PRE-EMPTIVE RIGHTS TO NEW SHARES

Pre-emptive Rights are statutory rights accorded to the holders of existing shares (“Existing Shareholders”) by virtue of Section 85(1) of the Companies Act 2016 (“CA 2016”). It provides that, subject to the constitution, where a company issues shares which rank equally to existing shares in terms of voting or distribution rights, those shares shall first be offered to the Existing Shareholders. This is to ensure that the relative voting and distribution rights of the Existing Shareholders would be maintained if the offer were accepted.

Such an offer shall be made to the Existing Shareholders in a notice specifying the number of shares offered and the time frame of the offer. If the offer is not accepted after the expiry of the period specified in the notice, it would be deemed to be declined and the directors may proceed to dispose those shares in such manner as the directors think most beneficial to the company.

The Pre-emptive Rights are typically found to be incorporated in the companies’ constitution which is also known as the contractual Pre-emptive Rights.

COMMON PRACTICE IN MALAYSIA

It is not unusual to find that most of the ordinary resolutions prepared by the Malaysian companies do not specifically set out the Pre-emptive Rights of the Existing Shareholders, with the assumptions that the Existing Shareholders would be aware of the likelihood of the dilution of their shareholding in the event of issuance of new shares and have impliedly agreed to waive the exercise of their Pre-emptive Rights when they approve such resolutions.
DENIAL OF STATUTORY AND CONTRACTUAL PRE-EMPTIVE RIGHTS

It was not until the recent Court of Appeal’s decision in Concrete Parade Sdn Bhd v. Apex Equity Holdings Bhd & Ors [2021] 9 CLJ 849 which held that an Existing Shareholder cannot be denied its Pre-emptive Rights unless there is “direction to the contrary” given during a general meeting, prior to such new shares being offered to outsiders.

In this case, the Court of Appeal disagreed with the High Court’s judgment that there had not been any contravention of the rights of pre-emption due to the fact that the placement has been approved by the shareholders at the extraordinary general meeting. It was, on the other hand, of the view that no resolution passed at a general meeting can completely displace the Existing Shareholders’ Pre-emptive Rights in the new shares. This was what sought to be done in this case via the subscription agreements where the breach was held to be oppressive and the issuance of the placement shares under the subscription agreements constitutes an unfairly prejudicial conduct within the meaning of Section 346 of the CA 2016, as it had resulted in:

i) the unjustified dilution of the appellant’s shareholding in the company as an additional 20 million new shares had been issued to the outsiders despite the statutory safeguard in Section 85 of the CA 2016, where the legislative intent was to “maintain the relative voting and distribution rights of the Existing Shareholders”; and

ii) the loss of opportunity to enhance the appellant’s shareholding in the company by subscribing for part of the placement shares.

The Court further emphasised that a resolution does not constitute a “direction to the contrary” for the following reasons:

i) A “direction to the contrary” must be obtained before any shares are offered to outsiders. In this case, the resolution was passed after the subscription agreements were signed for the offer of the placement shares to the seven placees. It follows that the resolution could not retrospectively allow the issuance of new shares to outsiders, in breach of Section 85 of the CA 2016.

ii) For a “direction to the contrary” to be operative, the proposed resolution must set out all the requisite information regarding the Existing Shareholders’ Pre-emptive Rights under Section 85(1) of the CA 2016 i.e.:

a) The Existing Shareholders had a statutory Pre-emptive Right to be offered any new shares which rank equally to existing shares issued by the company;

b) By voting in favour of the resolution for the issuance of the new shares, the Existing Shareholders would be waiving their Pre-emptive Rights; and

c) A waiver is only effective if the party waiving it had knowledge of his legal rights and with that knowledge consciously chose not to exercise the same.
**PRACTICAL GUIDE**

i) Although Section 75 of the CA 2016 grants directors the general power of allotment of shares in a company, it cannot be invoked to bypass the safeguards under Section 85 of the CA 2016. The Pre-emptive Rights must be waived via ordinary resolution. This is because Section 85 of the CA 2016 is not subjected to Section 75 of the CA 2016 and the former is only subjected to the constitution which makes no reference to the latter. Further, the express wording of Section 75 of the CA 2016 states that the directors “shall not exercise any power to allot shares in the company” unless the prior approval by way of resolution by the company has been obtained.

ii) The resolution must at least set out expressly that the Existing Shareholders have the statutory and contractual Pre-emptive Rights and by voting in favour of the resolution, the Existing Shareholders will waive their respective Pre-emptive Rights.

iii) Waiver of Pre-emptive Rights must be obtained before new shares are offered not on a pro-rata basis.

iv) For public listed companies, the Pre-emptive Rights cannot be removed by the company’s constitution despite Section 85 of the CA 2016 says “subject to constitution”. Pre-emptive Rights are required to be incorporated into the constitution of public listed companies pursuant to Paragraph 7.08 of the Main Market Listing Requirements (“MMLR”).

v) Set out below are some of the circumstances where waiver is required to be sought for new issuances in public listed companies:

a) General mandate for issue of securities in accordance with Paragraph 6.03 of the MMLR and Section 75 of the CA 2016;

b) Issue of securities in accordance with Paragraph 6.05 of the MMLR and Section 75 of the CA 2016;

c) Allotment of shares to directors etc. in accordance with Paragraph 6.06 of the MMLR;

d) Issue of convertible securities in accordance with Part I, Chapter 6 of the MMLR;

e) Share issuance scheme or share grant scheme in accordance with Part G, Chapter 6 of the MMLR; and

f) Dividend reinvestment scheme in accordance with Part G(A), Chapter 6 of the MMLR.