do not need approval by the industrial and commercial bureau to continue its business; (2) Some of the materials need not be summitted under the annual report system, such as the corporate audit report; (3) If the company does not undertake the annual inspection, the bureau could revoke its business license. However, the company may continue its business even if they do not summit qualified materials under the annual report system. The bureau will continue asking the company to summit its annual report. A continued failure to comply will result in the company being put on the list of abnormal business operations.

5 See http://www.gov.cn/zhengce/2014-08/23/content_2739774.htm. Site accessed on 14 December 2017.

6 According to the National Report on the Development of Market Participants, there were 10,400 newly enterprises on average established per day. See http://politics.people.com.cn/n/2014/1208/c70731-26170483.html. Site accessed on 10 March 2018.

7 For example, In the United Kingdom, the key statutory provision embodying this 'capital maintenance' rule is section 263 of the Companies Act 1985. This prohibits any form of distribution of corporate assets to shareholders except where the value of the distribution is less than that of the profits available for distribution. See John Amour, "Legal Capital: an Outdated Concept?" *European Business Organization Law Review*, 2006, Vol. 7, pp.8-9.

8 See Liu Junhai, *Protection of Shareholder's Right in Stock Company*, 1st Ed., Law Press, 2004, pp.162, and Du Jun, The principle, evolution and new subject of judicature of coporate capital, *Journal of Law Application*, 2014, Vol. 11, pp.3.

9 Creditors can be divided into two types, the voluntary creditor and the non-voluntary creditor. Voluntary creditor usually trades with the company in the form of contract, such as the bank, the supplier, the contractor, etc. They can decide whether to trade or not based on the credibility of the company. A non-voluntary creditor refers to creditors who do not contract with the company, and their debt is often generated because of tort. They cannot choose who to trade with and the legal system on corporate capital cannot protect this kind of creditor. This article mainly discusses the with voluntary creditor.

This article illustrates the importance of the capital maintenance doctrine in China and suggests modifications to be made to the capital maintenance rules. Part II introduces the evolution of the capital maintenance doctrine in the context of China. Part III explains why it is necessary that China should insist on the capital maintenance doctrine. Part IV discusses the importance that guiding cases play in the development of company law and lays out some suggestions to modify the capital maintenance rules through guiding cases. Part V presents a unique insight on the prospects of modifying the capital maintenance rules through guiding cases; and finally, Part VI concludes.

II. CAPITAL MAINTENANCE DOCTRINE IN THE CONTEXT OF CHINA

There is no formal definition of the doctrine of capital maintenance. A company's capital is considered as constituting its trust fund[10] which should not be returned to the shareholders. Some specific rules which laid restrictions on corporate capital usage were subsequently developed; such as rules restricting shareholders on withdrawing their paid-up capital, rules prohibiting share buyback and rules limiting capital reduction. However, after years of practice, the existing rules on the doctrine of capital maintenance were found to have imposed unreasonable restrictions on corporate capital usage. The UK Company Law Review Steering Group, set up in 1998 to reform English company law has noted that in practice, "creditors and potential creditors nowadays no longer regard the size of a company's issued share capital as a significant factor when considering whether or not to extend credit to it".[11] They pay much more regard to the company's financial strength as indicated by its financial ratio, its business prospects and the overall economic environment within which the company operates.[12] Therefore, the purpose of the capital maintenance doctrine has changed from that of protecting creditors to prohibiting shareholders from taking undue priority in securing their interests. As explained by Professor David Wishart, "In this respect, the rules derived from the principle of maintenance of capital performed the useful function of preventing other interests, mainly the shareholders, from taking undue priority. However, they were misdirected in protecting the capital fund as an absolute figure".[13]

Since the 20th century, a number of very important changes relating to the capital maintenance rules have been adopted in several jurisdictions,[14] resulting in the deregulation and relaxation of a number of measures. With regards to specific regulations,

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10 Capital maintenance doctrine was first put forward by Lord Story and his 'trust fund' theory. He illustrated in the leading case of *Wood v Dummer* in 1824, "the paid-up capital was considered as a promise offered by the shareholders, or trust fund raised by the shareholders in order to protect creditors, so the law should set up standards to achieve this objective".

11 Wee Meng Seng, "Reforming the Capital Maintenance Law: The Companies (Amendment) Act (2005)", *Singapore Academy of Law Journal*, 2007, Vol.19, p.305.

12 *Ibid*.

13 David Wishart, *Company Law in Context*, 1st Ed., Oxford University Press, 1994, p.177.

14 For example, Japan abolished rules on par value and allow company to buy back its shares in 2003 and 2001. Singapore carried out similar reforms on corporate capital in 2006.

the company law was modified to, among others, allow for capital reduction,[15] abolish rules on par value,[16] and allow for more exceptions to share buyback. Some jurisdictions like the United States, Canada and New Zealand have given up the doctrine of capital maintenance altogether and have instead adopted the solvency test[17]to protect creditors.[18]

The legal capital regime in China includes the capital contribution rules and the capital maintenance rules. In the past, the capital contribution rules required a minimal registered capital to be contributed before the company is started. As for the capital maintenance rules, there were a series of strict restrictions for shareholders withdrawing its contributed capital from the company, such as prohibiting share buyback, and strict restrictions on capital reduction.

As restrictions on corporate capital became relaxed around the world, China began to follow suit in relaxing its strict restrictions on corporate capital usage. The first amendment was in 2005, which reduced the minimal registered capital requirement and allowed the company to buy back its shares under prescribed conditions.[19] It also allowed the company to provide guarantees for its shareholders and other enterprises,[20] and cancelled the restrictions on a company investing in other businesses.[21]

The second amendment was in 2013, this deregulated restrictions on corporate capital, such as abolishing the minimal registered capital requirement and the time-limits for capital contribution. The purpose of the amendment was to simplify the requirements to start a company and encourage investment. However, there were nearly no changes at all to the capital maintenance rules in the amendments (The specific modifications are in Table 1).

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15 For example, in Australia, section 256B(1) Corporations Act 2001 provides that a company has the general power to reduce its share capital if three requirements are satisfied: first, the capital reduction is fair and reasonable to the company's shareholders as a whole; secondly, it does not materially prejudice the company's ability to pay its creditors; and thirdly, it is approved by shareholders.

16 For example, the Singapore Companies Act 2006 abolished par value and provides that shares of a company have no par or nominal value in 62A(1) of the Companies Act.

17 The solvency test is centered on the proof of solvency. It depends on whether the company can pay its due debts within a certain period after the allocation of the company's assets. If the company can be proved to be able to pay the due debts of that period, the company's assets can be returned to shareholders.

18 *Supra* n11, at pp301.

19 See Article 75 and article 143 of the 2005 Chinese Company Law.

20 See Article 16 of the 2005 Chinese Company Law.

21 See Article 15 of the 2005 Chinese Company Law.

Table 1. The Development of Legal Capital Regime in China

	Regulations	**1993 Company Law[22]**	**2005 Company Law[23]**	**2013 Company Law[24]**
Capital contribution rules	Subscribed capital or paid-up capital	Paid- up capital, all capital should be contributed before starting a company.	Subscribed capital, at least 20% for the first contribution and the rest should be paid in 2 years (5 years for investment company).	Subscribed capital, no time-limits on contribution.
	Minimal registered capital requirement	Limited liability company: production and wholesale 500,000RMB: retail industry 300,000RMB: IT and services industry 100,000RMB; Stock company: 10,000,000RMB	Limited liability company: 30,000RMB One-man company: 100,000RMB; Stock company : 500,000,000RMB	Abolished
	Forms of contribution	Cash, assets, intellectual property, right of land use. Non-cash contribution should not exceed 20% of the total paid-up capital.	Cash and other assets which can be valued and transferred, and contribution in cash should not be less than 30% of the total subscribed capital.	Unchanged except abolishing the proportion of non-cash contribution.
	Par value	Every share has par value and issue at a discount is not allowed	Unchanged	Unchanged

22 The 1993 Chinese Company Law was passed on 29 December 1993, and took effect on 1 July 1994.

23 The 2005 Chinese Company Law was passed on 27 October 2005, and took effect on 1 January 2006.

24 The 2013 Chinese Company Law was passed on 28 December 2013, and took effect on 1 March 2014.

Table I. The Development of Legal Capital Regime in China (continued)

	Regulations	**1993 Company Law[22]**	**2005 Company Law[23]**	**2013 Company Law[24]**
Capital maintenance rules	Guarantee ability	Not allowed to guarantee for shareholders or other enterprises.	Allowed if the resolution is passed by the board or the meeting of shareholders.	Unchanged
	Investment ability	The accumulative investment should not exceed 50% of the net assets of the company, except investment companies and holding companies provided by the State Council.	A Company can invest in other enterprises, but should not become the contributor who bears unlimited joint liability unless otherwise provided for by law.	Unchanged
	Capital Withdrawal	Not allowed	Unchanged	Unchanged
	Distribution	Profits may be distributed to shareholders after making up the losses and withdrawing the legal reserve and welfare reserve.	Profits after tax can be distributed to shareholders after making up the losses and withdrawing legal reserve.	Unchanged
	Share buyback	Not allowed	Dissenting shareholders may request that the company buys back their shares under prescribed conditions.	Unchanged
	Capital reduction	Company should inform creditors who have the right to require the company to pay back its debts or give reasonable guarantee before capital reduction	Unchanged	Unchanged

As seen from the above table, the 2013 reform on corporate capital has had the following effects: (1) China still adopts the legal capital regime, instead of the authorised

capital regime. This is because company shares are issued once, and the right to issue new shares remains with the shareholders, not the board of directors; (2) it does not change shareholders' obligation to contribute, but the time-limit for contribution is cancelled. Shareholders may now contribute in installments; (3) although there is no minimal subscribed capital requirement, other regulations with respect to the capital maintenance doctrine have not changed at all. Capital which has been contributed to the company cannot be reduced or returned to shareholders, unless certain prescribed conditions are satisfied. After the 2013 reform, it is much easier to start a company than ever before, but shareholders still need to follow strict restrictions on corporate capital in business.

However, this may create new problems with respect to corporate capital. For example, if shareholders promise to finish the contribution in 100 years, or even longer, how would creditors be protected if the said shareholders failed to fully contribute? Can a creditor ask the shareholders to contribute or repay the debts directly? As capital maintenance rules have placed unreasonable cost on shareholders and reduced flexibility on corporate capital, some common law jurisdictions have given up the capital maintenance doctrine and adopted the solvency test to protect creditors instead.[25] Should China relax or even abolish the capital maintenance doctrine?

III. SHOULD CHINA ABOLISH THE CAPITAL MAINTENANCE DOCTRINE?

Why do we need capital maintenance rules to protect creditors? In economic terms, these rules might be understood as a response to problems of information asymmetry in corporate credit markets.[26] However, after the 2013 reform, both the government and the company are obligated to disclose some of the registration and financial information to the public.[27] This decreases the information asymmetry between the company and its creditors to some extent. Creditors no longer rely solely on the contributed capital to judge the credibility of the company and protect themselves. On practical grounds, the capital maintenance doctrine has been criticised for imposing unreasonable costs and restrictions on company management without providing benefits to justify the costs.

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25 For example, the United States, Canada and New Zealand, have gave up the capital maintenance doctrine and adopt solvency test.

26 John Armour, "Share Capital and Creditor Protection: Efficient Rules for a Modern Company Law", *The Modern Law Review*, 2000, Vol. 63, p.365.

27 According to Article 6 of the Regulation, AIC should disclose information on corporate registration, chattel mortgage, equity pledge and administrative penalty. Article 7 of the Regulation stipulates that other bureau should disclose administrative license approval, change, renewal information, administrative penalty information and other information which should be open to the public. Article 8 and 9 stipulates the obligation for the enterprises to summit its annual report, which include: (1) address, postal code, phone number, E-mail and other information of the enterprise;(2) information on the existence status of the enterprise, such as opening, closing and liquidation;(3) investment, equity purchase information; (4) the amount, time and method of capital contribution subscribed and actually paid by shareholders or initiators; (5) equity transfer and other equity change by shareholder of limited liability company; (6) website of the company, name and web address if it engaged in online business; (7) the number of employees, total assets, total liabilities, external guarantee, total owners' equity, total business income, main business income, total profit, net profit, total tax.(this is optional).

In practice, what the creditor is concerned about the most is the company's ability to perform. Subscribed capital and paid-up capital are certainly two of the most important factors affecting the company's ability to perform.[28] But creditors will consider other factors, such as the reputation of the company, past trading records with the company, earning per share, asset-liability ratio and other financial ratios. Furthermore, net assets may be diminished or lost in the course of the company's trading, even if the registered capital remains constant. If the company does well, the net assets may exceed its registered capital. Conversely, if the business performs poorly, net assets may be less than the company's registered capital. Therefore, when creditors judge the company's performance, they are more concerned with the net assets rather than the corporate capital. On the other hand, if shareholders have better investment opportunities, it may make more economic sense to return contribution to shareholders, as it will increase the whole social welfare without infringing upon the interest of creditors. This is in accordance with Pareto Improvement[29] which is one of the objectives of the society. If we insist on the outdated and mechanical doctrine of capital maintenance, prohibiting companies from returning its assets to shareholders, it will limit corporate autonomy, in turn reducing the effectiveness of deployment of the company's assets. As pointed out by the Interdisciplinary Group on Capital Maintenance of EU:

> Any return of assets to shareholders increases the risk to creditors; but without a return for investors, companies could not perform and contribute to general welfare, and even creditors would not be in business at all. It is thus a question of reasonable balance, or proportionality.[30]

The main function of the capital maintenance doctrine is to protect creditors. Creditor protection is necessary due to the information asymmetry between the company and its creditors. If the problem of information asymmetry is addressed by other mechanisms, should the capital maintenance doctrine be kept?

As mentioned before, the Regulations stipulate disclosure obligations for both the enterprise and the government agencies.[31]As soon as the Regulation was promulgated in August 2013, the SAIC established the National Credit Information System of Enterprises[32]and officially made the information accessible to the public. It was designed to decrease the information asymmetry between the company and its creditors, in hopes that creditors may better assess the credibility of the company through these information disclosures. This would then make transactions more reliable.

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28 In China, the company should register its subscribed capital in the business license, and the paid-up capital should be reported in the annual report. Shareholders shall make capital contribution in accordance with the subscribed capital, and the unpaid capital subscribed by shareholder is regarded as the debt owed by shareholders to the company.

29 Pareto Improvement is named by the famous economist Vilfredo Pareto. He puts forward that if a policy makes at least one person better off without making anyone worse off, it will be efficient for the whole society.

30 Interdisciplinary Group on Capital Maintenance, "Reforming Capital: Report of the Interdisciplinary Group on Capital Maintenance", *European Business Law Review*, 2004, Vol.15, p.919.

31 *Supra* n27.

32 See http://gsxt.saic.gov.cn. Site accessed on 15 December 2018.

However, the above measure only solved the ex-ante information asymmetry problem before creditors enter into transactions. But what if a company reduces its capital after the transaction? The reality in China today is that directors who breach their duties of loyalty are seldom constrained and punished.[33] Creditors's rights are usually infringed because of director's misuse of coporate capital, such as false capital contribution, withdrawal of capital, or related-party transaction. Although the Regulation obligates disclosure by both the company and the Bureau, the company only has to disclose part of its financial information to the System, together with other pieces of information from the bank, the tax bureau or the court. These are required to be included in the System but are kept separately from the disclosed financial information. This results in a situation where the information collected by the System is not reflect in the actual financial and operation status of the company. Hence, creditors will be able to accurately assess the credibility of the company and the ex-post information asymmetry has not been fundamentally changed. Capital maintenance doctrine is still considered to be useful to protect creditors. We should not simply abolish the capital maintenance doctrine, but instead modify it to make it more suited to its role of creditor protection.

IV. HOW TO MODIFY THE CAPITAL MAINTENANCE DOCTRINE IN THE CONTEXT OF CHINA?

China is a civil law country without the principle of stare decisis. However, understanding the flexibility offered by case law, the PRC Supreme People's Court laid out the Provisions on Case Guidance (the Provisions) in 2010, and has released 96 guiding cases up to June, 2018.[34] The Provisions stipulated that the courts should make reference to the guiding cases released by the Supreme People's Court when faced with similar cases.[35] In 2015, the Supreme People's Court further promulgated Rules for the Implementation of the Provisions on Case Guidance (the Rules). It also stipulates that if a case is similar to the guiding cases issued by the Supreme People's Court, the courts are to make judgment by referring to those relevant guiding cases.[36] The guiding case or cases are to be cited in the reasoning but it need not be the basis of the judgment.[37] According to the above regulations, we can conclude that the guiding cases have *de facto* binding effect for similar cases in China.

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[33] Compared with 3000 corporate law suits, there were only 16 lawsuits with regard to director duties in court of Beijing from 2005 to 2007, and 15 of them lost in the suits. See Lou Jianbo, Yan Hui and Zhao Yang, "Study on the application of fiduciary duty of directors, supervisors and senior executives in the Company Law-- empirical research on relevant cases of court of Beijing from 2005 to 2007", Essays on commercial law(Vol.21), Law Press, 2012, pp.535. According to another report released by court of Beijing, there were only 61 cases related to duty of loyalty of directors and senior executives from 2010 to 2015. See Beijing Higher People's Court, "White paper on the trials of duty of loyalty of directors and executives of companies from 2010 to 2015", http://www.sohu.com/a/156656876_818183. Site accessed on 15 December 2018.

[34] Besides, the Supreme People's Court has routinely released cases in the form of bulletins since 1985. These cases have similar guiding effect in practice.

[35] See Article 7 of the Provision.

[36] See Article 9 of the Rules.

[37] See Article 10 of the Rules.

A. The Importance of Guiding Cases in the Development of Chinese Company Law

In common law jurisdictions, some of the rules of company law originate from cases, such as the *Solomon* case[38] which arose due to the independent personality and limited liability of the company. The 2006 UK Company Act summarised the rules of directors duties in different cases and for the first time specified the general duties for directors.[39] Compared to statutes, case law has an advantage in terms of flexibility and uniformity. When there is no relevant regulation, the court may create new rules through case law. In case of legislative ambiguity, case law may also unify judicial rules. Cases are also important in China. There have been numerous examples which have proven the importance of cases in the development of Chinese company law, especially when it comes to capital maintenance rules.

As an example, in China, some of the capital maintenance rules are first summarised by cases. For example, in the 1993 Company Law, the accumulated investment of the company could not exceed 50% of the company's net assets. But in practice, the judge does not mechanically apply this rule. In the event that the court decides that the investment would not infringe upon the interests of the shareholders and creditors, this rule did not hold. An instance of this scenario is succinctly demonstrated in the following case.

> A Shenyuan company, Jiuhuan company and Huaxin company signed a cooperation contract to incorporate the Songhuajiang oil station company. Later, Jiuhuan and Huaxin said that the accumulated investment of Shenyuan exceeded 50% of its net asset, so the cooperation contract was invalid. The court however decided that the cooperation contract was valid.[40]

The court explained in its reasoning that even though the accumulated investment exceeded 50% of the company's net asset, the purpose of the limitation was to prevent such investment from infringing upon the interest of shareholders and creditors, not the company receiving the investment. In addition, the company's net asset changes from time to time. As a result, the investment and the cooperation contract were valid. In the 2005 amendment, such limitations were subsequently abolished from Chinese company law.

Second, the sophistication of judges varies from place to place in China, and as such contradictions among rules inevitably exists in large numbers of legislation,[41] judges may reach different judgments despite similar facts.

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38 *Solomon v Solomon Co. Ltd*, [1897] A.C.22.

39 See Article 170-177 of the 2006 UK Company Act.

40 *Shanghai Jiuhuan huaxin oil sale Co. Ltd v Shanghai Shenyuan trading Co. Ltd*. (2002) Shanghai No.314, civil tribunal 3 judgement of last resort.

41 For example, Article 72 of the General Provisions of Civil Law (2017) stipulates, the directors and other corporate executive agencies or members of decision-making organisations shall be the obligatory liquidators. However, Article 183 of the 2013 Company Law provides that the liquidator of a limited liability company shall be all its shareholders rather than members of the board of directors or executive directors, and the liquidator of a stock company shall be members of the board of directors or other personnel separately determined by the general meeting of shareholders. As such who shall be the liquidator of the company is in dispute.

Guiding cases help to reduce the uncertainty of regulations. As guiding cases have *de facto* binding effect upon other courts, judges may make decisions according to the summarised application rules thus reducing the probability of 'same facts but different judgment'.

Third, according to the report of Zhongyuan district people's court of Zhengzhou city, which first executed the guiding cases approach, the number of meetings convened by the judicial council of the court to discuss complicated cases has reduced by 50%, and overall the number of meetings reduced by nearly 80%.[42] Additionally, since the client may better predict the result of the suit through comparing similar casess, the appeal rate also saw a 12% decrease.[43] The guiding case approach has thus improved judicial efficiency and reduced the rate of erroneous judgment.

Further, the guiding cases approach may improve the efficiency of legal reforms. According to the institutional change theory, there are two kinds of institutional change. One is the induced institutional change[44] which has a lower cost in the enforcement of law, and the other is the mandatory institutional change[45] which has a lower cost in enacting the law. The guiding cases approach discussed in this paper is an example of induced institutional change. With cumulated cases, the court summarises the rules in the application of law, and then promulgates it in the form of written legislation. This process is a 'bottom (the court) up (the legislature)' approach which conforms to the process of induced institutional change.

It takes a long time to modify the statute because it needs to follow complicated procedures, which may require many drafts and several rounds of review. The guiding cases approach is thus more flexible when it comes to introducing new rules. Lastly, the rules summarised by the guiding cases may eventually become statutory provisions. After applying the rules in different cases multiple times, people will understand and accept these rules. This also expedites the enforcement of the law.

For example, the capital maintenance rule prohibits shareholders from withdrawing their contributed capital. But how should the withdrawal of capital contribution be defined? Company law has yet to clarify specific rules on capital withdrawal. As a result, the court summarised the rules on withdrawing contributed capital based on their understanding of the doctrine of capital maintenance.

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42 Zhang Dongbo, "Empirical studies on establishing the guiding case system", selected paper by Shen Deyong, *Research on the typical guiding cases in China*, 1st ed, People's Court Press, 2009, pp.134-135.

43 *Supra* n21.

44 Induced institutional change is also called demand-oriented institutional change. It refers to people spontaneously advocating and organising to change or replace the existing arrangements and creating new arrangements in order to gain opportunities for profit. The typical characteristic of the induced institutional change is spontaneous. It is a process 'from bottom to the top'. As the need for new arrangement comes from the people, it is easy to be understood and carried out.

45 Mandatory institutional change is also called supply-oriented institutional change. It refers to a kind of institutional change in which external coercive force, such as administrative power and legislation, promotes and make changes on the arrangement. The typical characteristic of the mandatory institutional change is its coerciveness. It is a process 'from the top to the bottom'. It may has lower cost in making new arrangement, but it may has higher cost in carry it out, since people may not agree to the new arrangement.

> Kuari Company was set up by Mr. Gao and Mr. Yan, but the contributed capital of Mr. Gao was borrowed from Hennan Company. After registration of the company, Kuari Company returned the contributed capital to Hennan. The court decided that as a shareholder of the company, Mr. Gao cannot borrow money that is used for verifying the company capital and then withdraw it to the lender in just a few days. The court recognised it as being a typical type of withdrawing of the contributed capital, so Mr. Gao should pay the contributed capital back to the company.[46]

In fact, there are different ways that the shareholder may withdraw the contributed capital. After numerous cases, the PRC Supreme People's Court finally promulgated the applicable rules in the form of judicial interpretation in 2010[47] which summarised the guiding rules on capital withdrawal.[48]

B. Examples to Modify the Capital Maintenance Rules through Guiding Cases

Even if the capital maintenance rules have yet to be modified, the court does not follow the rules rigidly. On the contrary, the court judgments have attempted to introduce changes in accordance with their understanding of the capital maintenance doctrine. The court can create new rules in the form of guiding cases when there is no specific rule, or when the rule is ambiguous.

For example, shareholders can transfer company assets in the form of share buyback. According to Article 74 of the 2013 company law, under any of the following circumstances, shareholders who vote against the resolution of the shareholders' meeting, may request the company to purchase their shares at a reasonable price: (1) the company that has made profits for five consecutive years has failed to distribute any dividends to the shareholders for five consecutive years; (2) the company is about to undergo a merger, to be split up, or transfer major properties to others; (3) when the business terms as specified in the articles of association expires, or other reasons for dissolution as prescribed in the articles of association occur, the shareholders must adopt a resolution to modify the articles of association to allow the company to continue its existence.[49]

What if the company buys back its shares from shareholders beyond the prescribed conditions? Would the validity of the purchase be impugned under such conditions? In the following case, the court allowed the company to buy back its shares despite not satisfying the prescribed conditions.

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46 *Mr. Gao v Shanghai Kuari chemical Co.Ltd*, (2010) Shanghai No. 617 civil tribunal 4 judgment of last resort.

47 See Article 12 of the Provision on the application of the Company Law of the People's Republic of China(III).

48 According to the judicial interpretation, the forms of illegal withdrawing of contributed capital includes, fictitious claims and liabilities, allocation of inflated profits, related party transactions, and other kinds of withdrawing without legal procedures.

49 Article 142 of the 2013 Chinese Company Law stipulates the prescribed conditions for stock company, which provides that in one of the following cases could company buy back its shares:(1) reduce the company's registered capital;(2)merge with other companies holding shares of the company;(3) awarding shares to employees of the company; and (4) shareholder requests the company to purchase its shares because he objects to the resolution of merger or spilt up of the company made at the shareholders' meeting.

Mr. Ye used to be the shareholder of a company, and he signed a contract with the company to transfer his shares to the company. Mr. Ye then sued the company for delayed payment. The judge explained in the verdict that though Article 74 allows the company to buy back its shares under certain conditions, it did not prohibit the company from buying its back its shares. That is to say, that the company and its shareholders could agree to buy back its shares. Apart from this, the judicial interpretation in this case also stipulated situations for buying back shares, other than those indicated under company law.[50] This agreement reached by the shareholder and the company does not harm the interests of the creditors. Therefore, the judge decided that the share buyback contract was valid.[51]

It is not unusual to allow companies to buy back its shares in situations which do not satisfy the prescribed conditions. According to an empirical study conducted by scholars in China, 23.07% of the 39 cases allowed the company to buy back its shares in cases where the prescribed conditions were not satisfied, while the other 76.93% of 39 cases strictly followed the rules laid out in company law.[52]

Table II. Cases on share buyback in limited liability company in China.

Situations	Quantity	Percentages
The court supports share buyback beyond the prescribed conditions	9	23.07%
The court supports share buyback within the prescribed conditions	30	76.93%

Data accurate as of September 2014.

Share buyback is not only a measure to protect shareholders who vote against the resolution of the shareholders' meeting, it is also widely used as, among others, a means of anti-takeover, stock option and Employee Stock Ownership Plan (ESOP), among others. The strict restriction on share buyback limits its application and reduces efficiency of usage of company assets. Some bureaus in China have tried to modify the rules on share buyback. For example, the Shanghai Stock Exchange published the guidance for listed company to buy back its shares in the form of centralised quotation trading. According to the above guidance, the Exchange encourages listed companies to buy back its shares under seven conditions, including, when the share price is lower than the net asset per

50 According to Article 5 of the Provision on the application of the Company Law of the People's Republic of China(II), Where the parties agree to have the company or its shareholders buy back their shares or by way of capital reduction in order to continue the business of the company, and this does not violate the mandatory provisions of laws and administrative regulations, the people's court shall recognise the validity of the agreement.

51 *Ye yuwen v Peixian Shuntian Real Estate Development Co.Ltd* (2008) Jiangsu No. 0048, civil tribunal judgment of last resort.

52 Zhou Linbin, Yu bin, "The Improvement on Capital Reduction in the Reform on Corporate Capital in China", *Journal of Sun Yat-sen University (social science edition)*, 2015, Vol.5, pp.141.

share.[53] In practice, there are several cases where the company buys back its shares because of the depressed value of its shares in the stock market.[54]

After years of practice, Chinese company law eventually modified its rules on share buyback on 26 October 2018.[55] Article 142 of the Company Law added two situations allowing share buyback: (1) the conversion of shares into convertible corporate bonds issued by a listed company and (2) a listed company may buy back its shares when it is necessary to maintain the company's value and shareholders' rights and interests. This further relaxed the restrictions on share buyback.

IV. PROSPECTS TO MODIFY THE CAPITAL MAINTENANCE DOCTRINE THROUGH GUIDING CASES

The 2013 reform only relaxed capital contribution rules, but the capital maintenance rules has not changed at all. This may result in conflicts with respect to corporate capital. According to the 2013 Company Law, China has adopted the subscribed capital system, and shareholders can make contributions in installments.[56] If the company is unable to repay its debts to creditors, will shareholders be obliged to make contributions before it is due? How can creditors be protected if shareholders refuse to make full contribution? The following discussions will provide us with an effective substitute to modify the capital maintenance rule using the guiding cases approach (prior to the amendment of the company law). In judicial practice, the court in China should not mechanically follow outdated rules on capital maintenance, but should improve the rules through guiding cases.

A. Rules on Share Buyback

Although the rules on share buyback were relaxed in 2005, restrictions remain extremely stringent. Typically, if the prescribed conditions of share buyback are not met, the court will not endorse the validity of the share buyback transaction. However, there are many

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53 Article 4 of the Guidance stipulates, if a listed company meets any of the following circumstances and the share buyback does not affect its continuing business ability, the exchange encourages it to buy back shares: (1) the stock price continues to be lower than the net assets per share; (2) the cash flow generated by business activities is continuously positive, or there is a large amount of idle funds; (3) the asset-liability ratio is significantly lower than the industry average; (4) it is unable to pay cash dividends to shareholders for a long time due to the failure to make up losses after the implementation of material assets reorganisation; (5) having the ability to pay dividends but the level of cash dividends is relatively low; (6) there is a big difference in the market pricing of a-shares, b-shares or h-shares issued, and the stock price of A certain class of shares is too low to reflect the value of the company; (7) other circumstances identified for the purpose of adapting to the development and changes of the securities market and protecting the legitimate rights and interests of investors. http://www.sse.com.cn/lawandrules/sserules/listing/stock/c/c_20150912_3985861.shtml, Site accessed on 26 January 2018.

54 For example, the listed company Handan Steel (600001) bought back its share from the stock market in 2005, the price is lower than its net assets. This was the first case in which a listed company bought back its shares.

55 See Decision of the Standing Committee of the National People's Congress on amending the Company Law of the People's Republic of China, http://www.court.gov.cn/zixun-xiangqing-57402.html, Site accessed on 21 November 2018.

56 Article 26 of the Chinese Company Law provides that the registered capital of a limited liability company shall be the capital contribution subscribed by all shareholders registered with the company registration.

situations in which it would be logical to declare share buyback transactions valid even if it does not satisfy the pre-requisite conditions. One instance would be the case where the China Securities Regulatory Commission encouraged listed companies to adopt the Employee Stock Ownership Plan (ESOP). Under this plan, listed companies would buy back its shares and then deposit these shares into ESOP. Share buyback is also widely used in Valuation Adjustment Mechanisms.[57] These circumstances do not meet prescribed conditions stipulated by company law and different courts had different outcomes on whether these transactions were valid. Finally, the Supreme People's Court in a 2010 decision,[58]affirmed the validity of a share buyback agreement between shareholders. However, the court also held that a share buyback agreement between a company and its shareholders may infringe upon the interests of the creditors, and in such cases, the transaction would be invalid.

Recently, the Supreme People's Court released guiding case No. 96[59] which allows companies to buy back its shares under the condition prescribed in the company's Articles of Association. This further relaxed the prescribed conditions of share buyback stipulated under Article 74 and Article 142 of the Company Law.

B. Rules on Distribution

The doctrine of capital maintenance requires profits to be distributed to shareholders only if certain conditions are met. According to the existing rules, profits after-tax should be used to make up losses and withdrawn only for legal reserve.[60] This regulation remained unchanged after the 2013 reform, and has resulted in confusion. First of all, it raises the question of whether the subscribed capital would be accounted for in the company's net assets. If the subscribed capital is due but not actually paid by shareholders, would it count into the company's net assets?.[61] From a legal perspective, the subscribed capital should be counted towards the company's net assets. However, from the perspective of the accountant, only the paid-up capital should be counted towards the company's net assets. Secondly, should the company distribute dividends to shareholders who have not fully paid their capital? If the shareholder fail to contribute as scheduled, is it possible for the company to refuse to distribute dividends to him or turn the dividends into contribution to the company instead? Lastly, after the 2013 reform, it has become common for shareholders to contribute in installments, but the law still requires the company

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57 Valuation Adjustment Mechanism is widely used in the contract of venture capital investment. Investor and shareholder/company often agree, if the company can not achieve a certain profit or other conditions, investor is entitled to require the shareholder/company to buy back his shares at a fixed price.

58 *Gansu Shiheng Co.Ltd v Suzhou Haifu investment Co.Ltd*, (2012)The Supreme People's Court No.11 civil tribunal judgment of retrial.

59 *Song Wenjun v Xi'an dahua catering Co. Ltd*, (2014) Shanxi No.00215 civil tribunal 2 judgment of retrial.

60 According to Article 166 of 2013 Chinese Company law, when the company distributes the after-tax profits of the current year, 10% of the profits shall be included in the company's legal reserve. If the amount of the company's accumulated legal reserve is more than 50% of the registered capital, it may not be withdrawn.

61 For example, company A's subscribed capital is 100 million, but the paid-up capital is 10 million, and it is due to contribute the remaining 90 million. If shareholders don't contribute to it on time, does it count into the company's assets?

to withdraw legal reserve from profits until it has accumulated more than 50% of the subscribed capital. Is it still necessary for the company to withdraw the legal reserve, or should it be decided by the company?

Regrettably, there is no guiding case on this matter and the court has reached different decisions even in cases where the facts are analogous.[62] It is necessary for the Supreme People's Court to unify applicable rules on dividend distribution. First, the paid-up capital is usually less than the subscribed capital, and it may be long before shareholders complete their contribution. In order to reflect the company's actual financial status and provide accurate information for creditors, only the paid-up capital should be counted towards the company's net assets, and dividends should be distributed based on the paid-up capital. Second, the shareholders' exercise of their rights should be based on their paid-up capital rather than subscribed capital. Therefore, companies should distribute dividends in proportion to the shareholder's paid-up capital. Capital which is due but not actually paid should be viewed as debt to the company, and the indebted shareholder should be obligated to contribute. Therefore, the company may convert the dividends that are ready for distribution to shareholders who have failed to fully pay their subscribed capital to the company. Finally, the legal reserve should be used to make up losses, expand business, or to increase the company's paid-up capital. As creditors no longer fully rely on corporate capital to ascertain the company's credibility, company law should not compel it to withdraw its legal reserve, this ought to be decided by the company.

Furthermore, the doctrine of capital maintenance does not prohibit all returns of capital from the company to shareholders. An example of permissible return of capital to shareholders would be the distribution of dividends. It incentivises shareholders to invest in the company. Shareholders may be disincentivised to invest in the company if they fail to receive dividends over a protracted period of time. In China, there is a large number of listed companies which do not distribute dividends to shareholders.[63] However, if the distribution rule is too strict, it may result in low efficiency in the usage of company assets. According to the existing dividend distribution rule, a company should make up for prior losses before it distributes dividends from profits to shareholders. But if the losses are too large, and cannot be made up for within a short period of time, shareholders may not receive dividends for a long time. The frustrated shareholders may simply apply for bankruptcy as a result, instead of restructuring the company to turn it into a more profitable company. Moreover, Chinese Company Law pins liability for illegal

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[62] For example, in a case made by Lanzhou intermediate people's court, one of the shareholder didn't contribute as scheduled to the company, and the company didn't distribute dividends to him. The court held it is reasonable for the company to limit the right of distribution if shareholder didn't fully contribute. See *Wang Donghai v Liu Yanchun*, (2014) Lanzhou No. 328 civil tribunal 2 judgement of last resort. However, in another case made by the Yiwu intermediate people's court, the court held the company should distribute dividend to shareholder as long as he is the shareholder of the company, no matter he contributes or not. See *Gong Hanfang v Gong Xianmu & Zhejiang Yiwu Jiaying knitting Co. Ltd*, (2018) Yiwu No.324 civil tribunal judgement of last resort.

[63] According to the statistic released by the press in 2009, there were 496 listed companies for more than 3 consecutive years without dividends, among which 107 listed companies for 9 consecutive years, and 85 listed companies for 10 consecutive years. See http://news.163.com/09/0316/06/54GNJUIN000120GU.html. Site access on 8 December 2018. The China Securities Regulatory Commission promulgated some guidance on cash dividends, such as a notice on encouraging listed companies to merge and restructure, cash dividends and share buybacks in 2015, and thus improved slightly in the cash dividends.

or improper dividend distribution. If dividends are illegally or improperly distributed to shareholders, it would be returned to the company.[64] Therefore, it is important for the court to relax the conditions on dividend distribution by using guiding cases before the Company Law is amended. [65]

C. Rules on Capital Reduction

According to company law, companies should follow a series of procedures when reducing its registered capital.[66] But there is no liability rule on capital reduction. If a company does not follow the procedure on capital reduction, for example, not informing creditor in most cases, who should be responsible for the illegal capital reduction? Rules on capital reduction have been criticised theoretically and practically for a long time.

Rules on capital reduction have became more complicated after the 2013 reform. For instance, if creditors disagree with the resolution on capital reduction, would the creditors be able to compel the company to repay its debts or provide guarantees? Furthermore, should shareholders be held liable for illegal capital reduction? In other cases, if the company decides to reduce its capital at the time when the capital contributions from shareholders is due, would capital reduction be effective? The above questions reflect the conflicts between capital reduction and capital contribution after the reform. Rules on capital reduction need to be revised according to the modifications on company contribution rules. But before the modification on capital reduction, we may clarify and unify the applicable rules of capital reduction through guiding cases.

When we examine cases related to capital reduction, a number of rules can be drawn: (1) the 'capital' in 'capital reduction' refers to subscribed capital, not paid-up capital because after the 2013 reform, the company only needs to register its subscribed capital, the paid-up capital is reported in its annual report; (2) if a company illegally reduces its capital, court would usually holds that the capital reduction is valid. With regard to the liability rule of illegal capital reduction, the Supreme People's Court released a guiding case in the 2016 Bulletin, holding that illegal capital reduction is similar to illegal capital withdrawal, and should be decided according to Article 14 of the Provisions on the Application of the Company Law of People's Republic of China (III). Such application would see the beneficial shareholders bearing the supplementary liability to pay off the

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64 According to Article 166 of the 2013 Chinese Company law, where the shareholders' meeting or the board of directors, in violation of the provisions on distribution, and distribute profits to shareholders before the company makes up the losses and withdraws the legal reserve, the shareholders shall return the profits distributed in violation of the provisions to the company.

65 Some of the jurisdictions adopt the insolvency statement, which requires the shareholder or the management give statement that, if company cannot pay back the debts on time after distribution/capital reduction, they will bear the liability to pay back the debts for the creditors.

66 Article 177 of the 2013 Chinese Company law provides that, when a company needs to reduce its registered capital, it must prepare a balance sheet and a list of assets. The company shall, within 10 days from the date of making the decision to reduce its registered capital, notify the creditors and publish the notice in a newspaper within 30 days. The creditor shall, within 30 days from the date of receipt of the notice, and within 45 days from the date of the announcement, if the notice is not received, have the right to require the company to pay off its debts or provide the corresponding guarantee.

debts within the scope of capital reduction.[67] Although some of the courts are of similar opinion, they held that the decision should be made in accordance with Article 13 of the same Provision[68] instead.[69] Besides, some of the courts held that illegal capital reduction is different from illegal withdrawal of capital, and shareholder should not assume supplementary liability.[70] To date, there is no unified applicable rule.

What about illegal subscribed capital reduction? In a decision made by a lower people's court, where a shareholder has failed to contribute as scheduled, and the company illegally reduced its registered capital, shareholders should bear supplementary liability to pay off the debts within the scope of capital reduction.[71] Unfortunately, two problems remain unsolved in this case. First, the above decision is made by different courts and there is no guiding cases which has *de facto* binding effect on the other courts. Second, there is no case regarding the liability of illegal capital reduction for shareholders if the subscription period has not expired, and this remains controvesial both in theory and in practical application.

In order to clarify and unify the applicable rules on capital reduction, it is necessary for the PRC Supreme People's Court to release guiding cases before the amendment of the company law.

CONCLUSION

As the understanding of capital maintenance doctrine has evolved, among other things, to prohibit shareholders having undue priority in securing their interests, some capital maintenance rules have become outdated resulting in low efficiency and usage of corporate capital. Corporate capital is no longer the only factor creditors utilise to assess the credibility of the company. Though the 2013 reform is a positive step in clarifying the existing law, it is not comprehensive enough and it also generates conflicts between capital contribution rules and capital maintenance rules. It reduces the ex-ante information asymmetry between the company and its creditors, but the ex-post information asymmetry has yet to be fundamentally solved. Therefore, the capital maintenance doctrine is considered to be necessary in protecting creditors.

The guiding cases by the PRC Supreme Court (as discussed above) is a viable approach to solving the problems in practice. The guiding cases approach has been proven

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67 According to Article 14 of Provisions on the application of the Company Law of People's Republic of China (III), where the creditors of the company request the shareholders who have withdrawn their capital to bear supplementary compensation liability for the part of the company's debts which cannot be paid off within the scope of the principal and interest of the withdrawal of capital, the people's court shall support the claim.

68 Article 13 of Provisions on the application of the Company Law of People's Republic of China (III) provides that where creditors of the company request shareholders who have not contributed or have not fully contribute to bear supplementary compensation liability for the part of the company's debt that cannot be paid off, the court shall support the claim.

69 *Changshu branch of Agricultural Bank of China v Suzhou kexin non-financing guarantee Co. Ltd & Li Chao*, (2016) Jiangsu Changshu No.8409 civil tribunal judgment of first resort.

70 *Guangdong Qiulu industrial Co.Ltd v Taihua Gaoxin ranzheng (Jiaxing) Co.Ltd*, (2017) Jiaxing No.405 civil tribunal judgment of last resort.

71 *Shenzhen huacheng industrial Co. Ltd v Feng Yao & Huang Weiming*, (2016) Nanchang Donghu, No.4862, civil tribunal judgment of first resort.

to be an efficient measure in China. It has *de facto* binding effect, and may be potentially useful in supplementing written law. It is suggested that the capital maintenance rules should be modified before the amendment of the company law. Further, it is suggested that China may consider relaxing the capital maintenance rules by using guiding cases. For example, share buyback in circumstances beyond the prescribed conditions should be allowed and the stringent conditions restricting dividend distribution should also be relaxed. It would also be helpful to clarify and unify the liability rule on capital reduction, especially the liability rule for illegal subscribed capital reduction.

Multiple Nationalities in Refugee Law: Toward a Practical Approach

Ryan Corbett*

Abstract

The 1951 Convention Relating to the Status of Refugees (Refugee Convention), a treaty intended to protect some of the most vulnerable individuals in the world, has resulted in the exclusion of persons from refugee status due to a provision detailing citizenship requirements. According to the Refugee Convention, individuals who hold multiple nationalities must seek the protection of their other state(s) of nationality, or demonstrate why they cannot, before being able to be granted refugee status in another state. This paper will explore this provision of the Refugee Convention and the reasoning behind it, as well as survey issues that have arisen from its application over the past several decades, in order to recommend a more uniform application of the provision with an eye to the object and purpose of the treaty. The state application of Article 1(A)(2) can have serious implications for refugees fleeing the violence in Syria, North Korea, and countless other countries. We must take seriously interpretations of treaty law that are logical in theory, but lead to violations of rights and incongruous decisions in practice. This paper proposes an alternative view of effective citizenship and recommends a particular application of the Refugee Convention and understanding of citizenship.

Keywords: Refugee, Migration, Citizenship, Nationality.

I. INTRODUCTION

The 1951 Refugee Convention, a treaty that protects some of the most vulnerable individuals in the world, has resulted in the exclusion of persons from refugee status due to a provision detailing citizenship requirements. According to the Refugee Convention, individuals who hold multiple citizenships must seek the protection of their other state(s) of citizenship, or demonstrate why they cannot, before being granted refugee status in another state.[1] This article will explore this provision of the Refugee Convention and the reasoning behind it, as well as survey issues that have arisen from its application over the past several decades, in order to recommend a more uniform application of the provision with an eye to protecting some of the world's most vulnerable people.

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1 Convention Relating to the Status of Refugees Article 1(A)(2), July 28, 1951, 19 U.S.T. 6259, 189 U.N.T.S. 150 [hereinafter 1951 Refugee Convention].

First, this paper discusses the relevant provisions of the Refugee Convention, their initial purpose, and the issues that have arisen in their application in the past several decades in particular. Next, this paper will turn to examining the concept of citizenship in international law. This paper will argue that individuals holding a second, but ineffective, citizenship should not be excluded from refugee status on this ground alone. Third, this paper will explore two applications of this provision of the Refugee Convention by different states. These situations illuminate a spectrum of state interpretation of the Refugee Convention. North Koreans applying for refugee status in Australia often have been excluded from refugee status due to South Korea's act of entitling all North Koreans to South Korean citizenship. In addition, East Timorese asylum seekers have been systematically excluded from refugee status due to Portugal's decision to entitle East Timorese to Portuguese citizenship, a remnant of colonial rule. These state applications of the Refugee Convention have led to a non-uniform adjudication of refugee claims of dual nationals.

Using these two situations as a backdrop, this paper will conclude by presenting suggestions for the application of the Refugee Convention. States should adopt a new standard for ineffective citizenship, influenced by our understanding of what citizenship means today. Ineffective citizenship as described in the Handbook on Procedures and Criteria for Determining Refugee Status Under the 1951 Convention and the 1967 Protocol Relating to the Status of Refugees (UNHCR guidance) classifies very few situations of citizenship as such. The term 'ineffective citizenship' for the purposes of exclusion from the Refugee Convention should include situations in which a sovereign forces citizenship on groups with a tenuous 'genuine link' to the sovereign. Moreover, we cannot conflate the ability to acquire citizenship with the possession of citizenship. Third, we must look at the geopolitical realities of certain situations and understand that the imposition of citizenship is inappropriate and ought not to be considered effective. Finally, individuals excluded due to having dual citizenship should never be *refouled*, which means, returned to the country in which they fear persecution. If the individual is being excluded because he or she can seek protection of another state, the individual ought to be sent to the second state in which he holds nationality. Through a highlighting of the issues dual nationals face, as well as that of the lacuna UNHCR guidance leaves with respect to this problem, I hope to fill in the gap and provide guidance to states that will ensure states act in light of the humanitarian purpose of the Refugee Convention.

II. HISTORY OF THE REFUGEE CONVENTION

The newly-established United Nations General Assembly adopted the Refugee Convention in 1951 in response to the atrocities of World War II.[2] Hitler's rule resulted in millions of refugees fleeing their home countries, with no international legal instrument guiding states' responses to these people. In an effort to ensure something like World War II was never repeated, the newly formed United Nations drafted several international instruments,

[2] *Ibid.*

including the Refugee Convention.[3] The Refugee Convention was intended to protect some of the world's most vulnerable people fleeing atrocities and ensure that they would not be forced to return to a place where they were persecuted.[4]

Every treaty is thought to have an object and purpose, which states parties ought not act to frustrate. 'Object and purpose' is a term of art is discussed in the Vienna Convention on the Law of Treaties (VCLT), the international treaty that discusses how states should interpret and carry out treaties to which they are states parties.[5] Though not defined in the VCLT, the term object and purpose is generally understood to mean the 'essential goals' of a treaty.[6] The VCLT notes that a state is "obliged to refrain from acts which would defeat the object and purpose of a treaty" when it is a state party or it has expressed consent to be bound by the treaty.[7] Though debated, the object and purpose of the Refugee Convention is thought to be humanitarian, with an interest in protecting refugees and safeguarding their rights.[8] Therefore, states parties to the Refugee Convention must not act in any way to defeat the humanitarian object and purpose of the treaty.

The Refugee Convention defines a refugee as an individual who:

> [a]s a result of the events occurring before 1 January 1951 and owing to a well-founded fear of being persecuted for reasons of race, religion, nationality, membership of a particular social group or political opinion, is outside the country of his nationality and is unable or, owing to such a fear, is unwilling to avail himself of the protection of that country . . . .[9]

The Convention's 1967 Protocol (Protocol) expanded this definition to include those fleeing from events occurring any time after 1 January 1951.[10] Because no provision other than this temporal extension was added in the 1967 Protocol, I will refer to both the 1951 Refugee Convention and its 1967 Protocol as the Refugee Convention in this paper.

In addition to defining those included as refugees in international law, the Refugee Convention includes several clauses that exclude certain groups of individuals from refugee status. The second paragraph of Article 1(A)(2) excludes from refugee status those with multiple nationalities who can avail themselves of the protection of their second state of nationality, noting that:

> In the case of a person who has more than one nationality, the term 'country of his nationality' shall mean each of the countries of which he is a national, and a person shall not be deemed to be lacking the protection of the country of his nationality

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3 *Ibid*.

4 *Id.* at Art.33.

5 Vienna Convention on the Law of Treaties (23 May 1969).

6 David S. Jonas & Thomas N. Saunders, "The Object and Purpose of a Treaty: Three Interpretive Methods", *Vanderbilt Journal of Transnational Law*, 2010, Vol. 43, pp.567.

7 *Supra* n 5, at Art. 18.

8 James C. Hathaway & Michelle Foster, "The Law of Refugee Status", *European Journal of International Law,* 2015, Vol. 26, p.54.

9 *Ibid.* at Art. 1(A)(2).

10 1967 Protocol Relating to the Status of Refugees, 31 January 1967.

> if, without any valid reason based on well-founded fear, he has not availed himself of the protection of the countries of which he is a national.[11]

The Refugee Convention excludes those, or allows states to exclude those, who have a second nationality from international refugee protection. This Article of the Refugee Convention does not explicitly state what must happen if a person is determined to be ineligible for international protection.

However, Article 33 of the Refugee Convention notes that states may not *refoule* a refugee to any place where his life or freedom is at risk.[12] This means that a state cannot return a refugee to a place where they are at risk of persecution. If an individual is determined to be ineligible for refugee protection due to his having a second citizenship, a state is still prohibited from returning that person to his home country or a place he would be persecuted. This ensures that refugees will still be protected, even if an individual state is not required to act to protect him.

The British delegate first proposed the language on dual nationality in the drafting of the Refugee Convention, which "reflected the desire of many states to limit their obligations toward refugees".[13] Given the reality of World War II, states wanted to strike a balance between protecting vulnerable individuals and abdicating responsibility for large refugee influxes that they could not support. This clause was aimed at striking just this balance by excluding a group of individuals who could seek protection elsewhere.[14] Moreover, Article 1(A)(2) was included in the Refugee Convention because of the understanding of the role of states at the time. Usually, states "have no general obligation to admit foreigners or offer them protection."[15] Consequently, carving out as narrow an exception to this general premise as possible "required the strictest limitation that there be an initial reliance on national protection."[16] This imposed a new obligation on states in a way that sought to inflict the smallest burden possible.

At the time of the drafting of the Refugee Convention, dual citizenship was not as commonplace as it is today. In 1951, most states had laws banning their citizens from holding nationality in another state,[17] meaning the population potentially affected by this provision of the Refugee Convention was incredibly small. With time, dual citizenship became more common, as many individuals were granted multiple citizenships through either a *jus sanguinis* or *jus soli* theory of citizenship due to increased globalisation.[18] These changing national laws and increased dual citizenship resulted in challenges in the

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11 *Supra* n 1, at Art. 1(A)(2).

12 *Ibid.* at Article 33.

13 Jon Bauer, "Multiple Nationality and Refugees*", Vanderbilt Journal of Transnational Law,* 2014, Vol. 47, p. 917.

14 *Supra* n13, at p. 917.

15 Mark Sidhom, "*Jong Kim Koe v Minister for Immigration and Multicultural Affairs*: Federal Court Loses Sight of the Purpose of the Refugee Convention*", Sydney Law Review*, 1998, Vol. 20, p. 319.

16 *Ibid.*

17 Tanja Brondsted Sejersen, "I Vow to Thee My Countries': The Expansion of Dual Citizenship in the 21st Century," *International Migration Review*, 2008, Vol. 42, p. 534.

18 *Ibid.*

adjudication of refugee claims, the scope and particulars of which could not have been anticipated at the time of the drafting of the Convention.[19]

This has created practical problems for individuals fleeing persecution in their home countries. An individual does not always possess a second citizenship by choice or consent; "Territorial disputes or state succession can result in entire populations acquiring dual citizenship through no doing of their own."[20] Of course, lack of consent or choice on its own is not necessarily indicative of a problematic form of citizenship; most individuals in the world have citizenship at birth due to neither consent nor choice. However, the lack of consent and choice, in addition to actions, or inactions, taken by a sovereign raise questions about certain citizenships that we ought to find ineffective for the purposes of the Refugee Convention.

III. THE CONCEPT OF CITIZENSHIP

In order to understand Article 1(A)(2) of the Refugee Convention, its application, and the problems that abound in its application, it is first necessary to discuss what the term "nationality" or "citizenship" means.[21]

A. *What is Nationality?*

Nationality in international law is "very vague and imprecisely defined."[22] Several international court cases examined the concept of nationality in the twentieth century. In 1923, the Permanent Court of International Justice, the predecessor to the International Court of Justice, advised that nationality is within the purview of the domestic law of states, rather than that of international law.[23] States have wide latitude to determine who its nationals are, while international law places minimal limits on that discretion.[24] However, international law "neither contains nor proscribes certain criteria for acquisition and loss of nationality."[25]

Three decades later, in 1955, the International Court of Justice in *Nottebohm* noted that nationality must be based on "a social fact of attachment, a genuine connection of existence, interests and sentiments, together with the existence of reciprocal rights and duties."[26] This genuine connection suggests that an individual who possesses nationality "is in fact more closely connected with the population of the state conferring nationality than with that of any other state."[27] The idea of a national having a connection to a

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19 *Ibid.*

20 *Supra* n13, at p. 917.

21 For the purposes of this article, I put aside the discussion of the difference of nationality and citizenship and use both terms to refer to the same concept.

22 *Supra* n 15, at p. 321.

23 Nationality Decrees Issued in Tunis and Morocco on Nov. 8th, 1921, Advisory Opinion, 1923 P.C.I.J. (ser. B) No. 4 (Feb. 7.) at p. 24.

24 Oliver Dörr, "Nationality*", Max Planck Encyclopedia of Public International Law,* Nov. 2006, para. 4.

25 *Ibid.*

26 Nottebohm Case (*Liechtenstein v. Guatemala*) 1955 I.C.J. No. 18, at 6 (Apr. 6, 1955).

27 *Ibid.*

country of nationality in order for that nationality to be genuine seems to be the only clear requirement for nationality in international law. With dual citizenship, an individual likely will have a strong and significant connection with more than one state. However, it follows that the individual must still have a strong connection with both states in question in order for those citizenships to be genuine.

International human rights treaties address the actions of states in determining whom it calls, or refuses to call, citizens.[28] In 1948, the Universal Declaration of Human Rights was the first non-binding international instrument to address the right to nationality and deprivation thereof. It stated that "'[e]veryone has a right to nationality" and "[n]o one shall be arbitrarily deprived of his nationality nor denied the right to change his nationality."[29] Notably, this treaty imposed a negative obligation upon states, meaning rights upon which they must not infringe, rather than a positive obligation, meaning rights that states must provide. In 1961, the Convention on the Reduction of Statelessness noted that:

> a Contracting State shall grant its nationality to a person born in its territory who would otherwise be stateless. Such nationality shall be granted (a) at birth, by operation of law, or (b) upon an application being lodged with the appropriate authority, by or on behalf of the person concerned, in the manner proscribed by national law.[30]

This treaty took steps toward ensuring individuals will be granted nationality in at least one state. In addition, this treaty imposed obligations on states to act, rather than just to refrain from violating rights.

As it is for each state to determine who are its own citizens, the existence of a domestic law is pertinent as it "creates a *very strong presumption* both that the individual possesses that state's nationality as a matter of its internal law and that that nationality is to be acknowledged for international purposes."[31] As such, these domestic laws and determinations are rejected only "in 'exceptional cases' with the deciding factor being the extent to which the attribution of nationality infringes on the rights of the state."[32] In addition, the domestic determination can be rejected when such a determination violates international treaties, such as those discussed above.

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[28] *Supra* n 24, at para. 6. Many treaties address discrimination in the conferring of citizenship. The Convention on the Elimination of All Forms of Racial Discrimination forbids racial discrimination in the conferring of citizenship. International Convention on the Elimination of All Forms of Racial Discrimination, 7 March 1966. In addition, the European Convention on Nationality forbids discrimination based on sex and religion. Art. 5(1), European Convention on Nationality, ETS 166 (6 November 1997). The Convention on the Elimination of All Forms of Discrimination against Women, known as CEDAW, requires that states provide women with the same rights to citizenship as men. Art. 9(1), Convention on the Elimination of All Forms of Discrimination against Women, 18 December 1979.

[29] Universal Declaration of Human Rights, G.A. Res. 217A (III), U.N. Doc. A/810, at 71 (1948).

[30] Art. 1, 1961 Convention on the Reduction of Statelessness.

[31] *Supra* n 15, at p.321 (emphasis in original).

[32] *Ibid.*

The definition of nationality is important because nationality carries with it certain legal consequences, "which are basically an expression of the fact that by virtue of its nationality the individual is attached to a State, more than to any other."[33] Nationality has particular legal consequences for the individuals who possess it with regard to jurisdiction, admission, and diplomatic protection.[34] Jurisdiction refers to the ability of a state to exercise its power to call its nationals to its courts, and serves as the basis for the ability of states to protect their own nationals.[35] The duty of admission refers to a state's obligation to allow those holding its citizenship to enter its borders.[36] Lastly, diplomatic protection refers to a state's ability to hold another state responsible for the violation of international law that affects its citizens; in other words, this refers to a state's protection of its citizens through diplomatic measures.[37]

In addition, a state grants its nationals certain rights that it does not grant to non-nationals. Scholars have considered citizenship to determine "the scope of application of basic rights and obligations of states vis-à-vis other states and the international community."[38] Moreover, nationality is a requirement for the domestic "exercise of political rights and claims to protection and correlate duties, such as military or civil service obligations, which may, however, vary according to national law."[39] Thus, an individual can be said to be a national of a state in which he can exercise certain rights and is bound by obligations consistent with nationality in that state.

Generally, citizenship requires a genuine link between the individual and the state in question. Accordingly, "[t]he lack of a genuine link has been invoked as a reason against the granting of citizenship status . . . and as a justification for deprivation."[40] Conversely, "genuine links can also be invoked positively as a reason for awarding citizenship or as a reason against its deprivation."[41] There is no conclusive explanation of what constitutes a genuine link, though several scholars, treaties, and domestic courts have contended with this concept.

B. *What is Ineffective Nationality?*

The question of a genuine link between an individual and a state has also been raised when addressing the concept of ineffective nationality, or nationality in name only. Ineffective nationality stands in contrast with effective nationality, or one that affords the individual the protection of the sovereign; ineffective nationality does not afford the holder any such rights and is not regarded as a genuine nationality in light of this fact.

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33 *Supra* note 24 at para.42.

34 *Ibid.*

35 *Ibid.* at paras. 43-49.

36 *Ibid.* at paras. 50-51.

37 *Ibid.* at paras. 52-58.

38 *Supra* n 27, at p. 1.

39 *Ibid.*

40 Rainer Baubock & Vesco Paskalev, "Cutting Genuine Links: A Normative Analysis of Citizenship Deprivation", *Georgetown Immigration Journal*, 2015, Vol. 30, pp.100-01.

41 *Ibid.* at pp.100-01.

The UNHCR guidance suggests that only effective nationalities should be considered to be nationalities; ineffective nationalities should not exclude an individual from international refugee protection;[42] Further, the UNHCR guidance distinguishes "between the possession of a nationality in the legal sense and the availability of protection by the country concerned."[43] In cases where the nationality in question "does not entail the protection normally granted to nationals," that nationality may be deemed to be ineffective, meaning one that does not constitute a legitimate nationality.[44] The United Nations High Commissioner for Refugees, Handbook and Guidelines on Procedures and Criteria for Determining Refugee Status (UNHCR Handbook) notes that "as a rule, there should have been a request for, and refusal of, protection before it can be established that a given nationality is ineffective."[45] The individual must have requested and been refused protection of a state before that nationality is deemed ineffective.[46] If an individual holds a second nationality that is deemed ineffective, that individual would not be excluded from refugee status. However, under all other circumstances, the nationality of an individual is considered to be effective nationality and bars an individual from being granted refugee status according to the Refugee Convention.

Domestic courts have also considered the question of ineffective nationality. For example, in deciding whether Portuguese nationality is effective, Federal Courts in Australia have considered factors such as:

> whether Portugal would offer [an individual] protection in Australia or only in Portugal, whether he was reasonably able to travel to Portugal to obtain protection, whether he would be admitted to Portugal on arrival, and the administrative procedures [an individual] would need to undertake to satisfy the Portuguese authorities as to his Portuguese nationality.[47]

However, there is no clear list of criteria in international law that guides a national court or legislature in determining when a nationality ought to be deemed ineffective.

In addition, scholars have weighed in on the concept of ineffective nationality. James Hathaway, a leading scholar on refugee law, argues that in order for nationality to be effective, rather than formal, a state must be "willing to afford protection against return [of the individual] to the country of persecution."[48] In addition, Hathaway notes that "[w]hile it is appropriate to presume a willingness on the part of a country of nationality to protect in the absence of evidence to the contrary, facts that call into question the existence of a

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42 United Nations High Commissioner for Refugees, *Handbook and Guidelines on Procedures and Criteria for Determining Refugee Status,* December 2011, para.107.

43 *Ibid*.

44 *Ibid.* at para. 107.

45 *Ibid.*

46 *Ibid.*

47 *Supra* n15, at p. 325.

48 James C. Hathaway & Michelle Foster, *The Law of Refugee Status,* 2nd Ed., Cambridge University Press, 2014, p.59.

basic protection against return must be carefully assessed."[49] Here, he raises the question of whether other criteria ought to be considered when determining whether an individual holds nationality in fact or in name only.

UNHCR guidance, state practice, and scholarly opinions touch on the idea of ineffective nationality, but refer to it only as including a state refusing to grant protection to an individual when that protection is sought. However, this is a very limited category of problematic citizenships that would be considered ineffective, leaving all other citizenships to be effective despite the problems they may have.

While various tests can be used, it seems that a citizenship is deemed ineffective where the state cannot provide rights and protections to that person both in and outside its territory, where the individual may have to go through extensive procedures to be categorised as a citizen with the country, and where the state has refused help once sought. This begs the question: is this the only time we ought to consider a nationality ineffective, or ought the principle be expanded in order to adequately capture the system of protection the Refugee Convention sought to establish with an understanding of modern-day political realities? Given today's political realities, other considerations ought to be made when deciding whether a citizenship is effective.

IV. STATE INTERPRETATIONS OF ARTICLE 1(A)(2)

Because states are the primary entities adjudicating refugee claims,[50] it is important to survey how states interpret and apply the dual nationality provision of the Refugee Convention. Below are two examples of state practice surrounding this principle of the Convention, which present a spectrum of state practices. Each of these is intended to be illustrative, though not conclusively representative of the models of this provision as used by all states.

A. Australia's Interpretation for East Timorese

East Timorese encountered substantial problems in applying for refugee status in Australia. From about 1515 until 1975, Portugal held East Timor as a colony.[51] In 1975, Portugal began to decolonise East Timor, leading Indonesia to invade and annex the land.[52] Australia formally recognised this annexation in 1979.[53] However, the native East Timorese rejected Indonesia's claim to sovereignty.[54] There was a particularly violent period of several months in 1999 where Indonesia "deliberately engineered

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49 *Ibid.* at p. 59; *Supra* n 15, at p. 325.

50 In some countries, such as Egypt, UNHCR is the body adjudicating claims of refugees.

51 Christine Chinkin, "East Timor: A Failure of Decolonization*"*, *Australia Yearbook of International Law,* 1999, Vol. 20, p. 37.

52 Barbara Ann Hocking & Scott Guy, "East Timor as a Case Study on the Emergence of International Humanitarian Law in the Australian-Pacific Region*", Asia Pacific Yearbook of International Humanitarian Law*, 2006, Vol. 2, p.74.

53 Ryszard Piotrowicz, "Refugee Status and Multiple Nationality in the Indonesian Archipelago: Is There a Timor Gap?*"*, *International Journal of Refugee Law,* 1996, Vol. 8, p. 320.

54 *Ibid.*

civil disorder."[55] Conflict between the native peoples and the Indonesian forces resulted in clashes and political persecution, which led some East Timorese to seek asylum in surrounding countries, including in Australia.[56] During this period of Indonesian control, Portugal rejected Indonesia's claim over the land and insisted that East Timorese should be entitled to seek self-determination.[57]

Portuguese law suggests that those born in East Timor before 1976 are entitled to Portuguese citizenship. Article 4 of the Portuguese Constitution of 1976 noted that "all persons are Portuguese Citizens who are considered as such by law or under an international convention."[58] According to Portuguese citizenship law, those born "of a Portuguese mother or father born in Portuguese territory" are "Portuguese by origin".[59] Consequently, those born to a local mother or father in East Timor before Portugal's exit from East Timor would be Portuguese by origin. In addition, those born "of a Portuguese mother or father born abroad [who] have their birth registered at the Portuguese civil registry or [who] declare that they want to be Portuguese" are likewise categorised as Portuguese by origin.[60] According to this law, individuals born after Portugal's exit from East Timor could be considered entitled to Portuguese citizenship if their parents registered their birth or if they declared their desire to be Portuguese. Under this law, affirmative steps are required in order for a person born in East Timor after 1975 to be granted Portuguese citizenship. In addition, those born in Portuguese territory to a foreign father were also entitled to Portuguese citizenship.[61] As discussed above, until 1975 East Timor was Portuguese territory, and all those born in East Timor were entitled to Portuguese citizenship. However, it is important to note that those born in East Timor before Portugal's exit are *entitled* to Portuguese citizenship automatically, though not *granted* this status automatically.[62]

This previously has raised interesting questions in the context of East Timorese applying for refugee status in Australia. In the 1990s, the Australian government took the view that East Timorese ought to seek the protection of Portugal and be refused before being entitled to apply for refugee status elsewhere.[63] In one notable case, the Refugee Review Tribunal examined the refugee claims of three children born in East Timor between 1973 and 1976. The Tribunal found that there was a continuing link between Portugal and the people of East Timor before the Indonesian invasion, and concluded that Portugal could lawfully and reasonably treat the East Timorese as its citizens.[64] It

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55 *Supra* n 52, at p.74.

56 *Supra* n 53, at p.320.

57 *Supra* n 52, at pp.75-76.

58 Constitution of Portugal (1975), Art. 4.

59 Portuguese Nationality Act, Law 37/81, Art. 1(1)(a) (2006).

60 *Ibid.* at Art. 1(1)(c).

61 Law No. 2098 (July 29, 1959), Clause 1(I)(I) (Port.)

62 "Portuguese Nationality Law"*, World Heritage Encyclopedia,* http://www.worldlibrary.org/articles /portuguese_nationality_law. Site accessed 9 August 2018.

63 Kerry Carrington et al., "The East Timorese Asylum Seekers: Legal Issues and Policy Implications Ten Years On*", Information, Analysis and Advice for the Parliament*, 2002-2003, Vol. 17 https://www.aph.gov.au/binaries/library/pubs/cib/2002-03/03cib17.pdf. Site accessed 20 January 2019.

64 Refugee Review Tribunal, RRTA 1190 (29 May 1995).

noted that the international community recognised Portugal as the administrator of East Timor, and until 1975 Portugal was in control of East Timor.[65] Consequently, the Tribunal found that the two children born in 1973 and 1975, respectively, were Portuguese citizens, while the child born in 1976 after Indonesian annexation of East Timor was not since Portugal lacked control over East Timor at the time the child was born.[66] In this case, those children who were Portuguese citizens were not entitled to refugee status, while the youngest child was entitled to refugee status.[67] The Tribunal recognised that these children may not be able to establish Portuguese citizenship, but that they were required to attempt to do so before Australia would provide refugee protection to them.[68]

One year later, the Refugee Tribunal considered Article 1(A)(2)'s citizenship provision and concluded that East Timorese were Portuguese citizens. The defense argued that East Timorese are only conditionally eligible for Portuguese citizenship and are required to apply and produce a lot of paperwork in order to obtain this citizenship.[69] In addition, the defense argued that the individual applying for refugee protection did not want to become a Portuguese citizen and could not be compelled to try to adopt Portuguese citizenship.[70] The Tribunal rejected this argument, stressing that there was a genuine connection between the applicant and Portugal at his birth when Portugal administered East Timor, and rejecting the applicant's desires regarding Portuguese nationality as irrelevant.[71] The Tribunal consequently rejected the individual's application for refugee status in Australia due to his having Portuguese citizenship.

The Australian Government maintained that East Timorese born during the Portuguese administration of the area are Portuguese citizens and therefore not entitled to refugee status in Australia.[72] This is the case regardless of the actions or desires of the applicant, and regardless of his or her connections, or lack thereof, to Portugal.[73]

The Federal Court of Australia overturned this presumption of Portuguese citizenship in three separate court cases. In *Jong Kim Koe* in 1997, the court stated that while the individual was granted Portuguese citizenship upon his birth in 1973 in East Timor, the Tribunal must consider whether that citizenship is effective or not.[74] The Court stated that the Tribunal should use factors such as whether the individual could enter Portugal legally without a visa, whether he could be deported to East Timor, and whether he would have to engage in a long process to acquire an identity card.[75] The Court noted that only where a

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65 *Ibid.*

66 *Ibid.*

67 *Ibid.*

68 *Ibid.*

69 Refugee Review Tribunal, RRTA 220 (7 February 1996).

70 *Ibid.*

71 *Ibid.*

72 James Cotton, "East Timor and Australia: Twenty-five Years of the Policy Debate", *Nautilus Institute,* Sept. 21, 1999, http://nautilus.org/napsnet/napsnet-special-reports/east-timor-and-australia-twenty-five-years-of-the-policy-debate/. Site accessed 10 September 2018.

73 *Ibid.*

74 *Jong Kim Koe v Minister for Immigration & Multicultural Affairs* 306 FCA (2 May 1997) (Austl.).

75 *Ibid.*

citizenship is determined to be effective can it be used as a bar from refugee protection.[76] In *Lay Kon Tji* in 1998, the Court held that "…'effective nationality' is a nationality that provides all of the protection and rights to which a national is entitled to receive under customary or conventional international law."[77] The Court determined that the Portuguese citizenship that East Timorese have is ineffective, due to the fact that if an East Timorese person does not wish to be Portuguese he will not be afforded the same protections as other Portuguese citizens.[78] In addition, if an East Timorese person is deported to Portugal, he likely would not be given the same protections as Portuguese citizens until he undertakes a process to obtain citizenship documents.[79] In 2000, the Federal Court again overturned a Tribunal decision in *SRRP and Minister for Immigration and Multicultural Affairs*. The Court noted that Portugal does not offer effective protection to East Timorese individuals in the form of travel documents or right to freely enter the country.[80] Because Portugal does not provide East Timorese with rights or protections against being returned to East Timor, the Court determined that this citizenship was ineffective.[81] The Court again concluded that ineffective citizenship cannot prohibit refugee protection.[82]

In response, Australian Government passed a law in 1999 stating that only the domestic law of the country concerned can be used in determining the citizenship of an individual.[83] In an effort to limit the reach of the decisions of the Full Federal Court, the legislature passed a far more restrictive approach to second nationality analysis.[84] This Border Protection Legislation allowed the Tribunal to reject applications for refugee status, and allowed the government to deport individuals to East Timor after their applications for refugee status were rejected.

In 2002, soon after these cases and the passage of the Border Protection Legislation, East Timor achieved independence from Indonesia. This resulted in an extreme decrease in East Timorese asylum seekers entering Australia.[85] In addition, the change in circumstance meant that Australia began to review these cases in a different light. After 2002, Australia was able to justify the repatriation of most applicants from East Timor because they feared persecution from Indonesian forces, who were no longer present in the country.[86] However, Australia's approach to the citizenship analysis has continued to affect other groups of refugees.

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76 *Ibid.*

77 *Lay Kon Tji v Minister for Immigration & Ethnic Affairs* 1380 FCA (Oct. 20, 1998) (Austl.).

78 *Ibid.*

79 *Ibid.*

80 *SRPP and Minister for Immigration and Multicultural Affairs* AATA 878 (5 October 2000) (Austl.).

81 *Ibid.*

82 *Ibid.*

83 Border Protection Legislation Amendment Act 1999, Item 91N(6) (Austl.).

84 Andrew Wolman, "North Korean Asylum Seekers and Dual Nationality*", International Journal of Refugee Law,* 2012, Vol. 24, p. 813.

85 *Supra* n 63, at p. 15.

86 *Ibid.*

B. The UK's Interpretation for North Koreans[87]

The Democratic People's Republic of Korea, otherwise known as North Korea, is consistently considered to be one of the worst human rights violators in the world.[88] The Government has employed such tactics as arbitrary arrests and detentions, restricted media and civil society, and enforced disappearances.[89] This systematic violation of the rights of North Korean nationals resulted in 'tens of thousands of North Koreans' fleeing to nearby states.[90] Most first make their way to China and later move to other countries, with many going to South Korea.[91] However, for various reasons, many instead move from China to other countries to apply for refugee status there.

South Korean law seems to indicate that North Koreans are given automatic citizenship to South Korea. The 1948 South Korean Constitution states that the territory of South Korea "shall consist of the Korean peninsula and its adjacent islands," which includes the territory currently known as North Korea.[92] The South Korean Nationality Act states that anyone born to a parent who holds South Korean nationality, or born on the Korean peninsula, holds South Korean nationality.[93] Scholars, courts, and other states "have accepted that, in principle, provided an individual born in North Korea is not descended from two foreign (non- North or South Korean) parents, he or she would also be a South Korean national from birth."[94]

In order to be protected by South Korea and to formally be recognised as South Korean, an individual must apply for protection at a South Korean diplomatic or consular mission abroad.[95] The head of the respective mission will inform the Minister of National Unification and the Director of the Agency for National Security Planning.[96] The Minister will then make a decision on the admissibility of the application and subsequently inform the head of the relevant diplomatic or consular mission.[97] Once the decision has been made and the relevant individuals informed, the individual will be provided protection and identity documents.[98] The law states no time limitation on how long this process may take.

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87 In addition, Australian Refugee Review Tribunals "have regularly claimed that North Korean asylum applicants are, in fact, already South Korean nationals, and therefore do not meet the criteria for being considered refugees under article 1(A)(2) of the Refugee Convention." *Supra* n 84, at p. 799.

88 "World Report 2017: North Korea*"*, *Human Rights Watch,*12 January 2017, http://www.refworld.org/docid/587b582b13.html. Site accessed 15 September 2018.

89 "North Korea 2016/2017"*, Amnesty International,* 2017, https://www.amnesty.org/en/countries/asia-and-the-pacific/north-korea/report-korea-democratic-peoples-republic-of/. Site accessed 16 September 2018.

90 "A Case for Clarification: European Asylum Policy and North Korean Refugees*"*, *European Alliance for Human Rights in North Korea,* Jun. 13, 2015, Vol. 7, https://www.eahrnk.org/articles/policy-and-research/a-case-for-clarification-european-asylum-policy-and-north-korean-refugees. Site accessed 20 September 2018.

91 *Ibid.*

92 Art. 3, 1948 Daehan Minkuk Hunbeob [Hunbeob] [Constitution], (July 17, 1948) (S. Kor.).

93 Art. 3 Nationality Act, (amended Dec. 13, 1997) (S. Kor.).

94 *Supra* n 83, at p. 799.

95 Art. 7, North Korean Refugees Protection and Settlement Support Act, 21 January 2014.

96 *Ibid.*

97 *Ibid.* at Art. 8.

98 *Ibid.*

However, the South Korean Act on the Protection and Settlement Support of Residents Escaping from North Korea "limits protection to North Korean escapees in three different ways."[99] First, Article 3 states that protection will only be provided to Koreans "who have expressed their intention to be protected by the Republic of Korea."[100] This means that North Koreans who do not wish to live in or be considered citizens of South Korea will not be afforded the protection of South Korea. Second, North Koreans must not have 'earned their living' for 'a considerable period' in another country after leaving North Korea.[101] The government of South Korea has explained this to mean anyone who has lived outside of North Korea for a long period of time without approaching South Korean officials is ineligible for protection.[102] The exact amount of time after which an individual is no longer eligible for protection is not specified, nor has any government official clarified this. After such a time period, North Koreans are no longer entitled to protection by South Korea. Third, those who are deemed "unfit for the designation as persons eligible for protection" are excluded from South Korean nationality.[103] A South Korean government official has noted that certain categories of individuals, such as 'bogus defectors' as well as "persons who have committed murder, aircraft hijacking, drug trafficking, and terrorism" are excluded as unfit for protection.[104] The official and the government of South Korea have not clarified further what constitutes a 'bogus' defector.

The United Kingdom (UK) adjudicates many claims of North Koreans, finding that they hold South Korean nationality and are therefore ineligible for refugee status elsewhere.[105] In *KK and Ors*, the Tribunal evaluated the claims of three North Korean nationals.[106] The tribunal accepted that the individuals had a well-founded fear of persecution in North Korea.[107] However, the Tribunal rejected the idea of effective nationality, concluding that "for the purposes of the Refugee Convention, where a person already has a nationality (even if he has no documents to that effect) that is the end of the matter: he is a national of the country concerned."[108] The Tribunal concluded that North Korean individuals born of North Korean parents are South Korean nationals at birth and therefore ineligible for protection as refugees elsewhere.[109] In making this determination, the Tribunal relied on the UK Home Office report, which serves as guidance

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99 *Supra* n 83, at p. 799

100 *Supra* n 95, at Art. 9.

101 *Ibid.*

102 "The situation of citizens of the Democratic People's Republic of Korea (North Korea) who approach embassies of the Republic of Korea (South Korea) in Canada or in other countries to request citizenship", *Immigration and Refugee Board of Canada,* Jun. 3, 2008, https://irb-cisr.gc.ca/en/country-information/rir/Pages/index.aspx?doc=452042. Site accessed 3 November 2018.

103 *Ibid*.

104 *Supra* n 102.

105 The U.K. interestingly denied refugee status to a Jewish refugee in 1991, stating that they could seek status in Israel. *Supra* n 53, at p. 336.

106 *Supra* n 83, at p. 806.

107 *KK and Ors v Secretary of State for the Home Dept*., para.6, [2011] (UK).

108 *Ibid.* at para. 82.

109 *Ibid.* at paras. 84-85.

for adjudicators of refugee claims.[110] This report notes that "an application for asylum owing to a fear of persecution in North Korea is, therefore, likely to fall for refusal on the basis that the person . . . could reasonably be expected to avail himself of the protection of another country where he could assert citizenship," namely South Korea.[111] However, the Tribunal held that because these three individuals were "outside Korea for more than ten years," they would be treated as individuals who lost their South Korean citizenship and therefore were entitled to refugee protection in the UK.[112]

The UK takes the position that all North Koreans who fled the peninsula within the last ten years are South Korean citizens, and therefore ineligible for refugee protection. The country has refused to engage with an analysis of effective nationality. According to the UK government, once an individual has a right to a second nationality, he must seek protection from this state before seeking international protection in the UK. This is the case regardless of the process required to formally obtain this nationality, the likelihood of the process being successful, or the desire of the individual to engage in that process and receive protection from this second state. This refusal to engage with an effective nationality analysis has led to the UK's denial of nearly all claims of North Koreans fleeing persecution.

V. RECOMMENDATIONS FOR THE APPLICATION OF ARTICLE 1(A)(2)

The purpose of the Refugee Convention is to protect refugees and ensure international cooperation in doing so. Each of the above examples features a denial, or an attempted denial, of refugee status for an entire population because of an imposed dual nationality. However, these policies can have individual impacts on applicants who hold dual nationality through, for example, parentage or lineage. These examples demonstrate the disturbing implications that arise from a literal application of a provision in the Refugee Convention. In the 1950s, less than ten countries allowed dual citizenship.[113] At that time, few individuals were able to hold dual citizenship, and none of the laws explained above existed. Today, two thirds of states allow dual nationality, accounting for slightly under half of the world's population being entitled to dual citizenship.[114] The past 68 years have seen mass decolonisation, political crises, and globalisation that could not have been foreseen at the time of the drafting of the 1951 Refugee Convention. The law

110 *Country Information and Guidance: North Korea: Opposition to the Regime*, U.K. Home Office (Oct. 2016), http://www.refworld.org/pdfid/57f63cd94.pdf. Site accessed 14 November 2018.

111 *Ibid.* at sec. 2.2.9.

112 *Supra* n107, at para. 91. Australia also has a history of denying North Koreans' asylum claims. Upon denial, many of these individuals are sent to China, a country known to return North Koreans to their home country. Roberta Cohen, "China's Forced Repatriation of North Korean Refugees Incurs United Nations Censure", *Brookings,* July 7, 2014, https://www.brookings.edu/opinions/chinas-forced-repatriation-of-north-korean-refugees-incurs-united-nations-censure/. Site accessed 22 January 2019.

113 *Supra* n 17, at pp. 531, 534.

114 Youyou Zhou, "Are rich countries more likely to allow dual citizenship?", *Quartz,* 20 September 2018, https://qz.com/1342183/are-rich-countries-more-likely-to-allow-dual-citizenship/. Site accessed 29 January 2019.

and our interpretation of ineffective citizenship must adapt to our current world in order to achieve the goal of the Refugee Convention: protecting the world's most vulnerable.

The Refugee Convention should not be used to deny refugee claims based on the exercises of sovereignty of certain states, or based on citizenship that is in fact ineffective. The differing applications of Article 1(A)(2) create confusion and problems for refugees seeking protection from persecution and lawyers who undertake to represent them. Refugee law affects individuals and should be accessible and understandable to the people it will affect. There should be a uniform application of Article 1(A)(2) regardless of the country of asylum of the applicants. However, this uniform application must be informed by our current global climate and must have a focus on protection of the world's most vulnerable people who are seeking safety.

In order to remedy the issues that arise in situations such as those described above, a new standard for ineffective nationality should be adopted to ensure individuals are not denied refugee protection simply because of one state's exercise of sovereignty. In addition, regardless of the standard for ineffective citizenship employed, states must refrain from *refouling* individuals who would satisfy the definition of 'refugee' but for a second citizenship.

A. *New Standard for Ineffective Citizenship*

As discussed above, the current standard for ineffective nationality requires that an individual seek protection of a state and be denied this protection. Only then can a nationality be said to be ineffective, thereby allowing an individual to seek refugee protection elsewhere. However, this standard is far too inflexible given the situations discussed above.

However, there are additional situations in which citizenship should also be seen as ineffective. First, an evaluator of the citizenship must look beyond simply the laws of the state in determining whether a citizenship is effective. Citizenship is not contained in the laws of the country alone; international law suggests that a genuine link must exist between the individual and the country. As noted, there are obligations individuals have to their countries of nationality, as well as rights those individuals are guaranteed by the state. For example, an individual must have access to protection of their state of second nationality even outside of that state, have the ability to vote, be required to serve in an army, or be required to pay taxes. When individuals are not granted these rights and are not bound by these obligations, we cannot say the individual holds citizenship of that country.

National laws alone, absent other rights and protections that typically are afforded to nationals, cannot suffice to denote citizenship. Using an example above, because South Korea cannot and does not provide protection for North Koreans outside its borders, does not grant this citizenship automatically, and can deny citizenship to an individual for various reasons, this ought not be considered an effective citizenship. The rights and protections normally afforded to nationals must be granted to individuals in order for them to be considered citizens. North and South Korea certainly have a shared history and a close historical link. However, the link between individual North Koreans and South Korea is tenuous at best. South Korea hopes for a unified Korea where all North

Koreans would be citizens of this state. However, this certainly cannot be understood to be enough of a link to constitute a genuine link for the purposes of citizenship.

Consequently, we should not conflate the availability of citizenship with citizenship itself. The countries above each claim entire groups of people as their citizens yet do not provide documents, rights, or status to these individuals until they arrive in the country in question. This can best be understood as an inchoate right. An individual must provide documentation and proof, approach an embassy, and engage in a process to receive protection from the state in question. This is not a right in itself, but an inchoate right; one that may develop into a full right to citizenship, but is not as it stands a right to citizenship. While every North Korean *may* acquire South Korean nationality, this does not mean that every North Korean *is* a South Korean national.

This conflation between an inchoate right and an actual right is a particularly troubling premise to accept when conflicts exist between the law of the state of origin and that of the state of second citizenship of the individual. Many countries do not allow their citizens to hold a second citizenship; Indonesia and North Korea are two such countries.[115] How can the law of the applicant's country of origin be reconciled with the law of the country of alleged second citizenship when this is the case? Certainly, an adjudicator cannot only consider the law of the applicant's country of second citizenship and completely disregard the domestic law of the applicant's country of origin. If a country prohibits dual nationality for its citizens, those citizens cannot be understood as having held a second nationality since birth. For example, because North Korean law prohibits dual citizenship, North Korean citizens escaping the regime cannot be understood as having South Korean citizenship since birth. They must instead be understood to hold an inchoate right to citizenship, or an ability to acquire South Korean citizenship upon review of application to South Korea. This would mean that North Koreans do not hold a second nationality and should not be excluded from refugee status on this basis alone. This important distinction must be considered in a determination of effective citizenship.

In addition, states must look at the geopolitical realities to understand why the imposition of certain citizenships is inappropriate and should not prevent an individual from receiving protection as a refugee. When a citizenship arises from conflicts between sovereigns, such as between North and South Korea, or after a period of decolonisation, as is the case with East Timor, and forced upon individuals, states must not accept this as effective. In each of the examples, domestic laws that force citizenship upon another weaker or unrepresented population is problematic. Each of these is an exercise in sovereignty that largely remains unchallenged in the international sphere. One of the few areas in which this arises is in the adjudication of refugee claims. This is especially problematic when the persecution the individual is fleeing from is a direct or indirect consequence of the colonisation by that state. An individual would then be forced to seek the protection of the state that acted as a catalyst for their persecution. Forced nationality

[115] See, as example: "List of Countries that Allow or Disallow Dual Citizenship", http://dlgimmigration.com/united-states-citizenship/list-of-countries-that-allow-or-disallow-dual-citizenship/. Site accessed 25 September 2018.

in this instance, when the individual seeks to divest himself of this citizenship, ought not to be considered effective.

Therefore, in order for a citizenship to be effective, the individual must actually be treated as a citizen of the country, with all the rights and obligations that accompany that status according to domestic law. In addition, there must be a genuine link between the individual and the state and the individual must actually hold the citizenship, not merely be entitled to hold the citizenship, in order to be denied protection as a refugee. Lastly, forced citizenship in certain circumstances, such as when it is a result of conflict between states or when a colonising state imposes it on the local population, ought not to be considered effective.

B. *Eye to Non-Refoulement*

The object and purpose of the 1951 Refugee Convention is the protection of individuals from persecution in their country of origin. According to the VCLT, those that are states parties to the 1951 Refugee Convention must not act to frustrate that purpose. States parties must act in accordance with Article 33 of the Convention and therefore must not return refugees to their country of origin, or to countries that may later return them to their country of origin.[116]

Regardless of a determination of the individual's second citizenship, they ought never to be returned to their country of origin or to a third country that could later return them to their country of origin. Individuals who hold a second citizenship but who otherwise would satisfy the definition of 'refugee' in the 1951 Refugee Convention should be sent to their country of second citizenship rather than returned to their country of origin or returned to a neighboring country. The individuals above fit the definition of 'refugee' in that they are outside their home country owing to a well-founded fear of persecution because of political opinion, nationality, race, religion, or membership in a particular social group. These individuals must be transferred to their second country of nationality. It is inappropriate and frustrates the object and purpose of the 1951 Refugee Convention to return an individual to his country of origin in order that he can approach his country of second citizenship.

VI. CONCLUSION

This paper has discussed the principles of nationality and ineffective nationality. Each of the states above applies the principle differently, leading to different conclusions about what constitutes ineffective nationality, and whether that analysis is necessary in an adjudication of a refugee claim. The term ineffective citizenship should consider the realities of today and a deeper analysis ought to be made of effective citizenship for the purposes of refugee claims. In making this determination, states should consider the links between the individual and the state, including the rights and obligations that the individual has. In addition, the adjudicator of a claim must separate an inchoate right to citizenship,

[116] *Supra* n 1, at Article 33.

or the availability of citizenship, from citizenship itself. Moreover, citizenship imposed on entire populations in certain circumstances ought not to be recognised as effective, since they are the result of peculiar exercises in sovereignty. Regardless of the considerations adopted, individuals must never be returned to their country of persecution, or a transit country that will later return them to their country of persecution.

Adopting these new considerations in determining the effectiveness of a citizenship will allow states to act in accordance with the object and purpose of the Refugee Convention and will prevent states from escaping responsibility to protect vulnerable individuals. With a concept as undefined as ineffective citizenship, states must ensure they are acting in accordance with the object and purpose of the treaty and adjust their understandings of the term as world perspective on, and individual rights to, dual nationality shift.

Standard of Fault for Recipient and Accessory Liability

Kwong Chiew Ee*

Abstract

Barnes v Addy is arguably one of the most important judgments in modern equity as it represented for the first time that third parties could be held personally liable to a beneficiary under a trust, through either recipient or accessory liability. These two liabilities are now commonly known respectively as 'knowing receipt' and 'dishonest assistance'. There has been considerable amount of controversy relating to the standard of fault required for each form of liability resulting from two English cases decided in early 2000s, *Twinsectra v Yardley* and *BCCI (Overseas) Ltd v Akindele*. This article seeks to critically assess the development of the law on the standard of fault for each liability post-*Twinsectra* and *Akindele*, and the treatment of the law by the Malaysian courts. This article will also examine how Malaysian courts have failed to adopt a principled approach in setting the standards of fault for recipient or accessory liability.

Keywords: Knowing Receipt, Dishonest Assistance, Equity.

I. INTRODUCTION

The law on dishonest assistance and knowing receipt found its origin in the House of Lords case of *Barnes v Addy*.[1] The case is arguably one of the most important judgments in modern equity as it represented for the first time that third parties could be held personally liable to a beneficiary under a trust.

In *Barnes v Addy*, Lord Selborne LC set out two circumstances upon which third parties can be held liable to a beneficiary under a trust. The first scenario is where the third party receives some part of the trust property in breach of trust. This is often referred to as the first limb of *Barnes v Addy* and is usually stated as liability for 'knowing receipt'. The second situation is where a third party dishonestly assisted in the breach of trust by a trustee. This form of liability is known as the second limb of *Barnes v Addy* and is commonly referred to as liability for 'dishonest assistance'.

There has been considerable amount of controversy relating to the standard of fault required for each form of liability resulting from two English cases decided in early 2000s,

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1 (1874) LR 9 Ch App 244.

Twinsectra v Yardley[2] (*Twinsectra*) and *BCCI (Overseas) Ltd v Akindele*[3] (*Akindele*). This article seeks to critically assess the development of the law on the standard of fault post-*Twinsectra* and *Akindele*, and the treatment (or rather, mistreatment) of the law by the Malaysian courts.

II. COMMON FEATURES AND DIFFERENCES OF THE TWO LIABILITIES

There are, in essence three common features for liabilities under knowing receipt and dishonest assistance.[4]

First, the plaintiff in an action for 'knowing receipt' and 'dishonest assistance' enforces a personal remedy, and not a proprietary remedy against the defendant. The remedy to which the plaintiff is claiming is not restoration of the trust property *in specie*, but restoration of the equivalent value of the trust property.

Secondly, when a defendant is found liable for either knowing receipt or dishonest assistance, he is liable to account as a 'constructive trustee', which means that he is liable to account for any gain or profit that he has made from the trust property.[5] It is said that the words 'constructive trustee' in this context denotes that the defendant is 'construed by the court' to have rendered himself personally liable to account to the plaintiff beneficiary in the same way that a trustee would be liable in a case of breach of trust.[6] The defendant will thus be treated *as though* he is a constructive trustee, although he, in fact, is not a trustee.[7]

The last common feature for both forms of liability is that they are both fault-based liabilities. As a form of fault-based liability (instead of strict liability), the state of knowledge of the defendant is an important constituent element to both forms of liability. It is this third common feature, i.e. the element of knowledge, that has been subject to much judicial debate and controversy for many years.

While the English courts have consistently acknowledged that different tests of knowledge should apply to the two limbs of *Barnes v Addy*, little has been said of the doctrinal justification for the difference. Brightman J in *Karak Rubber Co Ltd v Burden*

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2 [2002] 2 AC 164.

3 [2000] EWCA Civ 502.

4 See, Snell's Equity, Sweet & Maxwell, para 30-066.

5 *Paragon Finance plc v D B Thakerar & Co* [1999] 1 All ER 400; *Novoship (UK) Limited & ors v Nikitin & ors* [2014] EWCA Civ 908.

6 Aliastair Hudson, Equity and Trusts (6th Ed., Routledge Cavendish), p.872.

7 See *Dubai Aluminium Co v Salaam* [2002] UKHL 48, where for this reason, Lord Millet has suggested for the words 'accountable as constructive trustee' in the context of third-party liability be replaced with the words 'accountable in equity'. The characterisation of accessories to breach of trust as not being true trustees has important implications. For example, in *Williams v Central Bank of Nigeria* [2014] UKSC 10, the English Supreme Court held that a defendant under dishonest assistance and knowing receipt is not a "true trustee" and any action against it does not fall under s. 21(1)(a) of the English Limitation Act 1980 (which prescribed for no period of limitation for an action by a beneficiary for breach of trust). S. 22(1)(a) of the Malaysian Limitation Act 1953 is *in pari materia* with s. 21(1)(a) of the English Limitation Act 1980.

(No. 2) questioned whether there was "any particular logic in having different fault requirements for the two different liabilities".

Professor Paul S Davies takes the view that the normative basis of recipient liability is different from assistance liability, and therefore, the two liabilities should be treated differently.[8] Liability in knowing receipt is non-participatory and inherently passive. As such, a person who is in receipt of a trust property may not have necessarily contributed to the primary wrong. Thus, *Davies* opined that it is not helpful to amalgamate both forms of liability. His view on why both should be treated differently is encapsulated in the following passage:

> Recipient liability is based upon accounting for a benefit actually received, and considerations regarding the vindication of equitable property rights must be balanced against the importance of protecting the defendant's ability to rely upon property receipt. This principle of security of receipt is irrelevant to the general principles of accessory liability, since such liability is not premised upon the defendant's receipt of anything.[9]

As a corollary to this, it can be argued that the reason why the standard of fault for liability for recipient liability[10] should be lower than that of assistance liability[11] lies with the question of whether the defendant has gained from his wrongdoing. A defendant under accessory liability does not retain the trust property. For recipient liability, the defendant has gained from his wrongdoing in the form of the receipt of the trust property, which justifies the lower standard of knowledge.[12] Viewed from this perspective, recipient liability should therefore be treated as different from assistance liability.

III. KNOWING RECEIPT – THE MOVE FROM CONSTRUCTIVE KNOWLEDGE TO UNCONSCIONABILITY

A. Pre-Akindele

With respect to liability under knowing receipt, English courts were traditionally divided as to what standard of knowledge is required for the liability to exist. On one hand, courts have found that liability for knowing receipt must be based on the existence of

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8 Paul S Davies, *Accessory Liability*, (Oxford: Hart Publishing, 2015), p. 92.

9 *Ibid.*

10 Historically, the standard of fault for recipient liability is constructive knowledge and more recently, unconscionability.

11 The standard of fault is 'dishonesty'.

12 Although it is important to qualify that a recipient would remain liable for knowing receipt even if he has subsequently transferred the trust property to another person.

actual knowledge.[13] On the other hand, some courts have also accepted that constructive knowledge is sufficient.[14]

In *Baden, Delvaux and Lecuit and others v Societe Generale pour Favoriser le Developpement du Commerce et de l'Industrie en France SA*[15] *(Baden),* Peter Gibson J comprehensively set out the five levels of knowledge that will typically give rise to constructive trusteeship.[16] These different levels of knowledge in the 'Baden scale' are:

(i) actual knowledge;
(ii) willfully shutting one's eyes to the obvious;
(iii) willfully and recklessly failing to make such enquiries as an honest and reasonable man would make;
(iv) knowledge of circumstances which would indicate the facts to an honest and reasonable man; and
(v) knowledge of circumstances which will put an honest and reasonable man on inquiry.

Nourse LJ in *Akindele* opined that knowledge on the scale of (i) to (iii) are considered as categories of actual knowledge, whereas from scale (iv) to (v) are categories of constructive knowledge.[17]

The following passage from the judgment of Millet J in *Agip v Jackson*[18] is often cited as the authority for the proposition that constructive knowledge is sufficient to establish knowing receipt:

> [T]he person who receives for his own benefit trust property transferred to him in breach of trust ... is liable as a constructive trustee if he received it with notice, actual or constructive, that it was trust property and that the transfer to him was a breach of trust, or if he received it without such notice but subsequently discovered the facts. In either case he is liable to account for the property, in the first case as from the time he received the property and in the second as from the time he acquired notice

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13 *In re Montagu's Settlement Trusts* [1987] Ch 264; *Eagle Trust plc v SBC Securities Ltd* [1993] 1 WLR 484 and *Cowan de Groot Properties Ltd v Eagle Trust plc* [1992] 4 All ER 700.

14 *Agip v Jackson* [1990] Ch 265, 291; *Rolled Steel Products (Holdings) Ltd v British Steel Corporation* [1986] Ch 246; Houghton v Fayers [2000] 1 BCLC 511.

15 [1992] 4 All ER 161, [1993] 1 WLR 509, 575-576.

16 See, for e.g. *Re Montagu's Settlement Trust; Westpac Banking Corporation v Savin* [l985] 2 NZLR 41, 42 *Equitycorp Industries Group Ltd v Hawkins* [l991] 3 *NZLR* 700, 703; *Agip (Africa) Ltd v Jackson* [l990] Ch 265, 267 and 292; *Cowan de Groot Properties Ltd v Eagle Trust plc* [l9921 4 All ER 700,702 and 754; *Polly Peck International plc v Nadir* (No 2) [l9921 4 All ER 769,771; *Eagle Trust plc v SBC Securities Ltd* (No 2) [l9961 1 BCLC 121,122.

17 See however, *Davies*, supra note 6 at p. 72, where the author opined that only category (i) of the *Baden* scale of knowledge amounts to actual knowledge.

18 [1990] Ch 265, 291, cited with approval in *Pharmmalaysia Bhd v Dinesh Kumar Jashbhai Nagjibha Patel & Prs* [2004] 7 CLJ 465 at 559 and *Multi-Code Electronics Industries (M) Berhad & Anor v Gordon Toh Chun Toh & Ors* [2013] 3 MLRH 182 at page 161. Emphasis added.

In the same vein, Millett J in *El Ajou* v *Dollar Land Holdings plc*[19] observed in obiter that "dishonesty or want of probity involving actual knowledge (whether proved or inferred)" was not required for knowing receipt as:

> [a] recipient is not expected to be unduly suspicious and is not to be held liable unless he went ahead without further inquiry in circumstances in which an honest and reasonable man would have realized that the money was probably trust money and was being misapplied.

In this regard, Sir Robert Megarry in *Re Montagu's Settlement Trusts Duke of Manchester v National Westminster Bank Ltd and others*[20] observed as follows vis-à-vis actual knowledge:

> The relevant knowledge which would make a recipient of trust property a constructive trustee was actual knowledge that the property was trust property, or knowledge which would have been acquired but for ignoring the obvious or willfully and recklessly failing to make such inquiries as a reasonable and honest man would have made, since in such cases there was a want of probity which justified imposing a constructive trust

In essence, it is widely accepted that knowledge falling under any part of the Baden scale spectrum is sufficient to find liability for knowing receipt. In *International Sales and Agencies Ltd* v *Marcus,*[21] *Lawson J* said*:*

> In my judgment, the knowing recipient of trust property for his own purposes will become a constructive trustee of what he receives if either he was in fact aware at the time that his receipt was affected by a breach of trust, or if he deliberately shut his eyes to the real nature of the transfer to him . . . or if an ordinary reasonable man in his position and with his attributes ought to have known of the relevant breach. This I equate with constructive notice . . . I am satisfied that in respect of actual recipients of trust property to be used for their own purposes the law does not require proof of knowing participation in a fraudulent transaction or want of probity, in the sense of dishonesty, on the part of the recipient.

However, this position has changed following the formulation of the much broader unconscionability test by Nourse LJ in *Akindele*, which has since been adopted in other common law jurisdictions.[22]

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19 [1993] 3 All ER 717.

20 [1992] 4 All ER 308, cited with approval by the Court of Appeal in *Tan Sri Dato' (Dr) Rozali Ismail & Ors v Chua Lay Kim (P) & Ors* [2016] 3 CLJ 84. Emphasis added.

21 [1982] 3 All ER 551.

22 *George Raymond Zage III and another v Ho Chi Kwong and another* [2010] 2 SLR 589 (Singapore Court of Appeal); *Thanakharn Kasikorn Thai Chamkat (Mahachon) (aka Kasikornbank Public Co Ltd) v Akai Holdings Ltd (in liquidation)* (Hong Kong Court of Final Appeal).

B. Akindele – The Test of Unconscionability

The case of *Akindele* concerns a claim by the liquidators of the ill-fated Bank of Credit and Commerce International (BCCI) against Mr. Akindele, a Nigerian businessman for the return of the payments he received under a divestiture agreement in 1988.

The genesis of the case started in 1985, when Mr. Akindele agreed with ICCI Overseas to purchase 250,000 shares in BCCI Holdings. ICCI Overseas imposed a condition that Mr. Akindele was to hold the shares for two years. It was also agreed that upon the expiry of the two years and up to five years from the date of the agreement, Mr. Akindele will receive a return of 15% per annum on his investment if he was to sell his shares. In 1998, Mr Akindele decided to sell the shares by way of a divestiture agreement, and ICCI Overseas paid him a total of US$ 16.679 million. The whole arrangement was in fact part of a fraudulent scheme perpetrated by BCCI to purchase its own shares through nominee companies. The liquidators for BCCI claimed that Mr. Akindele was liable as a constructive trustee both on the ground of 'knowing assistance' and, in relation to the 1988 divestiture payment, on the ground of 'knowing receipt'.

It was therefore important for the Court of Appeal to decide whether Mr. Akindele had the requisite mental element, given that he did not knowingly participate in the fraudulent scheme. His Lordship took the view that the *Baden* categorisation was "not formulated with knowing receipt in mind."[23] Nourse LJ propounded the single test of knowledge for knowing receipt, which entails the law to consider whether "[t]he recipient's state of knowledge must be such as to make it unconscionable for him to retain the benefit of the receipt". This test, according to his Lordship, is simpler and has the advantage of enabling the courts to "… give common-sense decisions in the commercial context in which claims in knowing receipt are now frequently made…" in comparison to the *Baden* scale espoused by Peter Gibson J.

Following Nourse LJ's introduction of the unconscionability standard, some academicians have now recast the liability of knowing receipt as 'unconscionable receipt'.[24] It is important to note that although Nourse LJ has introduced the concept of 'unconscionability' to knowing receipt, his Lordship was quite unequivocal in stating that the nature of its liability is not restitutionary-based, but fault-based, given that strict liability (which is the nature of a claim in restitution) is not suitable for commercial transactions.[25]

Nourse LJ had opined that the unconscionability test is designed to "avoid those definition and allocation to which the previous categorisations [i.e. the *Baden* test] have led". If that was its intention, then an examination of cases post-*Akindele* will reveal that the unconscionability test has failed to achieve its intended purpose. Although the *Akindele* test has eschewed the more principled approach in the *Baden* test in favour of the more

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23 At 454, G-H.

24 See Graham Virgo*, Principles of the Law of Restitution* (OUP, 2015), at 645; Alastair Hudson, *Principles of Equity and Trusts* (Routledge, 2016); See also, Susan Barkehall Thomas, '*Goodbye' Knowing Receipt. 'Hello' Unconscientious Receipt*, Oxford Journal of Legal Studies, Volume 21, Issue 2, 1 January 2001, Pages 239–265, where the author used the term 'unconscientious receipt'.

25 The rejection of restitutionary basis for knowing receipt is re-affirmed in *Brown v Bennett* [1999] 1 BCLC 649 and *Houghton v Fayers* [2000] 1 BCLC 571.

'flexible' test of unconscionability, courts have continued to use the *Baden* categorisations to inform the meaning of 'unconscionability'. For example, post-*Akindele*, courts have interpreted unconscionability to include dishonesty, willfully and recklessly failing to make such inquiries as an honest and reasonable person would make.[26]

The perceived 'flexibility' of the unconscionability test is problematic for a number of reasons. For one, Nourse LJ did not provide a clear guidance as to what standard should unconscionability be judged upon i.e. whether it is an objective or a subjective test. *Akindele* did not provide any guidance as to the pertinent question of whose conscience has to be affected i.e. the recipient, or a reasonable person, or a reasonable person with the knowledge of the recipient. Critics have said that "it is difficult to clearly ascertain what unconscionability means and how it is to be assessed"[27] and that the word 'unconscionability' is "the most slippery of words".[28] One should note that unconscionability "is a very unruly horse, and once you get astride it, you never know where it will carry you".[29] Professor Peter Birks had said:[30]

> "Unconscionable" gives no guidance. At one extreme it is unconscionable not to repay what you were not intended to receive. At the other extreme, it is unconscionable to be dishonest. "Unconscionable," indicating unanalysed disapprobation, thus embraces every position in the controversy. If we look at what the court did, rather than at the word in which it summed up the test which it intended to apply, we can see that Chief Akindele held onto his money as a result of a factual inquiry resembling an inquiry into constructive notice: he neither knew nor ought to have known of the improprieties going on inside BCCI. In this inquiry "unconscionable" seems no more than a fifth wheel on the coach.

At this juncture, it is relevant to recall that Lord Nicholls in *Royal Brunei Airlines v Tan*[31] has cautioned against the use of unconscionability for accessory liability,[32] as it is not clear what the word means, especially to non-lawyers. His Lordship observed that:

> Unconscionable is a word of immediate appeal to an equity lawyer. Equity is rooted historically in the concept of the Lord Chancellor, as the keeper of the Royal Conscience, concerning himself with conduct which was contrary to good conscience. It must be recognised, however, that unconscionable is not a word in everyday use by non-lawyers. If it is to be used in this context, and if it is to be the

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26 *Niru Battery Manufacturing Co v Milestone Trading Ltd [*2002] EWHC 1425 (Comm), [2002] 2 All ER (Comm) 705, 741. This was endorsed in the Court of Appeal: [2003] EWCA 1446 (Civ); *Abou-Rahmah v Abacha* [2006] EWCA Civ 1492.

27 Davies, *supra note 6,* p. 77.

28 Andrew Burrows*, Construction and Rectification* in A Burrows and E Peel, *Contract Term*s (OUP, 2007), p. 88.

29 Quote credited to Burrough J in *Richardson v Mellish* [1824] 2 Bing 229, 252, who had made that statement in the context of the application of public policy in the realm of conflict of laws.

30 Peter Birks, Arianna Pretto-Sakmann, *Breach of Trust* (Hart Publishing, 2002), p. 201.

31 [1995] 2 AC 378.

32 [1995] 2 AC 378 (PC), 392

> touchstone for liability as an accessory, it is essential to be clear on what, in this context, unconscionable means. If unconscionable means no more than dishonesty, then dishonesty is the preferable label. If unconscionable means something different, it must be said that it is not clear what that something different is. Either way, therefore, the term is better avoided in this context.

The unconscionability test does not provide any guidance to a person as to how one should order his or her conduct. Nonetheless, it has been acknowledged that *Akindele* "represents the present law in England".[33]

Indeed, the difficulty in the application of the unconscionability test becomes apparent if one is to examine its application in Malaysian courts.

C. Malaysian Courts' Application of the Akindele Test

The Court of Appeal was accorded the opportunity to re-examine the standard of knowledge for knowing receipt under Malaysian law in *Ooi Meng Khin v Amanah Scotts Properties (KL) Sdn. Bhd.*[34] (*Ooi Meng Khin*). The facts of *Ooi Meng Khin* are as follows.

The plaintiff had discovered that its employee, the third defendant had carried out large numbers of unauthorised transactions to siphon monies out of the plaintiff to fund his gambling activities. The plaintiff claimed that the fourth, fifth, and seventh defendants were each liable to pay the monies they had received from the third defendant for liability under knowing receipt. One of the contentious points in this case was whether the fourth, fifth, and seventh defendants had the necessary knowledge of the breach of trust by the third defendant when they received monies under the impugned transactions.

In this regard, at paragraph [21] of the judgment in *Ooi Meng Khin*, Abang Iskandar JCA opined that the essential element of the causes of action of receipt and assistance is 'dishonesty':

> In both these causes of action of receipt and assistance, the essential element that the claimant will have to establish against the third party is that his receipt of the claimant's property must be one that was dishonest, and that the assistance rendered was also dishonest, in which case, he has acted as an accessory to the breach of trust.

Immediately in the subsequent paragraph however, Abang Iskandar JCA appears to have endorsed Nourse LJ's test of unconscionability when his Lordship said at paragraphs [22] and [23] that:

> [22] We noted that the learned trial judge had rightly referred to the Singapore case of *George Raymond Zage III and another v Ho Chi Kwong and another* [2010] 2 SLR 589 which had in the course of its deliberation, referred to the decision of learned Justice Nourse LJ in the English Court of Appeal case of *Bank of Credit and Commerce International (Overseas) Ltd and another v Akindele* [2001] Ch

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33 *Charter Plc v City Index Ltd* [2008] Ch 313.

34 [2014] 6 MLJ 488. (Emphasis added).

> 437 where the learned Lord Justice had stated the test in determining precisely the degree of knowledge for the recipient of trust property, to be fixed with liability, to be as follows, namely … [t]he recipient's state of knowledge must be such as to make it unconscionable for him to retain the benefit of the receipt.
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> …
>
> [24] With respect, we found that the learned trial judge did not err in adopting the test the Lord Justice Nourse's test as enunciated in the *Akindele*'s case and further clarified by Justice VK Rajah JA in the *Zage III*'s case.

Despite having adopted Nourse LJ's test of unconscionability, his Lordship still proceeded to state at paragraph [34] that "[c]entral, therefore, in this concept of knowing receipt is the proof of dishonesty on the part of the recipient…". This is respectfully incorrect, as liability for receiving property that has been dissipated in breach of trust is not dependent upon the dishonest state of mind of the recipient. Instead, the plaintiff is required to only show that the recipient has knowledge that will make it unconscionable for him to retain the trust property. If the claimant is able to show that the defendant is dishonest, it follows that he will meet the threshold of unconscionability.

In other words, while it is unconscionable to be dishonest, absence of dishonesty should not be equated with absence of unconscionability as one can still be unconscionable but not necessarily dishonest. It is not correct to say that "the essential element that the claimant will have to establish against the third party is that his receipt of the claimant's property must be one that was dishonest", as even something below dishonesty would suffice to establish 'unconscionability' under knowing receipt. In this regard, it is instructive to refer to the judgment of VK Rajah JA in the Singapore Court of Appeal in *George Raymond Zage III and another v Ho Chi Kwong and another*,[35] which was cited with approval in *Ooi Meng Khin*:

> As candidly acknowledged by Nourse LJ when he formulated the test in *Akindele*, unconscionability is a malleable standard that is not free from difficulty in its application. The degree of knowledge required to impose liability will necessarily vary from transaction to transaction. In cases where there is no settled practice of making routine enquiries and prompt resolution of the transaction is required it seems to us clear that clear evidence of the degree of knowledge and fault must be adduced. We are also inclined to agree that the test, as restated in *Akindele*, does not require actual knowledge. This would be contrary to what we believe was the spirit and intent of Nourse LJ's formulation: it seems to us that actual knowledge of a breach of trust or a breach of fiduciary duty is not invariably necessary to find liability, particularly, when there are circumstances in a particular transaction that are so unusual, or so contrary to accepted commercial practice, that it could be unconscionable to allow a defendant to retain the benefit of receipt. The test of unconscionability should be kept flexible and be fact-centered.

[35] [2010] 2 SLR 589, para. [32]. (Emphasis added).

It is clear Nourse LJ's conception of unconscionability for knowing receipt does not require the plaintiff to establish actual knowledge. Therefore, the test for unconscionability cannot be subjective dishonesty because that would require the plaintiff to establish actual knowledge. Therefore, Abang Iskandar JCA had, with respect, erred in saying that the state of mind for recipient liability "must be one that was dishonest".

To further add to the confusion, the Court of Appeal in *Ooi Meng Khin* then went on to endorse the defence of change of position for recipient liability, at paragraph [37]:

> In the circumstances of this case, D7 was only a mere conduit and that it had not been dishonest and as such it ought to be entitled to avail itself to the defence of change of position.

The defence of change of position is a defence available for a defendant in an unjust enrichment claim. It is the law's response to the unfairness of a strict-liability claim of unjust enrichment and as such, it is irrelevant to the claim of knowing receipt which a fault-based claim is. To put it simply, if a person is found to be liable for knowingly receiving a property dissipated in breach of trust, he cannot be allowed to avail himself to the defence of change of position which at its core, is dependent upon absence of fault.

As such, the decision of the Court of Appeal in *Ooi Meng Khin* is unsatisfactory for two reasons. Firstly, it appears that dishonesty is now required in order to establish knowing receipt. This is contrary to the approach taken in other common law jurisdictions, which require only proof of unconscionability. Secondly, having now elevated knowing receipt to a highest form of fault-based liability, the Court of Appeal then endorsed the defence of change of position for knowing receipt, a defence designed to counteract the effect of a strict-liability claim.

The Court of Appeal was presented with the opportunity to clarify *Ooi Meng Khin* two years later in *Tan Sri Dato' (Dr) Rozali Ismail & Ors v Chua Lay Kim (P) & Ors (Rozali Ismail)*,[36] but the case only managed to add to the confusion created by *Ooi Meng Khin*. In *Rozali Ismail,* Abdul Aziz Abdul Rahim JCA cited the following passage from *Re Montagu's Settlement Trusts Duke of Manchester v National Westminster Bank Ltd and others*[37] at page 308:

> The relevant knowledge which would make a recipient of trust property a constructive trustee was actual knowledge that the property was trust property, or knowledge which would have been acquired but for ignoring the obvious or willfully and recklessly failing to make such inquiries as a reasonable and honest man would have made, since in such cases there was a want of probity which justified imposing a constructive trust.

One would note that "willfully and recklessly failing to make such enquiries as an honest and reasonable man would make" in the *Baden* scale is a form of actual knowledge.

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[36] [2016] 3 CLJ 84 at page 106.

[37] [1992] 4 All ER 308. Emphasis added.

It is noted that in *Rozali Ismail*, the Court of Appeal (apart from endorsing the actual knowledge test) also endorsed the unconscionability test in *Akindele* for recipient liability:

> [45] We also refer to the case *Bank of Credit and Commerce International (Overseas) Ltd v Akindele* [2000] 4 All ER 221 where Lord Justice Nourse sets out in his grounds of judgment at p. 455 and we quote (and agree):
>
> > All that is necessary is that the recipient's state of knowledge should be such as to make it unconscionable for him to retain the benefit of the receipt.
> >
> > For these reasons I have come to the view that, just as there is now a single test of dishonesty for knowing assistance, so ought there to be a single test of knowledge for knowing receipt. The recipient's state of knowledge must be such as to make it unconscionable for him to retain the benefit of the receipt. A test in that form, though it cannot, any more than any other, avoid difficulties of application, ought to avoid those of definition and allocation to which the previous categorisations have led. Moreover, it should better enable the courts to give common sense decisions in the commercial context in which claims in knowing receipt are now frequently made, paying equal regard to the wisdom of Lindley LJ on the one hand and of Richardson J on the other.

It is evident that the Court of Appeal in *Ooi Meng Khin* and *Rozali Ismail* has blurred the lines between actual knowledge, constructive knowledge, and unconscionability. This approach is contrary to Nourse LJ's view in *Akindele* that there should be a single test of knowledge on knowing receipt, and that the standard should be one of unconscionability.

It appears that under Malaysian law, recipient liability can exist if the recipient has acted 'unconscionably' which is defined as dishonestly or has willfully and recklessly failed to make such enquiries as an honest and reasonable man would make. The confusing way in which the Malaysian courts have applied the test of unconscionability belies Nourse LJ's view that the unconscionability test will enable courts to give "common sense decisions in the commercial context". The current lack of clarity as to what amounts to 'unconscionability' is an antithesis to common sense.

Therefore, it is hoped that Malaysian courts will revisit the question of whether Nourse J's unconscionability test is appropriate for recipient liability. In this regard, it is helpful to seek guidance from Australia where its apex court in *Farah Constructions Pty Ltd v Say-Dee Pty Ltd*[38] has reaffirmed the Baden test of knowledge for recipient liability:

> … circumstances falling within any of the first four categories of Baden are sufficient to answer the requirement of knowledge in the first limb of *Barnes v Addy* but does not travel fully into the field of constructive notice by accepting the fifth category. In this way, there is accommodated, through acceptance of the fourth category, the proposition that the morally obtuse cannot escape by failure

38 [2007] HCA 22.

> to recognise an impropriety that would have been apparent to an ordinary person applying the standards of such persons. These conclusions … as to what is involved in 'knowledge' for the second limb represent the law in Australia.

The Australian High Court did not adopt the unconscionability test in *Akindele* and at the same time, also rejected t the strict liability test for recipient liability which was adopted by the Court of Appeal.

More recently, the Supreme Court of Victoria[39] provided further guidance on how one should interpret the third and fourth categories of the Baden scale of knowledge. For the third category - wilfully and recklessly failing to make inquiries as an honest and reasonable person would make, it "involves such a calculated abstention from inquiry as would disentitle the third party to rely upon lack of actual knowledge of the trustee's or fiduciary's wrongdoing".[40] For the fourth category - knowledge of circumstances which would indicate the facts to an honest and reasonable person – the court observed that this category "is designed to prevent a third party setting up his or her own moral obtuseness" as an excuse for not recognising an impropriety that would have been apparent to an ordinary person applying the standards of such ordinary person.[41]

The effortless manner in which the Australian courts have applied the Baden test for recipient liability brings into question whether there was a need for Nourse LJ to introduce the unconscionability for recipient liability in the first place. The answer to that question is evident if one is to observe how Malaysian courts have struggled to understand Nourse LJ's test. As such, Malaysian courts should follow the approach taken in Australia, and reinstate the Baden test for recipient liability.

IV. DISHONEST ASSISTANCE – OBJECTIVE DISHONESTY OR SUBJECTIVE DISHONESTY?

A. Dishonesty as defined by Lord Nicholls in Royal Brunei Airlines v Tan[42]

As for liability for assisting in breach of trust, it is settled law that the standard of knowledge required is one of 'dishonesty'.[43] The 'objective dishonesty' test propounded by Lord Nicholls in *Royal Brunei Airlines v Tan*[44] (Royal Brunei Airlines) is widely accepted as the standard bearer for the dishonesty test under dishonest assistance.

There are two interwoven facets to the test of dishonesty for liability under dishonest assistance as propounded by Lord Nicholls in *Royal Brunei Airlines*.[45] First, accessory liability does not require a dishonest and fraudulent design on the part of the trustee.

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39 *Harstedt Pty Ltd v Tomanek* [2018] VSCA 84.

40 *Harstedt Pty Ltd v Tomanek* [2018] VSCA 84, para. 86.

41 *Ibid.*

42 [1995] 2 AC 378.

43 *Royal Brunei Airlines v Tan* [1995] 2 AC 378; *Karak Rubber Co Ltd v Burden (No 2)* [1972] 1 All ER 1210; *Baden v Société Générale pour Favoriser le Développement du Commerce et de l'Industrie en France SA* [1992] 4 All ER 161, [1993] 1 WLR 509; *Selangor United Rubber Estates Ltd v Cradock (a bankrupt)* (*No 3*) [1968] 2 All ER 1073.

44 [1995] 2 AC 378.

45 [1995] 2 AC 378.

This is simply logical, for otherwise, a dishonest third party may defraud an honest albeit ignorant trustee to commit a breach of trust, and not be caught because there was no dishonest and fraudulent design on the part of the trustee.

Secondly, the liability of the accessory should be dependent on the accessory's own dishonest participation in the breach rather than knowledge, as the requirement of knowledge has led the courts into "tortuous convolutions" in deciding the level of knowledge possessed and required.

Dishonesty, according to Lord Nicholls, is a question of whether the third party has come up to the standard of an honest person in the circumstances, taking into account the third party's knowledge of the facts, his experience, intelligence and practicability of his or the trustees' actions amongst other things.

Therefore, while one has to show that the defendant has engaged in an 'advertent conduct' assessed in the light of defendant's actual awareness at the relevant time, the test for dishonesty does not require that the defendant himself should have appreciated the fact that he was dishonest.

In this regard, if the mental state of the defendant is dishonest by ordinary standards, it matters not that he adheres to a different moral code because honesty is not an 'optional scale' with higher or lower values according to the standards of each individual. Accordingly, dishonesty is measured on an objective standard with subjective considerations.

B. Twinsectra– A subjective test or a combined test?

It appears that the House of Lords in *Twinsectra* have adopted a different interpretation of 'dishonesty' from that of Lord Nicholls. Lord Hutton who delivered the leading judgment concluded that the test of dishonesty involves a combined objective-subjective test that requires the Court to ask this: first, whether an honest person would have done what the third party did and if the answer is yes, then second, whether the defendant appreciated that fact.

In the course of his Lordship's judgment, Lord Hutton considered three possible standards of dishonesty: purely subjective, purely objective and the 'combined test', and concluded that Lord Nicholls in *Royal Brunei Airlines* clearly meant for the 'combined test' to be applied.

Respectfully, while Lord Hutton is right in stating that the test is a 'combined test', his Lordship has erred in his application of the test. Lord Nicholls in considering the subjective elements (e.g knowledge, experience and intelligence) to be relevant in assessing whether the defendant has come up to the standard of an honest man, but in no way relevant to decide whether the defendant would have appreciated that he has acted against the dishonest standard for that will be allowing the defendant to set his own standard of dishonesty.

Unfortunately, the majority of the House of Lords did not appreciate this point. Lord Hoffman in support of Lord Hutton further stated that the dishonest state of mind meant "consciousness that one is transgressing ordinary standards of behavior", which means that the defendant has to be conscious that he has fallen below the standard of an honest and reasonable man.

As a result, the majority's approach in *Twinsectra* has brought the test for dishonest assistance in line with the criminal law test for dishonesty laid down in *R v Ghosh*[46] despite Lord Nicholls' disapproval of the same in *Royal Brunei Airlines*.

Lord Millett who delivered the dissenting judgment objected to the majority's formulation and pointed out that there is "no trace in Lord Nicholls' opinion" of the requirement of the defendant's awareness that he was acting contrary to what an honest man would do. The decision in *Twinsectra*, being the decision of the House of Lords was binding upon all English courts. In its aftermath, *Twinsectra* was subjected to heavy criticisms by legal commentators as the subjective test has raised the barrier for knowledge far too high in order for one to establish accessory liability.

C. Clarification of the Law Post-Twinsectra

The Privy Council was given the opportunity to clarify the law in *Barlow Clowes International v Eurotrust International*[47] *(Barlow Clowes*), and did not disappoint. In *Barlow Clowes*, Lord Hoffman admitted that the majority in *Twinsectra* was ambiguous as to their application of Lord Nicholls' dishonesty test. His Lordship was of the opinion that on deeper examination of Lord Hutton's speech in *Twinsectra*, there was in fact no requirement that the defendant must have reflection as to the normally acceptable standards. Rather, what Lord Hutton really meant was that the defendant is required to possess knowledge of the transaction that will render his participation contrary to the normally acceptable standards. Lord Hoffman observed that Lord Hutton's conception of 'knowledge' refers to knowledge of the transaction and not knowledge that the defendant has fallen below the ordinary standard of dishonesty.

Lord Hoffman stopped short of saying that the majority of the House of Lords have simply erred. Instead, his Lordship stated that the majority in *Twinsectra* did not attempt to alter Lord Nicholls' formulation in *Royal Brunei Airlines* and that *Twinsectra*'s formulation was ambiguous but no different from *Royal Brunei Airlines*. This left the door open for the lower courts in England to apply the correct approach in *Barlow Clowes* and inject clarity into the English law without having to depart from precedent.

The opportunity to clarify the English law position on this issue was duly taken up by the English Court of Appeal in *Abou-Rahmah v Abacha*[48] (*Abou-Rahmah*). Taking a rather pragmatic approach, Arden LJ accepted that *Twinsectra*, being the House of Lords decision, was binding on the Court of Appeal. Her Ladyship, however, saw no difficulty in applying *Barlow Clowes* as it did not involve a departure from the House of Lords' decision in *Twinsectra*. The role *of Barlow Clowes*, according to her Ladyship, was merely to clarify the speeches of Lord Hutton and Lord Hoffman in *Twinsectra*. Therefore, it was open for the Court of Appeal to apply *Barlow Clowes*' interpretation of *Twinsectra* and *Royal Brunei Airlines*.

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46 [1982] 3 WLR 110.

47 [2005] UKPC 37.

48 [2006] EWCA Civ 1492 (CA).

As such, one may conclude that the test of dishonesty in English law in relation to dishonest assistance is no longer uncertain due to the clarification given by the Privy Council in *Barlow Clowes*. The case confirms that under English law, the standard of dishonesty is objective (and not a mixed test), and the defendant's awareness or actual knowledge of the dishonest standard is immaterial. Across the causeway, the Singapore Court of Appeal in *George Raymond Zage III v Ho Chi Kwong* has likewise adopted this approach:

> [F]or a defendant to be liable for knowing assistance, he must have such knowledge of the irregular shortcomings of the transaction that ordinary honest people would consider it to be a breach of standards of honest conduct if he failed to adequately query them.

The clarification of the test for dishonesty is indeed welcoming. It is worth noting that the subjective dishonesty test in criminal law introduced by *R v Ghosh*[49] has recently been overturned in the UK Supreme Court.[50] This reaffirms that the subjective dishonesty test has no place in English law.

D. The Subjective Dishonesty Test Adopted by the Federal Court

In Malaysia, the Court of Appeal in *Kuan Pek Seng @ Alan Kuan v. Robert Doran & Ors*[51] has precisely taken the same view in *Barlow Clowes* and *Abou-Rahmah*, by accepting that *Twinsectra* does not alter the objective dishonesty test propounded by Lord Nicholls in *Royal Brunei Airlines*. Jeffrey Tan FCJ (sitting as a judge at the Court of Appeal) said as follows:

> [59] … what Lord Hutton said in *Twinsectra* has now been restated and reinterpreted in *Barlow Clowes International Ltd (in liquidation) and others v Eurotrust International Ltd and others* [2006] 1 WLR 1476, where it was accepted by Lord Hoffman, who delivered the judgment of Their Lordships, 'that the test whether a person was consciously dishonest in providing assistance[,] required him to have knowledge of the elements of the transaction which rendered his participation contrary to ordinary standards of honest behavior'. At p 1481, Lord Hoffman explained that 'the reference to 'what he knows would offend normally accepted standards of honest conduct' meant only that his knowledge of the transaction had to be such as to render his participation contrary to normally acceptable standards of honest conduct. It did not require that he should have had reflections about what those normally acceptable standards were'. Arden LJ in *Abou-Rahmah v Abacha* [2006] EWCA Civ 1492, has now endorsed *Barlow Clowes* as representing the current English law.

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49 [1982] 3 WLR 110.

50 *Ivey v Genting Casinos UK Ltd t/a Crockfords* [2017] UKSC 6.

51 [2013] 2 MLJ 174.

However, just as one thought that the dust has settled in *Kuan Pek Seng*, the Federal Court in a later case took a different approach by interpreting *Twinsectra* as introducing a subjective test. In *CIMB Bank Bhd v Maybank Trustee Bhd*[52] Arifin Zakaria CJ observed that Twinsectra has introduced the concept of subjective dishonesty:

> [145] The above principle was extended by *Twinsectra Ltd v Yardley and others* [2002] 2 All ER 377 (HL), when it introduced the two-fold tests of an objective and subjective test
>
> …
>
> [146] In a gist, a new test was introduced by *Twinsectra*, in that the concept of subjective dishonesty became a requirement in a breach of trust situation.

In his judgment, Arifin Zakaria CJ did not refer to or consider the judgment of Jeffrey Tan FCJ in *Kuan Pek Seng*.

Recently in *Malaysian International Trading Corporation Sdn Bhd v RHB Bank Berhad,*[53] the Federal Court re-affirmed the interpretation adopted in *CIMB Bank Bhd v Maybank Trustee Bhd* that *Twinsectra* has introduced the element of subjective dishonesty. It is noted that *Malaysian International Trading Corporation Sdn Bhd v RHB Bank Berhad*[54] is a case on constructive trust, and not dishonest assistance. Nonetheless, the Federal Court made the following observation:

> That was the basic principle alluded to prior to the development of the law of constructive trust whenever parties asserted the existence of a constructive trust. In sequence, *Carl Zeis Stiftung v Herbert Smith & Co (No. 2)* [1969] 2 All ER 377 and *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 3 All ER 97 started the development and was eventually extended to *Twinsectra Ltd v Yardley And Others* [2002] 2 All ER 377. The new approach saw the introduction of a two-fold test of an objective and subjective test. This test which demands the additional subjective honesty ingredient was approved by *CIMB Bank Bhd v Maybank Trustees Bhd & Other Appeals* [2014] 3 CLJ 1.

The Federal Court did not, in its two decisions, clarify what 'subjective' dishonesty entails i.e. whether it requires one to establish that the defendant appreciates what he was doing was dishonest according to normally acceptable standards, or that he has actual knowledge of the conduct that is alleged to be dishonest. To the best of my knowledge, there is no reported High Court, Court of Appeal or Federal Court judgment that has addressed this point at the time this article was written.

The upshot is that the Malaysia courts remain bound by the "subjective dishonesty" test adopted by the Federal Court. However, as the Federal Court has not given a definitive definition of "subjective dishonesty", it is open for courts to adopt the approach in *Barlow Clowes* and *Abou-Rahmah* i.e. by interpreting subjective dishonesty to mean

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52 [2014] 3 MLJ 169.

53 [2016] 2 CLJ 717.

54 [2016] 2 CLJ 717.

that the defendant has knowledge of the dishonest transaction and not knowledge that the defendant has fallen below the ordinary standard of dishonesty. It is hoped that the Malaysian courts will seize the opportunity to clarify this aspect of the law when the opportunity arises.

V. CONCLUSION

The current state of law for knowing receipt and dishonest assistance in Malaysia remains unsatisfactory.

In *Akindele,* Nourse LJ has propounded the single test of knowledge for knowing receipt, which entails the law to consider whether "[t]he recipient's state of knowledge must be such as to make it unconscionable for him to retain the benefit of the receipt." This test has now been adopted in most major common law jurisdictions. However, in Malaysia, the Court of Appeal in *Ooi Meng Khin* and *Rozali Ismail* has blurred the lines between actual knowledge, constructive knowledge, and unconscionability, contrary to the approach in *Akindele*. Given the lack of clarity as to what amounts to 'unconscionability' in recipient liability, Malaysian courts should follow the approach taken in Australia, and reinstate the Baden test for recipient liability.

As for dishonest assistance, English law has adopted the test of objective dishonesty. The Malaysia courts remain bound by the 'subjective dishonesty' test adopted by the Federal Court. However, as the Federal Court has not given a definitive definition of 'subjective dishonesty', it remains open for Malaysian courts to interpret subjective dishonesty to mean that the defendant has knowledge of the dishonest transaction and not knowledge that the defendant has fallen below the ordinary standard of dishonesty.

Gender Equality by International Norms: An Analysis on Hindu Marriage and Divorce Laws in South Asia with Special Attention to Bangladesh

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Abstract

Personal laws govern the social phenomenon of marriage and the dissolution of marriage, in Bangladesh. A great deal of debate surrounds the issue of Hindu marriage and the right to divorce, under the orthodox Hindu legal regime. It is observed that no significant legal changes have addressed or rectified the age-old provisions of discrimination. Hindus, being a minor community in Bangladesh has been deprived of the benefits that come with expected changes. This paper examines the laws relating to Hindu marriage and divorce in the South Asian context, focusing on India, Nepal and Pakistan with special concern to Bangladesh. It aims to illuminate the constitutional validity of un-unified personal laws and analyses the existing laws which create a safeguard for sustaining the longstanding patriarchal system within the Bangladeshi society. It also observes a flagrant non-compliance with the twin principles of equality and non-discrimination found within the normative framework of universal human rights. The article questions the practical reason behind this non-compliance and suggests some initiatives that could be adopted to ensure justice for the Hindu women of Bangladesh. In spite of the numerous limitations, every effort adds to a robust voice for Hindu women's rights in the country.

Keywords: Hindu Marriage and Divorce, Gender Equality, Discrimination in Hindu Law.

I. INTRODUCTION

Marriage is a social phenomenon that unites two people in a sacred union. Hindu marriage is a sacred union involving various ceremonies that unite not only the two people, but the extended families as well. In *Shastriya*, an ancient Hindu law, Hindu marriages are treated as a sacrament or *Sanskara*.[1] *Shastriya* law enjoins all men to marry for the purpose of procreating sons necessary for carrying on the progenitor's lineage and for the spiritual benefit that saves them from the fires of hell. On the other hand, the dissolution of a marriage is a procedure to break all the vows taken during the sacred ceremony of

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1 Sree Mridulkanti Rakhshit, *The Principles of Hindu Law*, 6th ed., Kamrul Book House, 2008, p. 98.

marriage.[2] In Bangladesh, Hindu women would endure enormous hardships; rather than a separation from their spouse or a divorce. Bangladeshi Hindus follow the *Shastriya* law in this regard, where no right to divorce exists. While polygamy is allowed for men, (they can remarry after a separation) women have the choice of either staying in the marriage or living alone. Though they have a right to live separately (from their husband) they cannot seek a divorce; this has been a debatable issue. In contrast, other South Asian countries, namely, India, Pakistan and Nepal have ensured the right to dissolve marriage. However, no measure has been taken in Bangladesh. This not only weakens the social structure; it also violates the provisions of the Constitution and is inconsistent with international instruments.

This article analyses Hindu personal laws in South Asia regarding marriage and divorce; and the responsibility of the state to both its Constitution as well as international human rights obligations. The next part of the paper discusses Hindu marriage laws concerning prohibitory decrees, ceremonies, polygamy and registration of marriage applicable in Bangladesh as well as other South Asian countries. The following part then focuses on the dissolution of marriage under this law and addresses the issue of discrimination which is prevalent in Bangladesh with comparisons drawn from other South Asian countries. The article attempts to address the question: why are Hindu women in Bangladesh prejudiced? Bound to live a woeful existence in various circumstances. A premeditated approach has been taken to identify the practical reasons for the non-implementation of initiatives that have been proposed by different organs. Lastly, recommendations have been made for the adoption of necessary measures to eliminate the inequitable system that has been in practice for far too long.

II. LEGAL SYSTEM OF BANGLADESH AS REGARD TO HINDU MARRIAGE AND DIVORCE LAWS AND ITS CONCERN TO MAJOR HUMAN RIGHTS JURISPRUDENCE

The legal system of Bangladesh has its roots in the laws of British India. The country adopted laws that were prevalent during the colonial rule in the sub-continent and is a common law jurisdiction. Even after independence, the laws inconsistent with the spirit of the new independent country continued. In the sphere of Hindu personal laws, Bangladesh continues to follow the *Shastriya* law. Having a Muslim majority, Hindu's make up only 8.5% of the total population of the country.[3] Although people of different beliefs enjoy the freedom to exercise their religious rights without any interference, the age old discriminatory Hindu laws prevail. According to the Constitution, secularism is recognised as one of the fundamental principles of state policy in Bangladesh. In accordance with this spirit of secularism, the country keeps its public affairs free from any religious interference. Reforms have been made to Muslim personal laws to eradicate

[2] Md. Ashabur Rahman, Protection of Right to Divorce for Hindu Woman, Law Journal Bangladesh, http://www.lawjournalbd.com/2017/03/protection-of-right-to-divorce-for-hindu-woman/, site accessed on 10 April 2018.

[3] Official Census Results, 2011, p. xiii, Bangladesh Government.

prejudicial provisions; no such initiatives however have been made to Hindu personal laws. Hindu women are primarily affected by this; under *Shastriya* law they cannot inherit property and they do not have the right to dissolve their own marriages even if it is detrimental to life.

Several international human rights conventions contain the principles of equality and non-discrimination. Bangladesh has ratified several international human rights conventions with reservations to a few provisions. The domestic application of international human rights law has been the subject of much debate (from its inception) due to the directory nature of international law which generates a conflicting view regarding compliance to international norms and the state law. From international law's perspective, national courts as the state organs are required to conform to international norms due to the universal nature of human rights standards. The universality of human rights norms is disputed by a number of states upholding the idea of cultural relativism. While debates and dissent over the 'universality' of human rights continue (as they have by no means reached a consensus) courts across the world have generally acquiesce to the less contentious international human rights provisions, such as the right to life and liberty, freedom from torture, and so on.[4] The common practice of all states is that the Higher Judiciary has the jurisdiction to deal with issues pertinent to international instruments.[5] Bangladesh has a similar practice and have acquiesced to some human rights instruments.

The Universal Declaration of Human Rights[6] (UDHR) has served as the foundation for two binding United Nations (UN) human rights covenants, the International Covenant on Civil and Political Rights[7] (ICCPR) and the International Covenant on Economic, Social and Cultural Rights[8] (ICESCR). The principles of the UDHR are also elaborated in other international treaties, such as the International Convention on the Elimination of All Forms of Discrimination against Women (CEDAW). The UDHR continues to be widely cited by governments, academics, advocates, constitutional courts, and by individuals who appeal to its principles for the protection and recognition of their human rights. The UDHR recognises the inherent dignity, the equal, and inalienable rights for all human beings as a foundation of freedom, justice and peace in the world.[9] It assures people that they are entitled to all human rights without distinction of any kind; like, race, colour, sex, language, religion, political or other opinion, national or social origin, property, birth or other status.[10] Equal rights to marriage and its dissolution for both men and women can be found in these different international instruments. The UDHR has

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4 Sumaiya Khair, *Bringing International Human Rights Law Home: Trends and Practices of Bangladeshi Courts*, 2011, 17 Asian Yearbook of International Law, p. 49.

5 An advisory report on "Universality of Human Rights and Cultural Diversity", by the Advisory Councils of International Affairs, Netherlands, No. 4, June 1998.

6 Adopted in the United Nations General Assembly at its 3rd session on 10 December in 1948 as resolution 217 at the Palais D Chaillot in Paris, France.

7 The International Covenant on Civil and Political Rights was adopted by the United Nations General Assembly on 19 December 1966.

8 Adopted and opened for signature, ratification and accession by General Assembly resolution 2200A (XXI) of 16 December 1966; entry into force 3 January 1976.

9 Preamble of the UDHR.

10 Article 2, UDHR.

given both men and women equal rights to marriage and to its dissolution irrespective of race, nationality and religion. Article 16(1) of the Declaration provides that-

> Men and women of full age, without any limitation due to race, nationality or religion, have the right to marry and to found a family. They are entitled to equal rights as to marriage, during marriage and at its dissolution.[11]

CEDAW is an international treaty adopted by the General Assembly of the United Nations (UN) in 1979 to eliminate discrimination against women so that they can enjoy full human rights including equal access to opportunities in areas such as political and public life, health, education and employment.[12] Article 16(1) of CEDAW stipulates that, the states parties shall take all appropriate measures to eliminate discrimination against women in all matters relating to marriage and family relations on the basis on equality between men and women.[13] It ensures the same rights and responsibilities to both the husband and wife during the marriage and dissolution.[14] Bangladesh is one of the first few countries that ratified CEDAW in 1984 with reservations to two articles, namely, Article 2 and Article 16(1c). Article 2 provides that state parties ratifying CEDAW declare their intent to enshrine gender equality into their domestic legislation, repeal all discriminatory provisions in their laws, and enact new provisions to guard against discrimination against women. Article 16 (1c) mandates that state parties shall take all appropriate measures to eliminate discrimination against women in all matters relating to marriage and family relations and, in particular, shall ensure a basis of equality of men and women. Despite the state having adopted many laws and policies over the last few decades with regards to the violence against women in accordance with the principles under CEDAW, it has retained its reservations. The issue of reservation in consideration with *Shariah* principles, has been criticised by different state actors as it is contrary to some of the articles found in the Constitution of Bangladesh.

A. The Constitution of the People's Republic of Bangladesh 1972

The Constitution is the supreme law of the country and has supremacy over all other laws. The Constitution states that all citizens are equal before the law and are entitled to equal protection of law.[15] The Constitution also provides that the state will ensure equal rights to all citizens and remove social and economic disparities.[16] The principle of non-

[11] Right to marriage.

[12] Overview of CEDAW, See Cedaw Aware, http://cedaw.aware.org.sg/what-is-cedaw/ site accessed on 15 April 2018

[13] Article 16 (Right to property marriage and dissolution), CEDAW.

[14] *Ibid*. at Articel 16(1) (c)

[15] Article 27, The Constitution of the People's Republic of Bangladesh

[16] *Ibid*. at Article 19.

discrimination is declared in Articles 28[17] and 29. Although Article 28(2) excludes personal laws and practices from protection, clause 4 also empowers the state to enact special provisions for the development of women or children. Even though the state claims to be a secular one, its reservations to CEDAW have not been withdrawn and there have been no state initiatives to eliminate the discriminatory provisions of Hindu laws. These initiatives are necessary if changes to discriminatory laws are sought.

ICCPR ensures equality before the law and equal protection of law without any discrimination on the basis of race, colour, sex, language, religion, political or other opinion, national or social origin, property, birth or other status.[18] The ICCPR specifically provides for equal rights of spouses, and the right to marriage and divorce. Article 23(d) of ICCPR says that –

> States Parties to the present Covenant shall take appropriate steps to ensure equality of rights and responsibilities of spouses as to marriage, during marriage and at its dissolution. In the case of dissolution, provision shall be made for the necessary protection of any children.

Similarly, ICESCR provides the principle of non- discrimination and ensures equality between men and women[19] upon which Bangladesh has reservations.[20] Article 3 reads-

> The States Parties to the present Covenant undertake to ensure the equal right of men and women to the enjoyment of all economic, social and cultural rights set forth in the present Covenant.

Bangladesh has acceded to both of the covenants of ICCPR and ICESCR in the years 2000 and 1998 respectively.

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17 Article 28 enunciates that-
(1) The State shall not discriminate against any citizen on grounds only of religion, race, caste, sex or place of birth.
(2) Women shall have equal rights with men in all spheres of the State and of public life.
(3) No citizen shall, on grounds only of religion, race, caste, sex or place of birth be subjected to any disability, liability, restriction or condition with regard to access to any place of public entertainment or resort, or admission to any educational institution.
(4) Nothing in this article shall prevent the State from making special provision in favour of women or children or for the advancement of any backward section of citizens.

18 Article 26 (Law to prohibit discrimination), ICCPR.

19 Article 2(2) provides that, "The States Parties to the present Covenant undertake to guarantee that the rights enunciated in the present Covenant will be exercised without discrimination of any kind as to race, colour, sex, language, religion, political or other opinion, national or social origin, property, birth or other status".

20 It reserves the right to interpret the labour rights in Articles 7 and 8 and the non-discrimination clauses of Articles 2 and 3 within the context of its constitution and domestic law.

B. The Convention on Consent to Marriage, Minimum Age for Marriage, and Registration of Marriages 1962

The Convention on Consent to Marriage, Minimum Age for Marriage and Registration of Marriages 1962 (the Convention on Consent to Marriage) was a treaty agreed upon in the UN on the standards of marriage.[21] Bangladesh acceded to the treaty in 1998 with reservations to Articles 1 and 2. These two articles deal with the free consent of parties and the minimum age of marriage.[22] Article 3 of the treaty also provides for the compulsory registration of marriage to a competent authority. Registration of Muslim marriages are compulsory,[23] whereas, the registration of Hindu marriages is still optional.[24] This is clearly a non-compliance with the Convention on Consent to Marriage.

It is generally accepted that principles of international law, whether customary or treaty-based, are normative by character and are binding on states, still, controversies persist over the degree and extent to which these norms may be invoked and enforced.[25] While the rights in question must already be a part of domestic law, their nature and scope may be affected by customary international law.[26] Unavoidably, Bangladesh is under an obligation to abide by the principles of equality and non-discrimination as it is the moral duty upon the state to ordain domestic law in a manner that does not breach international law.

III. HINDU MARRIAGE LAWS IN SOUTH ASIAN COUNTRIES: ADDRESSING DISCRIMINATION IN BANGLADESH'S LEGAL REGIME

Hindu personal laws are based on Hindu *Dharma* which has its origins in India.[27] Hindu Law is divine in nature which can be observed from the words of Manu,[28] (the prominent *Smriti*[29] writer) and *The Veda*.[30] The *Smriti* is the approved usage and what is agreeable to one's soul (good conscience), which the wise have declared to be the quadruple direct

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21 The treaty was opened for signature and ratification by General Assembly resolution 1763 A (XVII) on 7 November 1962 and entered into force 9 December 1964 by exchange of letters, in accordance with Article 6.

22 Shahnaz Huda, Combating Gender Injustice Hindu Law in Bangladesh, The South Asian Institute of Advanced legal and Human Rights Studies (SAILS), 2011, p.12.

23 Section 3, The Muslim Marriages and Divorces (Registration) Act, 1974, Act no. LII.

24 Section 3, The Hindu Marriages Registration Act, 2012, Act no. XL.

25 *Supra* n 4, at p. 49.

26 *Supra* n 4, at p. 53.

27 Dr. Rabia Bhuiyan, Gender and Tradition in Marriage and Divorce, 1st ed., United Nations Educational, Scientific and Cultural Organization, 2010, p. 31.

28 The code of Manu was compiled between 2000 BC to 200 AD.

29 *Smriti* means 'what is remembered'. It refers to the utterance and precepts of the Almighty which have been remembered and handed down by the sages from generation to generation.
(D F Mulla, Principles of Hindu Law 15thEd., N M Tripathi Private Limited, Bombay 1982, p. 20.

30 *Veda* is the compilation of *Sruti* meaning 'what is heard and is believed to contain the very word of God.' Norshivan H Jhavala, Principles of Hindu Law 20thed., C. Jamnadas and Co. Educational and Law Publishers, Mumbai 2009, p. 3.

evidence of *Dharma*.[31] While marriage among the Muslims is a civil contract, among the Hindus it is a sacred ceremony. According to John D Mayne,[32] the purpose of a Hindu marriage is to acquire a male heir who has the capacity to confer spiritual benefit upon the deceased at the funeral ceremony. In the absence of any legislative enactments, Bangladesh continue to follow the ancient principles of Hindu Law. A Hindu marriage is conducted following multiple ceremonies and registration is not necessary. Most astoundingly, the marriage cannot be dissolved as divorce is not available under the ancient Hindu law provisions.

The application of this law discriminates against women and is against the principles of equality and non- discrimination. The neighbouring countries of Bangladesh namely, India, Pakistan and Nepal, have amended the ancient *Shastriya* Hindu law which are discriminatory towards women. India and Nepal, being Hindu majority countries addressed the orthodox law by enacting the Hindu Marriage Act in 1955 and the *Muluki Ain* in 1963, Nepal followed suit in 2019. Pakistan, being a country with a Muslim majority, has also brought landmark changes in Hindu personal laws by enacting the Hindu Marriage Act of 2015. The cultural pattern and socio-economic infrastructure of Bangladesh is fairly similar to its neighbouring countries, yet it has noticeably been reluctant to change this orthodox law. Hereafter, the article will discuss the relevant laws and will attempt to identify the practical reasons behind the disinclination to reform the Hindu laws in Bangladesh.

A. Requirements for a Hindu Marriage

In Bangladesh, the orthodox Hindu law imposes restraint on inter-caste marriages, disapproving the marriages conducted within prohibited degrees. Parties to the marriage have to be beyond the prohibited degrees of relationship, i.e. not of the same *gotra*[33] or *pravara*[34] and not the *sapinda*[35] of each other.[36] The marriage is only completed when all the ceremonies are performed. Moreover, an infant's marriage is deemed complete and legal in Hindu law.[37] Even though the *Shastriya* law imposes restriction on inter-caste

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31 Norshivan H Jhavala, *Principles of Hindu Law,* 20thEd., C. Jamnadas and Co. Educational and Law Publishers, Mumbai 2009, p. 3.

32 John Dawson Mayne, *The Treatise on Hindu Law and Usage*, 7thEd., 1906, Madras: Higgingbotham.

33 Two persons are '*sagotra*' if both of them descend in the male line from rishi or sage after whose name the gotra is called, however distant either of them may be from the common ancestor (D F Mulla, *Principles of Hindu Law*, 15th Ed., N M Tripathi Private Limited, Bombay 1981, p. 436).

34 Two persons are said to belong to the same *pravara*, if they are descendants in the male line from three paternal ancestor of the founder of a gotra (D F Mulla, *Principles of Hindu Law*, 15th Ed., N M Tripathi Private Limited, Bombay 1981, p. 561).

35 *Sapindas*, according to the *Dayabagha* school of law, are the persons who are connected by the offerings of the funeral cake or '*pinda*' (R K Agarwala, Hindu Law, 20th ed., Central Law Academy Allahabad, 2000, p. 35).

36 Mahua Zahur, "The Hindu Marriage System in Bangladesh: Addressing Discrimination", *Commonwealth Law Bulletin*, 2014.

37 Gooroodass Banarjee, *The Hindu Law of Marriage and Stridhan*, Thacker, Spink and Co., Calcutta, 1879, p. 111.

marriages, this has increased. According to Human Rights Watch,[38] inter-caste marriages are occurring more frequently now-a-days with the change in the collective mindset of Hindus from all castes. Depending on the educational qualification, professional diversity and financial status, inter-caste marriages are being solemnised and accepted by the society. The Hindu Marriage Disabilities Removal Act 1946 has paved the way for marriages between the Hindus belonging to the same *gotra* or *pravara*.[39]

If we pay attention to the Hindu law in India, it can be observed that the Hindu Marriage Act of 1955 has rectified the prevalent orthodox practices of *Shastriya* law. This Act has an overriding effect on all other laws and traditional practices. It is undoubtedly a reflection of the modern thought of the people at that time. The conditions and requirements to conduct a Hindu marriage provided by this Act have considerably been simplified.[40] With regards to the prohibited degree of relationship, it has specifically mentioned the lineage of progenitors between whom solemnisation of marriage is prohibited. Now marriage can be solemnised beyond these degrees.[41] The Act of 1955 has rendered the restrictions on inter-caste marriage as obsolete. As such, the division and discrimination as to caste is no longer as prevalent. If the marriage fulfills the conditions provided by the Act, it will not be nullified just because it has been solemnised between parties belonging to a different caste or sub-caste.[42]

B. Hindu Marriage Ceremonies

In Bangladesh, a Hindu marriage is ceremonious. The marriage is not complete without observing these preceding and following these wedding rituals. But the question of what formalities create the valid status of a marriage cannot be answered precisely and requires the social consideration of a particular community.[43] In the *Amulya Chandra Modak* case[44] two ceremonious requirements for a valid marriage were established, one is *viva homa* or invocation before the holy fire and another is *saptapadi* or the taking of seven steps around the holy fire. In this case, Kalpana Rani (who was 18 years old) was induced into believing that she was married to the appellant on the ground that they had

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38 "Will I Get My Dues…Before I Die?": Harm to Women from Bangladesh's Discriminatory Laws on Marriage, Separation and Divorce; Human Rights Watch 2012.

39 *Supra* n10, at Article 2.

40 Section 5, The Hindu Marriage Act, 1955, Act XXV.

41 According to section 3(g) of the Act, "degrees of prohibited relationship" means two persons- (i) if one is a lineal ascendant of the other; or (ii) if one was the wife or husband of a lineal ascendant or descendant of the other; or (iii) if one was the wife of the brother or of the father's or mother's brother or of the grandfather's or grandmother's brother or the other; or (iv) if the two are brother and sister, uncle and niece, aunt and nephew, or children of brother and sister or of two brothers or of two sisters. "Explanation- for the purposes of clauses (f) and (g) relationship includes- (i) relationship by half or uterine blood as well as by full blood; (ii) illegitimate blood relationship as well as legitimate; (iii) relationship by adoption as well as by blood; and all terms of relationship in those clauses shall be construed accordingly.

42 According to section 29(1)- A marriage solemnised between Hindus before the commencement of this Act, which is otherwise valid, shall not be deemed to be invalid or ever to have been invalid by reason only of the fact that the parties thereto belonged to the same *gotra* or *pravara* or belonged to different religion, castes or sub-divisions of the same caste.

43 Werner Menski, Hindu Law, Beyond Tradition and Modernity,1st ed., Oxford University Press, 2003, p. 278.

44 *Amulya Chandra Modak v the State* [1986] 35 DLR 35.

secretly exchanged garlands. She had consented to cohabiting with the appellant and subsequently became pregnant. The learned judges opined that Kalpana Rani was matured enough to understand that various compulsory rites like *viva homa* and *saptapadi* were not performed. Kalpana could not have believed that by the mere exchange of garlands with the accused, he had become her lawful husband.

The court acquitted the appellant from the charge of deceit. Due to the non-performance of the aforementioned two important ceremonies the marriage was invalidated. Due to the divergence of ceremonies the presumption of marriage is often at the discretion of the court. In another case of *Ramesh Chandra Adhikari v Bulbuli,*[45] a dispute arose about the presumption of marriage. In this case, even though the ceremonies were not properly held, circumstances suggested that there was a presumption of an existing marriage even though the defendant-appellant denied the fact. This is due to the absence of any statutory provision as to the mandatory ceremonies that had to be completed before a marriage is valid. Identifying the existence of marriage can be quite complicated thus giving rise to disputes.

As regards to the ceremonies to be followed in India, the Hindu Marriage Act of 1955 has upheld the customary rites and ceremonies of the parties. It states that, where '*saptapadi*' is included, marriage becomes complete and binding when the seventh step is taken.[46] By dint of this Act, the rituals of marriage have been simplified which eradicates the complications that arise as to the presumption of marriage.

The Marriage Registration Act of 1971 in Nepal is more progressive in nature. It has stipulated that no particular ceremonies are to be performed by the parties. If any party wants to follow any religious, ethnic or dynastic custom, tradition, usage or practice, it has to be addressed in front of the Marriage Registration Officer and witnesses.[47] Due to these provisions in India and Nepal, the solemnisation of a Hindu marriage has become much easier. Even though, Bangladesh shares a similar Hindu culture, it is left out of the positive transformations in Hindu law.

C. The Polygamous Nature of Hindu Marriage

The practice of polygamy in Hindu law evolved from necessity rather than from the desire of men. There are circumstances when a Hindu man may engage himself to more than one marriage, for example, for the procreation of a male issue.[48] The law prevalent for the Hindus in Bangladesh allows polygamy, though it is not an ideal practice in society. Hindu men may take as many wives as they want. They are not required by law to seek permission from the existing wife or any authority, and they do not have to fulfill any conditions before remarrying. However, polyandry is not permitted by law. As dissolution of marriage is not legally possible, a Hindu men may marry innumerable times even after deserting his wife. But a Hindu woman cannot even dissolve a marital tie

45 3 LNJ (AD) (2014) 49.

46 Section 7 (1), (2), the Hindu Marriage Act, 1955, Act XXV.

47 Section 8(2), The Marriage Registration Act, 2028 (1971).

48 *Supra* n 27, at p. 154.

that is unhealthy and unsatisfying and cannot remarry. She may however ask for judicial separation and maintenance.[49]

By the application of the Hindu Marriage Act of 1955, polygamy is now prohibited in India. Section 5 of the Act stipulates that neither party can have a living spouse at the time of marriage. Further, section 11 of the Act has declared that any such polygamous marriage as null and void. So now, in India, a Hindu man cannot have more than one wife. Section 17 of the Act provides for the punishment of such acts. Due to this express provision, bigamy is also removed from Hindu marriages. If such a marriage is solemnised between two Hindus while an existing spouse is alive, the marriage is considered void. The provisions of Sections 494[50] and 495[51] of the Indian Penal Code (45 of 1860) shall consequently apply. It makes polygamy a punishable offence and says that such marriage will be void; the husband or wife will be fined or punished for a term that may extend to seven years. In the case of concealment of the fact of a previous marriage, the husband or wife will be punished with a fine or imprisonment for a period that may extend to ten years. Previously, a Hindu man could marry without being accountable to his partner with little recourse available to the Hindu woman. These provisions have undeniably safeguarded the rights of Hindu women in the country.

Similarly, Nepal (who has a majority Hindu population) has brought dramatic changes by liberalising the ancient Hindu law principles. It has prohibited polygamy through the Marriage Registration Act of 1971. The provisions of this Act stipulates that marriage may be entered into if the male or female has no other husband or wife.[52] However, the Civil Code of the State (The *Muluki Ain*) mentions some grounds when a male may keep an additional wife, namely, if the wife has any contagious venereal disease which has become incurable, if she has become incurably insane, if no offspring has been born because of the wife, if she becomes crippled, if the wife becomes blind of both eyes and if she takes partition share from him pursuant to No. 10502 of the Chapter on Partition and lives apart. [53]

By dint of the Hindu Marriage Act 2017 Pakistan has prohibited bigamy for both male and female. The only exception says that, a man may remarry if his spouse cannot

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49 Section 2(4), The Hindu Married Women's Right to Separate Residence and Maintenance Act, 1946, Act XIX.

50 Marrying again during the lifetime of husband or wife: Whoever, having a husband or wife living, marries in any case in which, such marriage is void by reason of its taking place during the life of such husband or wife, shall be punished with imprisonment of either description for a term which may extend to seven years, and shall also be liable to fine. Exception: This Section does not extend to any person, whose marriage with such husband or wife has been declared void by a Court of competent jurisdiction, nor to any person who contracts a marriage during the life of a former husband or wife, if such husband or wife, at the time of the subsequent marriage, shall have been continually absent from such person for the space of seven years, and shall not have been heard of by such person as being alive within that time provided the person contracting such subsequent marriage shall, before such marriage takes place, inform the person with whom such marriage is contracted of the real state of facts so far as the same are within his or her knowledge.

51 Same offence with concealment of former marriage from person with whom subsequent marriage is contracted: Whoever commits the offence defined in the last preceding section having concealed from the person with whom the subsequent marriage is contracted, the fact of the former marriage, shall be punished with imprisonment of either description for a term which may extend to ten years, and shall also be liable to fine.

52 *Supra* n 47, at. Section 4(a).

53 Number 9, Chapter 17, *Muluki Ain* of Nepal, 2019 (1963), Act LXVII.

conceive a child and is medically declared to be so.[54] Any Hindu marriage solemnised while parties have a spouse living at the date of such marriage will be void. Similar to the Indian Act, this Act also declares polygamy as a punishable offence; applying Sections 494 and 495 of the Pakistan Panel Code 1860 accordingly.[55] Besides rendering the marriage as void, it has also provides for punishment of a fine or imprisonment for a term that may extend to seven years. The concealment of the fact of former marriage will give rise to a fine or imprisonment that may extend to ten years. Hindus are a minority in Pakistan as they are in Bangladesh. It is noticeable that even though it is an Islamic state, the rigorous modifications that have been brought by the Act of Pakistan is very appreciable.

D. Optional Registration of Marriage

Prior to 2012, there were no provisions for the registration of Hindu marriages in Bangladesh. As such, when a Hindu woman's marriage was challenged, she would face tremendous difficulty in proving her marriage.[56] Different potential problems arose due to the absence of any legal rule for registration of Hindu marriage, such as, proving the fact of marriage when the husband denies it, proving the legitimacy of children, maintenance of the wife, remedy in criminal cases arising due to family violence.[57] Post 2012, the enactment of the Hindu Marriage Registration Act 2012 has brought some changes to the primordial rule of Hindu marriage. It provides for the registration of Hindu marriage, though this is optional.[58] Theoretically, it has paved the way for the discriminatory law to change, however, reality suggests that this has not been the case.

In India, Section 8 of the Hindu Marriage Act of 1955 provides for the registration of Hindu marriages. It has declared the registration of marriage compulsory and anyone contravening the provision would be fined an amount which may extend to twenty five rupees.[59] However, the validity of any marriage will not be affected if it is not registered.[60] The mandatory registration of marriage may have had the effect of remarkably lessening the rate of denial of marriage. In Bangladesh, due to lack of compulsory registration the presumption of marriage depends on the contemplation of the performance of different ceremonies.

The Marriage Registration Act 1971 of Nepal provides that marriage is to be concluded through registration. The marriage concluded must be registered by the Marriage Registration Officer pursuant to Section 8 in the marriage register. Before concluding a marriage pursuant to this Act, the parties to the marriage and at least three witnesses shall sign a deed of declaration (affidavit) in a prescribed format and submit it to the Marriage Registration Officer.[61] By evaluating the laws prevalent in Nepal, it is

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54 Proviso Section 4(d), The Hindu Marriage Act, 2017, Act VII.

55 *Ibid* at Section 20.

56 *Swapon Kumar Gain v Amita Goldar* [2006] 58 DLR 26.

57 *Supra* n 22, at p. 19.

58 *Supra* n 24, at Section 3(2).

59 *Supra* n 46, at Section 8(2).

60 *Supra* n 46, at Section 8(5).

61 *Supra* n 47, at Section 8(1).

evident that a marriage may be concluded in the simplest way where no complication arises. Discriminatory provisions that are contrary to the spirit of the Constitution are no longer in practice.

Pakistan has also made a radical change in their Hindu marriage laws by enacting the Hindu Marriage Act of 2017. Hindus may solemnise their marriage following all the rituals and ceremonies[62] but it must be registered. Section 6(1) 0f the Act provides for a time period of fifteen days for registration after the solemnisation of such marriage. Anyone violating the provision relating to registration will be punishable under Section 23 of the Act with imprisonment for a term which may extend to three months or with fine which may extend to one thousand rupees or both.

The provision of optional registration of Hindu marriage in Bangladesh does not only trigger an oppressive situation but also creates legal complications. The Registration document is proof of a valid marriage which cannot be presented where the official document is asked for, like in the case of a visa application. Whereas the abovementioned countries have made it compulsory, the optional registration in Bangladesh has rendered it an ineffective one.

IV. DISSOLUTION OF HINDU MARRIAGE IN SOUTH ASIAN COUNTRIES: IS BANGLADESH'S PROVISION AN OPPRESSIVE ONE?

For the Hindus, as *Shastra* the marital bond is unbreakable. It is an eternal and indissoluble holy union. *Shastriya* law does not allow for the dissolution of marriage under any circumstances, even after the death of the husband. Manu observes, *"Let mutual fidelity continue until death. This is the summary of the highest law for husband and wife"*. There are divergence of opinions as to whether divorce is permitted by *Shastriya* law or not. The dominant view is that divorce is not permissible at all as the eternal bond is irrevocable. However, there is also much evidence in the long-established existence of various ancient customary forms of divorce among Hindus.[63] As per the ancient Hindu law divorce was observed in exceptional circumstances. According to Narada,[64] women were allowed another husband in certain situations, such as, where there is no trace of the husband, or that he is dead, or had converted into another religion, or was impotent, or had become an outcaste. Under almost similar circumstances, the dissolution of a marriage was supported by Parasara.[65]As a male child is an essential progeny in Hindu marriage, its absence affected dominantly while considering divorce. In some communities, divorce is allowed by custom and the courts enforced such custom provided they fulfilled the

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62 *Supra* n 54, at Section 5.

63 R K Agarwala, Hindu Law, 20th Ed., Central Law Academy Allahabad, 2000, p. 437.

64 Narada is an ancient Smriti writer and has notably progressive views on law. He has addressed age of majority and recognized separation and remarriage by a woman in certain circumstances. D F Mulla, Principles of Hindu Law, 15thed., N M Tripathi Private Limited, Bombay 1981, p. 28.

65 Parasara is also an ancient *Smriti* writer. He has recognised the usages and customs of the people as transcendent law.
D F Mulla, Principles of Hindu Law, 15th Ed., N M Tripathi Private Limited, Bombay 1981, p. 31.

requisites of a valid custom.[66] The practice of divorce is prevalent among the lower castes. However, it does occur among *Bramins* as well, although this fact is still highly controversial. Werner Menski pronounces, *"*Many texts point to certain circumstances in which separation may be necessary in view of higher concerns. Where there are no children, or if the wife (and sometimes the husband) seriously misbehaves, then this may be a ground for changing the marriage partner. Whether this is called to be a divorce, or something else, has become a controversial topic."[67] Till today Bangladesh follows the *Shastra.*[68] Hindu women have no right to seek a divorce. By dint of the Special Marriage Act of 1872, Hindus may marry outside of their religion or outside their caste. The Divorce Act of 1869 is applicable for the parties who contract marriages under the Special Marriage Act of 1872,[69] but to solemnise such marriages, the parties must declare that they do not profess any religion.[70]

Bangladesh, albeit being a secular country, does not embrace any measures to reform the prejudiced *Shastriya* law unlike India, Pakistan and Nepal. The principle of non-discrimination is professed in Articles 28 and 29 of the Constitution of People's Republic of Bangladesh. But Article 28(2) excludes personal laws and practices from protection and thus personal laws of different religions prevail unsorted. Even though there is no provision for Hindu divorce, Hindu women can seek a court decree for a separate residence and maintenance on few grounds[71] under the Hindu Married Women's Right to Separate Residence and Maintenance Act of 1946. She can – (1) ask for a judicial separation in case her husband suffers from a loathsome disease; (2) if he remarries or keeps a concubine; (3) if he abandons her or does any act of cruelty to her; or (4) if he converts to a different religion. Even this right to separate residence and maintenance is not an exhaustive one. A Hindu married woman shall not be entitled to such right from her husband if she is unchaste or ceases to be a Hindu. Moreover, she also loses the right if she fails to comply with a court decree for the restitution of conjugal rights. Judicial separation does not serve the purpose of separating one from the oppressed life. As polygamy is allowed in Hindu law, the husband may remarry. But the wife cannot remarry and start a new life.

A. The Constitution of the Republic of India 1950

The Constitution declares that India is a sovereign, socialist, secular, and democratic republic. It assures its citizens, justice, equality and liberty.[72] Article 14 of Part 3 of the Constitution provides for equality of every citizen before the law like that of Bangladesh.

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66 *Sankaralingam v Subban* [1894] ILR 17 Mad. 479.

67 *Supra* n 43, at p. 433.

68 Work of sacred scripture in Hindu *Dharma*.

69 Section 17, the Special Marriage Act, 1872, Act III.

70 *Ibid.* at Section 2.

71 *Supra* n 49, at Section 2 -(a) He is suffering from any loathsome disease; (b) he is guilty of cruelty towards his wife; (c)he is guilty of abandoning her against her wish; (d) he remarries; (e) he converts to another religion; (f) he keeps a concubine; and (g) any other justifiable cause.

72 Preamble, The Constitution of Republic of India.

Article 16 further provides that the state shall not discriminate against any citizen on the grounds of religion, race, caste, sex, place of birth or any of them. Aligned with the constitutional provisions of the country, the Hindu Marriage Act was enacted in 1955. It has since brought about drastic changes in the law. The primeval law has been substituted with new laws ensuring the concept of equality. The concerns regarding marriage and its dissolution are now dealt with without discriminating between a Hindu husband and wife. The Act of 1955 offers the equal right to divorce to Hindu husband and wife. Section 13 of the Act provides for dissolution of marriage to both Hindu man and woman on a number of modern fault grounds.[73]Adultery, unsound mind, incurable disease of leprosy, venereal diseases, polygamy and cruelty are grounds under the Hindu Marriage Act of 1955[74] to apply for a divorce. Besides, the Act provides special provision for the Hindu wife for the dissolution of the marriage in certain circumstances such as, if a Hindu male remarries, the wife may ask for divorce. She can also seek divorce due to rape, sodomy or bestiality of the husband.[75] These provisions are unquestionably a cutting-edge in eliminating the discrimination that has long been in existence.

B. The Constitution of Nepal 2015

The preamble of the Constitution of Nepal 2015, states that the State of Nepal upholds the essence of the principle of non-discrimination by eliminating discrimination based on class, caste, region, language, religion and gender and all forms of caste-based untouchability. Part 3 of their Constitution provides for the fundamental rights of the citizen where right to equality[76] is listed as one of such rights. It ensures that no discrimination shall be made among people on the grounds of origin, religion, race, caste, tribe, sex, economic condition, language, region, ideology or any other similar grounds. Furthermore, Article 38 of the Constitution ensures equal rights of women in every sector. Spouses shall have equal rights to property as well as in family affairs.[77]

With regards to the dissolution of marriage, Nepal established landmark reforms. Its Civil Code has provided for the right to dissolve a marriage by a wife. Chapter 12, No. 1 of the *Muluki Ain* provides the grounds of dissolution of marriage by the husband as well as by the wife. [78] If a wife has left her husband and lived separately for a continuous period of three years or more without his consent, or she has carried out any such act or intrigue or conspiracy as is designed to put an end to the husband's life, lead to his physical disability or result in any other severe physical or mental[79] suffering to him, or the wife suffers from any incurable venereal disease[80] or the wife is held to have sexual intercourse with any other man, the husband may dissolve his relation with

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73 *Supra* n 27, at p. 238.

74 *Supra* n 46, at Section 13.

75 *Supra* n 46, at Section 13(2).

76 Article 18, The Constitution of Nepal 2015.

77 *Ibid*. at Article 38(6).

78 Part 3.

79 Inserted by the Eleventh Amendment.

80 *Supra* n 53, at Chapter 12.

such a wife. Accordingly, it also says, if a husband has brought or kept another wife or banished her from the house, or not provided her with food and clothes or left the wife and lived separately without seeking any news of her and without taking care of her for a continuous period of three years or more or carried out any such act or intrigue or conspiracy designed to put an end to her life, lead to her physical disability or result in any other severe physical or mental[81] suffering to her or has become impotent, or the husband suffers from any incurable venereal disease[82] or the husband is held to have sexual intercourse with any other woman or the husband is held to have raped the wife as mentioned in Section 6 of Number 3 of the chapter on rape,[83] the wife may dissolve her relation with such a husband. The laws in Nepal do not provide unfettered right to a husband to divorce his wife and it also provides equal opportunity to the wives to dissolve any detrimental relation of marriage, unlike Bangladesh.

C. The Constitution of the Islamic Republic of Pakistan 1973

This Constitution also enshrines the principle of equality. Article 25A of part 2, Chapter 1 of the Constitution provides that everyone is equal before the law and no one shall be discriminated on the basis of sex. Being an Islamic State, Pakistan preserves the principles of democracy, freedom, equality, tolerance and social justice as enunciated by Islam.[84] It ensures adequate provisions for the minorities to freely profess and practice their religion and culture.[85] A momentous change related to issues under Hindu divorce was made when Pakistan enacting the Act of 2015. It was a much-awaited Act which obtained approval by Pakistan's Senate in 2017. The Act makes provision for the annulment of a Hindu marriage for both husband and wife on the grounds of adultery, cruelty, deserting the spouse for a period of not less than 2 years, conversion to another religion, spouse being incurably of unsound mind or mental disorder, incurable form of leprosy, venereal disease or HIV and if the spouse renounce the world by entering any religious order.[86] Moreover, the Act provides special grounds for the wife for the termination of her marriage.[87] Remarriage of the husband, rape or cruelty towards the wife, if the marriage was solemnised before the attainment of eighteen years by the wife; no matter if the marriage is consummated or not, these are considered as valid grounds for the annulment of the marriage by the wife.

D. The Position in Bangladesh

By discussing the Hindu Divorce laws in India, Nepal and Pakistan, it can be identified that these countries have developed their laws illuminating the principles of human rights jurisprudence and Constitutional provisions. Revolutionary laws have been enacted,

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81 *Ibid.*

82 *Ibid.*

83 Inserted by Some Nepal Acts to Maintain Gender Equality Amendment Act, 2063 (2006).

84 Preamble, The Constitution of the Islamic Republic of Pakistan 1973.

85 *Ibid.*

86 *Supra* n 54, at Section 12(1)(a).

87 *Supra* n 54, at Section 12(2).

with Bangladesh being the only exception. Even if we consider the fact that Hindus are a minority community in the country, Pakistan has a similar background; and despite being an Islamic state they have adopted crucial changes to eliminating the discriminatory provisions of the *Shastriya* law. It is a matter of great regret that even after being a secular state Bangladesh has not been able to make any such changes. Bangladesh stands alone when it follows the *Shastriya* prejudicing the lives of Hindu women. Even though some reforms have been introduced in case of Mohammedan law, Hindu laws remain unchanged. Recently in 2012, the Hindu Marriage Registration Act was enacted but the law does not render the registration of Hindu marriage compulsory.[88] Section 3 of the Act provides for the registration of a Hindu marriage, but if it is not registered the validity of the marriage will not be affected. As it is optional the court cannot confer any legally binding order, rather it depends upon the parties.

Hindu women in Bangladesh can go to the court to ask for remedies in certain cases such as dowry, non-maintenance, suppression and violence. Under section 3 of the Family Court Ordinance 1985, a Hindu wife can institute a suit against her husband for maintenance. The Dowry Prohibition Act 1980 and the *Nari-o-Shishu Nirjatan Daman Ain* of 2000 provides remedies for women and children in case of dowry and oppression. These Acts could not guarantee apposite fairness to them because even if they can ask for punishments and compensation for certain offences, they cannot divorce their husband. Hence, no matter how oppressed she is, she has to endure the conjugal life anyway or stay separately, but cannot dissolve the marriage as it is irrevocable. As there is no divorce for Hindu wives in Bangladesh, no opportunity for post-divorce maintenance is present unlike the Mohammedan law. The principles of equality and non-discrimination are enshrined in every Constitution. The states' initiative should be in compliance with these constitutional frameworks. The other South Asian countries mentioned in this paper have adopted more secular and non-discriminative provisions, leaving Bangladesh unaccompanied within the spectrum of Hindu personal laws.

V. REFORM AGENDA ON HINDU PERSONAL LAWS IN BANGLADESH: PRACTICAL REASON BEHIND RELUCTANCE IN MODIFYING THE EXISTING LAW

It is really disheartening that after a long time Bangladesh is still following the age-old orthodox laws even after the constitutional framework towards non-discriminatory and secular approach were put in place. Several proposals were made like, the Hindu Marriage, Adoption, Maintenance and Succession Related Codified Act 2006 by the Bangladesh Law Commission;[89] the Hindu Personal and Family Laws Ordinance 2008 by the Human Rights Congress of Bangladesh Minorities (HRCBM)[90] and the Hindu Marriage Act 2010

88 Section 3.

89 Bangladesh Law Commission (BLC) is a statutory body established by the Law Commission Act of 1996.

90 HRCBM is an international campaigning movement dedicated to protecting the human rights of people in Bangladesh, in particular religious minorities.

by the Coalition for the preparation of a Draft Hindu Marriage Law.[91] However, till today, the initiative to reform the present law by the parliamentarians remains unattended. Why are discriminatory Hindu laws still unattended to? This paper poses the question with a great surprise which needs to be resolved.

The United Nations Educational, Scientific and Cultural Organization (UNESCO) along with the non-governmental organisations for women prepared a report in 2005 entitled 'Marriage, inheritance and family laws in Bangladesh: towards a common family code' and submitted it to the government of Bangladesh.[92] After reviewing the proposal it concluded that a Uniform Family Code (UFC) would be impossible to achieve in Bangladesh's reality because the religious beliefs of different communities differ in terms of its origins, basis and faith.[93] Setting aside the concept of UFC, the idea of enacting a new law for the Hindus in Bangladesh has not been successful till now. Given the existing patriarchal rule and orthodox religious belief, the Hindu community does not seem encouraged to take any such initiative to reform the law. In 2011, the much debated Women's Policy announced by the Government reiterated the State's desire to ensure gender equality.[94] The policy also has implications for the rights of Hindu women but it was opposed vehemently by fundamentalist groups. Till today, the existing structure of society does not want to offer equal opportunities to the women. Though the mindset of modern Hindus are changing, a major section of society still believes in *Shastriya*. The spur of the religion is so resilient that many Hindu women themselves do not want to change the customary law, where any contradiction to it is considered a sinful deed.

VI. SUGGESTIONS FOR FUTURE INITIATIVES AND CONCLUDING REMARKS

As the idea of a UFC is not possible to implement in the current social arrangement, the legislators should take the initiative to consider enacting a new law by addressing the discrimination of prevailing Hindu laws. For example, the provision of registration of Hindu marriage should be made mandatory (rather than keeping it optional) to avoid various legal complication. Conducting a marriage should be kept as simple as possible, preserving the ceremonies to be followed should be decided by the parties. Polygamy should to be prohibited except in extraordinary circumstances. Most importantly, the provision of divorce by both the Hindu husband and wife needs to be introduced. If the purpose of marriage is not served and a sacred bond turns out to be prejudicial to their lives, it is better to dissolve the relationship.

A radical change cannot be made at once to reform the personal laws in Bangladesh, but initiatives should be taken to reform the separate provisions which are discriminatory, and which violate the egalitarian principles of human rights. At present time, the Hindu

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91 Under the initiative of '*Manuser jonno* Foundation' (MJF) and '*Bachte Shekha'*, a coalition of 17 NGO's was formed to propose reforms to the laws relating to Hindu Marriages in Bangladesh.

92 *Supra* n36.

93 *Supra* n36.

94 *Supra* n22, at p. 11.

community is gradually accepting the principle of equality. It is hoped that the government of Bangladesh would continue to address and reform the laws to comply with the constitutional provisions and existing international covenants.

Foreclosing on a Loan Agreement cum Deed of Assignment (Completing the Puzzle): A Review of the Federal Court Decision in *Damai Freight v Affin Bank Berhad*

Mark Goh Wah Seng*

I. INTRODUCTION

The Federal Court in *Damai Freight v Affin Bank Berhad*[1] *(Damai Freight)* had finally resolved the conundrum surrounding situations where the Issue Document of Title (commonly known as the 'title') of a property is issued but is not transferred to the assignor whilst the lender is foreclosing a property secured by a Loan Agreement cum Deed of Assignment (LADA).

A lender (usually the bank) may face various legal challenges which may affect the legality of its foreclosure proceeding if the title is issued before the lender completes the foreclosure under a LADA.[2] Should the bank complete its foreclosure under the LADA, despite the issuance of the title?[3] Will the bank be in breach of the National Land Code (NLC) if it proceeds to foreclose under the original LADA?[4]

If the bank decides to adopt the safer route of registering the Charge and recommencing foreclosure proceedings under the NLC, it would have lost valuable time, money and effort in its original foreclosure proceedings under the LADA. Alternatively, if the bank chooses not to register the Charge, it runs the risk of the court declaring the entire foreclosure proceedings void once the assigned property is issued with a title.

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1 *Damai Freight v Affin Bank Berhad* [2015] 4 MLJ 149.

2 The rationale for having the Deed of Assignment as a form of security was explained by Dr. Wong Kim Fatt in his article entitled "Absolute Assignment: Lender Selling Without Court Order?", *Malayan Law Journal,* [2002] 3 MLJ, p. cclxix.

3 *Ibid*. The same question was also raised by Dr. Wong Kim Fatt at pp. cclxxxvi where he questioned whether, 'after default of payment by the borrower/purchaser and the exercise by the lender of its right to sell the assigned property without a court order, must the lender now obtain a court order for sale if the strata title is issued before the sale or after the sale but before its completion?'.

4 '… the provisions of the Code as to the rights of chargors are designed for their protection and cannot be waived; nor can the chargor contract himself out of the Code. It follows that no power of sale can be conferred by a chargor under the Code on a chargee himself by way of a debenture or power of attorney or otherwise, but proceedings must be brought by the chargee to obtain a judicial sale in accordance with the rigid procedure laid down in the Code. In such circumstances, any power of sale which purports to be conferred on a chargee himself, omitting all mention of notice and periods of default by a debenture or power of attorney and the necessity for obtaining a judicial sale would be invalid and ineffective to entitle a purchaser to be registered as owner. Per his Lordship Edgar Joseph J in *Kimlin Housing Development Sdn Bhd (Appointed Receiver and Manager) (In Liquidation) v Bank Bumiputra (M) Bhd & Ors* [1997] 2 MLJ 805, p. 823.

This confusion was further compounded by two High Court decisions;[5] each case approving two diametrically opposing legal positions of law on this matter.[6] This legal issue which has been baffling practitioners (i.e. what steps should a lender take when an individual title is issued but is not transferred to the assignor whilst the lender is foreclosing a property secured by a LADA) was finally resolved by the Federal Court in *Damai Freight.*[7]

This article does not intend to discuss the legality of the assignment as opposed to a charge nor does it attempt to critically analyse Section 3 of the Civil Law Act 1956 or the judiciary's recognition of the concept of 'equitable mortgage' in Malaysia. Separate articles should be devoted to these issues. Instead, this article aims to justify the decision of the Federal Court decision in *Damai Freight* from various aspects of the law, particularly from the aspect of land law and the law on assignment.

II. THREE POSSIBLE STAGES WHERE AN INDIVIDUAL TITLE MAY BE ISSUED DURING A FORECLOSURE PROCEEDING.

Throughout a foreclosure proceeding under the LADA, the title of an assigned property may be issued at three different stages: (a) where the title is issued and transferred to the original assignor before foreclosure proceedings under the LADA commences; or (b) where the title is issued during the foreclosure proceedings (i.e. the period between the commencement of the foreclosure proceeding and completion of the auction); or (c) where the title is issued after the completion of the foreclosure proceedings.

This article will focus on the most contentious stage i.e. stage (b) where the title is issued during the period between the commencement of the foreclosure proceeding and completion of the auction.

III. WHERE THE INDIVIDUAL TITLE IS ISSUED DURING FORECLOSURE PROCEEDINGS UNDER THE LADA

In *Damai Freight*, the appellant had obtained the approval of the Selangor State Development Corporation, the *Perbandaran Kemajuan Negeri Selangor* (PKNS) to alienate a piece of land to the appellant. Pending issuance of the individual title to the said land, the appellant entered into a Lease Agreement with PKNS (Lease).The appellant subsequently took a loan totaling RM1.95 million from the respondent bank (which was then known as *Bank Buruh*). The loan was secured by a LADA of the Lease wherein

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5 *Ooi Chin Nee v Citibank Bhd* [2003] MLJU 5, HC and *Hong Leong Bank Bhd v Goh Sin Khai* [2005] 3 MLJ 154, HC.

6 In *Hong Leong Bank Bhd v Goh Sin Khai* [2005] 3 MLJ 154, the High Court held at para 63 that 'there is no statute or rule in common law that once an individual title or strata title is issued, the absolute assignment is extinguished.' Conversely, the High Court in *Ooi Chin Nee v Citibank Bhd* [2003] MLJU 5, p.22 held that 'in pursuance of their contractual rights, when there is an issue document of title as in this case, the plaintiff must get the property transferred to his name and then register a charge in favour of the defendant/bank.'

7 *Supra* n1.

the appellant had amongst others "absolutely assigned all its rights, title and interest"[8] under the Lease to the respondent. Around the time when the appellant had defaulted in its loan agreement, unbeknown to the respondent, the individual title to the said land was also issued. The respondent bank proceeded to sell the lands under the LADA. The respondent objected to the foreclosure, arguing amongst others that "the respondent bank had no right to enforce the LACA (LADA) and that the sale by the [respondent] bank was *ultra vires* the National Land Code 1965."[9] The sole issue of law which the Federal Court had to answer was this:

> Could a lender having an absolute assignment of rights over the land continue to realise his security under the LACA (LADA) even though the title to the said land was subsequently issued?

IV. THE LEGAL POSITION OF AN ASSIGNMENT IN A LADA

Before deciding on the appropriate steps which a lender should adopt, the Federal Court had to first consider the legal position of an assignment under a LADA.

After referring to Section 4(3) of the Civil Law Act 1956[10] and Mozley & Whiteley's[11] definition of a 'chose in action', his lordship Abdul Hamid Embong had rightly concluded that an assignment being a 'chose in action' is a personal right to sue.[12] The same view was also expressed by the court in *Bachan Singh v Mahinder Kaur & Ors*[13] where the court had observed that in a sale and purchase of land, the purchaser was only entitled to a right in *personam* in a nature of a chose in action when the contract was made.[14]

In the English case of *Torkington v Magee*[15] his lordship Channell J held that the expression 'chose in action' clearly describes "a known legal expression used to describe

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8 *Supra* n1, para 4.

9 *Supra* n1, para 10. Loan Agreement cum Assignment (LACA) was cited verbatim from the decision.

10 "Any absolute assignment, by writing, under the hand of the assignor, not purporting to be by way of charge only, of any debt or other legal chose in action, of which express notice in writing has been given to the debtor, trustee or other person from whom the assignor would have been entitled to receive or claim the debt or chose in action, shall be, and be deemed to have been, effectual in law, subject to all equities which would have been entitled to priority over the right of the assignee under the law as it existed in the State before the date of the coming into force of this Act, to pass and transfer the legal right to the debt or chose in action, from the date of the notice, and all legal and other remedies for the same, and the power to give a good discharge for the same, without the concurrence of the assignor." Section 4(3) Civil Law Act 1956 (Malaysia).

11 See also *Hong Leong Bank Bhd v Sum-Projects (Brothers) Sdn Bhd* [2010] 7 CLJ 1010, at para 19.

12 See also Dr. Wong Kim Fatt, "Absolute Assignment: Lender Selling Without Court Order?", *Malayan Law Journal,* [2002] 3 MLJ p. cclxix.

13 *Bachan Singh v Mahinder Kaur &Ors* [1956] 1 MLJ 97.

14 "…the point is that when that contract was made the purchasers acquired a right ad rem and in personam to the land which so far as the vendor was concerned they were entitled to have erected into a real right. I am not prepared to say that that amounted to an equitable right. I prefer to regard it as a legal right of the nature of a chose in action". *Bachan Singh v Mahinder Kaur &Ors* [1956] 1 MLJ 97, 98.

15 *Torkington v Magee* [1902] 2 K.B. 427.

all personal rights of property which can only be claimed or enforced by action and not by taking physical possession". [16]

Adopting the descriptions above, it therefore follows that the assignment which a purchaser has assigned to the bank under the LADA as security for the bank's loan is not an interest in land but merely a chose in action or a bundle of rights in the contract.[17]As a right in *personam,* the court observed that it "is [a]contractual right or benefit accruing under the Principal Agreement [the main Sale and Purchase Agreement].[18] An assignment merely transfers the chose in action to the banker.[19] These contractual rights collectively amounts to a legal chose in action. They cannot and must not be equated to *ownership* in immovable property.[20] Once the loan has been fully repaid, that chose in action is capable of being retransferred or reassigned to the borrower."[21]

This leads us to the next question; what are the legal effect(s) which flows from the fact that an assignment is only a personal right but not a right *in rem?*

V. THE EFFECT OF AN INDIVIDUAL TITLE ON A FORECLOSURE PROCEEDING UNDER THE LADA

As a chose in action, the assignment of rights by the assignor to the lender (usually the bank) is not considered as 'dealings' within the National Land Code. Hence, it does not come within the purview and control of the National Land Code nor the Strata Titles Act 1985.[22] Instead, the assignment is a contract entered between the lender and the assignor. This view was fortified by the Court of Appeal in *Hong Leong Bank Bhd v Tan Siew Nam & Anor*[23] where it was decided that the LADA is essentially "a contract between the [parties] where the [lender had] agreed to grant to the [borrower/assignor]

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16 *Supra* n 14, at p. 430.

17 See S.Y. Kok, "A Review of Loan Agreements and Deed of Assignment (Absolute) under the Malaysian Torrens System", *Current Law Journal, [1994] 2 CLJ p xxxv*.

18 "Where there is a valid binding contract for the sale of land, the purchaser, when he has performed his side of the contract, acquires a right ad rem which is also a right in personam. In other words, he acquires a right to the land as against the vendor personally but not good against the world as a whole and, in due course, that right can become a real right good against the world as a whole on registration in accordance with the Land Code…" *Bachan Singh v Mahinder Kaur &Ors* [1956] 1 MLJ 97, p. 98.

19 "… it must be clearly understood that what is capable of being assigned under the deed of assignment absolute … is only a legal right (a right of action at law or a right in rem) to the debt or the chose in action. At the time of giving notice to the other person from whom the assignor could have been entitled to receive the debt or specifically enforce his claim to the chose in action, the legal right of action at law will pass and transfer from the assignor to the assignee absolutely. This is quite different from the transferring of the ownership in immovable property which will require the State's magical act of registration in order to be effective. The assignee practically steps into the shoes of the assignor vis-À-vis the other person from whom the assignor could have been entitled to receive the benefit of and under the antecedent contract." SY Kok, A Review of the Court of Appeal Case of *Phileoallied Bank v Bupinder Singh and the Deed of Assignment* by Way of Charge Only, *Malayan Law Journal*, [2000] 1 MLJ lxv, p. lxxiv.

20 *Supra,* n18, at p. xc.

21 *Hong Leong Bank Bhd v Tan Siew Nam & Anor* [2014] 5 MLJ 34, para 72.

22 *Hong Leong Bank Bhd v Goh Sin Khai* [2005] 3 MLJ 154 was approved by the Federal Court in *Damai Freight v Affin Bank Berhad* [2015] 4 MLJ 149, at para 33.

23 *Hong Leong Bank Bhd v Tan Siew Nam & Anor* [2014] 5 MLJ 34.

a loan in exchange for the repayment of that loan with interest." The Court of Appeal rightly observed that "…The root of the loan transaction was not the property itself [as] the property merely served as a security for the repayment of the loan."[24] Thus being a contract, the rights of the assignment are governed solely by the terms which had been agreed between the bank and the borrower.[25]

One of the common agreed terms found in loan agreements which are commonly drafted to the bank's advantage would usually state that: 'Upon issue of a separate document of individual title to the said Land…the Borrower shall… *upon being so required to do by notice in writing from the Bank* take transfer or and execute a charge over the separate document of individual title…'. [emphasis added]

According to the Federal Court in *Damai Freight*, the abovementioned clause (and its variations) amounts to nothing more than a right or privilege that is extended to the lender under a contract.[26] Such a clause, as decided by the Federal Court in *Damai Freight,* does not make the creation of a charge a prerequisite (or condition) for the bank to proceed with foreclosure,[27] neither can the court compel the bank to register the charge when the court has no power to do so.[28] Since the bank cannot be forced to register a charge once the individual title to the land is issued, the bank should therefore (be allowed to) continue with the foreclosure proceedings which it started under the LADA even though the individual title was issued during the foreclosure process.[29]

Secondly, by affirming various cases,[30] the Federal Court in *Damai Freight* had effectively dismissed the argument that an absolute assignment will automatically be

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24 *Supra* n1, at para 53. See also the Federal Court decision in *Chuah Eng Khong v Malayan Banking Bhd* [1999] 2 CLJ 917 where it was held that an assignment is no more than a mere security given by the respondents to the appellant for repayment of the loan.

25 See the Federal Court in *PhileoAllied Bank (M) Bhd v Bupinder Singh a/l Avatar Singh* [2002] 2 MLJ 513, where it was held that "All things considered… that in the absence of any statutory provisions or common law requiring the equitable mortgagee to obtain a court order to realize its security under an absolute assignment of rights to land, the court should give effect to and recognise the contractual rights as determined between the vendor and the purchaser." Affirmed by the Federal Court in *Samuel Naik Siang Ting v Public Bank Bhd* [2015] MLJU 519*,* at para 44.

26 "On the plain reading of these two clauses, we agree with the submission of learned counsel for the bank that these clauses only confer contractual rights or privileges to the bank in terms of the execution of a charge upon the issuance of the separate document of individual title in respect of the land. In our considered view, the Bank is not, however, obliged to ensure the execution of the charge and thereafter to obtain an order for judicial sale before it could proceed to exercise its rights under the LACA upon the appellant's default under the loan. The underlined phrases in both sub-clauses above are manifestations of these rights of the bank." See *DamaiFreight,* n.1, para 30.

27 *Supra* n1, at para 31. See also the High Court in *Ruzain Zainudin & Anor v RHB Bank Berhad* [2011] 1 LNS 1196 where the Court was unable to find in the LADA any provision which makes it a "MUST" for the defendant to issue a notice to the plaintiffs to execute the Memorandum of Transfer and Charge. On the contrary, what the Court observed was an obligation on the plaintiffs themselves to take a transfer of and to execute a first legal charge in favour of the defendant. This they should do at their own cost and expense. They should also do so if so required by the defendant so to do.

28 See *Re Robinson, Pickard v Wheater* [1886] 31 Ch D 247, 249 referred to by the Federal Court in *PhilleoAllied Bank (Malaysia) Bhd v Bupinder Singh Avatar Singh & Anor*[2002] 2 MLJ 513.

29 *Supra* n1, at para 32.

30 High Court in *Hong Leong Bank Berhad v Goh Sin Khai* [2005] 3 MLJ 154, para 6; High Court in *Ruzain Zainudin & Anor v RHB Bank Berhad* [2011] 1 LNS 1196, para 45.

extinguished once the document of title is issued.[31] In fact, the term LADA fortifies the view that the deed and the terms of the loan cannot and should not be extinguished immediately because various negative legal implications may flow from an invalid assignment.

First and foremost, the automatic extinguishment of the assignment will effectively cause the security granted by the assignor to the lender to 'disappear' during the period between the creation and the registration of the individual or strata title in the name of the assignor, thereby causing the loan to be temporarily unsecured! The security will only 'reappear' or be secured again after the charge is registered in the lenders/bank's name. During this period, the financier's security will be at risk. This creates a dangerous lacuna in the law which serves only to benefit the assignor.[32] Financial institutions will not be willing to lend money for properties without individual titles, resulting in commerce coming to a grinding halt if this position is adopted. This cannot possibly be the legal position.

Secondly, the extinguishment of the deed of assignment will unjustly enrich the assignor which falls within the law of unjust enrichment. Recognised as an independent branch of law,[33] the law of unjust enrichment is neither "consent based nor wrong based".[34] It aims to restore any enrichment which one party may have obtained against the other. The principle behind unjust enrichment lies in the fact that no one should be made richer through the loss to another.[35] Hence, the law of unjust enrichment aims to restore that enrichment back to the claimant. In order to prove unjust enrichment, the Federal Court in *Dream Property Sdn Bhd v Atlas Housing Sdn Bhd*[36] had establish four elements; they are a) that the party was enriched; b) the enrichment must be gained at the [party's] expense; c) the retention of the benefit by the party was unjust; and d) there must be no defence available to extinguish or reduce the party's liability to make restitution.[37]

In his article entitled "An Introduction to the Law of Unjust Enrichment" by Alvin W-L See, the learned author listed various ways where a party's benefit may be unjust.[38] Amongst others, it includes the (total) failure of consideration and a compulsory discharge of another's debt.[39]Applying these two factors given by the author in the said article, it is submitted that if an assignment is dissolved once an issue document of title is issued, this will automatically cause a (total) failure of consideration and a discharge of the

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31 *Supra* n1, at para 37.

32 "This leads to a dangerous state of affair that can have far-reaching implications on the bank sector. If the assignment is extinguished by the mere fact that a strata title has been issued, the assignor would be in a position to deal with the property and the financier's security is at risk". See *Hong Leong Bank Berhad v Goh Sin Khai* [2005] 3 MLJ 154, at para 21.

33 *Dream Property Sdn Bhd v Atlas Housing Sdn Bhd* [2015] MLJU 33 at para 112.

34 Alvin W-L See, "An Introduction to the Law of Unjust Enrichment", *Malayan Law Journal,* [2013] 5 MLJ, p. xxv.

35 *Supra* n 34 at para 108.

36 *Supra* n 33.

37 *Supra* n 34, para. 117.

38 *Supra* n 34.

39 *Supra* n 34, at p. xxvi.

assignor's debt since the security for the debt is extinguished. As a result, the borrower will be unjustly benefiting from the loan he has obtained from the bank.

In *RHB Bank Bhd v Travelsight (M) Sdn Bhd & Ors and another appeal,*[40] whilst recognising that the LADA is different and independent from the sale and purchase agreement, the Federal Court had decided that even though the original security of the LADA may be lost or altered, the validity of the assignment remains. Thus, the bank's rights to lay the first claim over the assignor's property continues to remain intact even though the nature of assignor's property may have changed; be it in money or otherwise.

The third effect is highlighted by the case of *Goh Sin Khai.*[41] After conducting an extensive review of the NLC, the High Court decided that the assignor is not compelled by the NLC or the contract to register his name in the title once the individual title is issued.[42] This observation was duly affirmed by the Federal Court in *Damai Freight*.[43] Thence, to impose an obligation on the lender to register its charge when the assignor himself is not obliged to do so would not only be impracticable and unfair for the lender,[44] it will also create a lacuna in the law which benefits the assignor in a foreclosure proceeding. This view was succinctly stated by Justice Syed Ahmad Helmy in *Goh Sin Khai* when his lordship observed that "creating legal obstacles or unnecessary procedural impediments for an equitable mortgagee to realise the security is…unsound as it only serves to expose both lender and borrower to greater risks rather than bring any commercial benefit to either."[45]

Furthermore, as mentioned above, the rights so assigned under the LADA are not recognised by the NLC as 'dealings'.[46] Instead, they are contractual rights which though are independent of the NLC are nevertheless recognised under Section 206 (3) of the NLC.[47] Section 206(3) "serves to remind us that 'nothing in sub-section (1) shall affect

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40 [2016] 1 MLJ 175.

41 *Hong Leong Bank Bhd v Goh Sin Khai* [2005] 3 MLJ 154.

42 "There is no statute or rule in common law that once an individual title or strata title is issued, the absolute assignment is extinguished. Likewise, there is nothing to say that the assignee must extinguish the assignment by ensuring the assignor takes a transfer of the property and creates a charge in favour of the lender." See *Hong Leong Bank Bhd v Goh Sin Khai* [2005] 3 MLJ 154, at para 63.

43 *Supra* n. 1, para 33.

44 "The correct legal position may be stated as follows. When a property is reassigned to a borrower, it means that the bank executes a document relinquishing its security over the property. It cannot be equated with an obligation on the part of the bank to deliver title or possession of the property to the borrower. It is the developer who is obliged to deliver the property to the borrower after construction of the property and issuance of the strata/individual title." Court of Appeal in *Hong Leong Bank Bhd v Tan Siew Nam & Anor* [2014] 5 MLJ 34, para 62.

45 *Hong Leong Bank Bhd v Goh Sin Khai* [2005] 3 MLJ 154, para 66.

46 See *Chung Khiaw Bank Ltd v Hipparion (M) Sdn Bhd* [1988] 2 MLJ 62, p. 66. "That assignment cannot by any stretch of imagination be termed a 'dealing' with or in respect of land within the meaning of the Code. It only serves to transfer and vest in the second purchaser the rights and interest of the first purchaser under the sale and purchase agreement with the developer." High Court in *Hong Leong Bank Bhd v Goh Sin Khai* [2005] 3 MLJ 154, p. 68 as affirmed by the Federal Court in *Damai Freight (M) SdnBhd v Affin Bank Berhad* [2015] 4 MLJ 149, para 36.

47 "…our present NLC recognises the contractual operation relating to land as envisaged under Section 206(3) of the NLC, apart from the other dealings mentioned under Sections 206(1) which requires the compliance of instrument in accordance with sections 207 to 212 and registration under Part Eighteen of the NLC." Federal Court in *Damai Freight (M) SdnBhd v Affin Bank Berhad* [2015] 4 MLJ 149, para 39.

the contractual operation of any transaction relating to alienated land or any interest therein."[48] It therefore follows that until and unless the individual title of the property is registered in the assignor's name, the security under the LADA will continue to be governed by the contractual terms between the parties[49] including the sale of the property during a foreclosure proceeding. These rights, labeled as "pre-registration contractual right" or "the unregistered registrable interest"[50] will remain valid in all aspects even though it does not come within the purview of the NLC.[51]

VI. CONCLUDING REMARKS

The Federal Court decision in *Damai Freight* is a landmark decision which has brought much clarity to this area of land law in Malaysia. The judges must be applauded for a well-researched and thoroughly grounded judgment. Although the issuance of land titles is beyond the control of assignees and assignors alike, the case of *Damai Freight* has provided lenders (particularly financial institutions) with clear guidelines on the proper steps the lenders should take if titles are issued during foreclosure proceedings.

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48 *Chung Khiaw Bank Ltd v Hipparion (M) Sdn Bhd* [1988] 2 MLJ 62, p. 66.

49 "Malaysian courts have held that the contractual principles of law will govern the sale and purchase of land transaction until the registration of title, Tan Hooi Ping, "Seeking Specific Performance In Cases of Breach of Sale and Purchase of Land in Malaysia — An Analysis", *Malayan Law Journal* , [2013] 2 MLJ clv, p. clxiii.

50 S.Y. Kok, *The Torrens System and Equitable Principles,* Sweet & Maxwell Asia, Petaling Jaya, 2010, pp 521–523 referred to by Tan Hooi Ping, *Seeking Specific Performance in Cases of Breach of Sale and Purchase of Land in Malaysia — An Analysis*, [2013] 2 MLJ clv, clxiv.

51 "Section 206 (3) of the NLC, by providing a liberal application of equity, recognises the contractual operation of any transaction relating to alienated land or any interest therein. In this regard, we see no reason as to why a similar recognition could not be accorded to the Bank in exercising its power of sale over the Land in accordance with the contractual provisions under the LACA." Federal Court in *Damai Freight (M) SdnBhd v Affin Bank Berhad* [2015] 4 MLJ 149, para 41.