Corporate insolvency and corporate rehabilitation

THIS ARTICLE HIGHLIGHTS THE MAIN CHANGES TO THE CORPORATE INSOLVENCY AND REHABILITATION PROCEDURES UNDER THE COMPANIES BILL 2013

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The Companies Bill 2013 (Bill), which revamps the Companies Act 1965 (Act), is based on the recommendations made by the Corporate Law Reform Committee ("CLRC") back in 2008. The Companies Commission of Malaysia published a copy of the Bill for public consultation and is presently reviewing the feedback received.

This article will touch on areas of the Bill which help to reform the existing areas of receivership and winding up. In order to better promote a corporate rehabilitation framework, this article will expand on how the Bill also introduces the new mechanisms of the judicial management scheme and the corporate voluntary arrangement.

RECEIVERSHIP

Appointment

The receivership provisions in the Bill substantially expand on the existing provisions in the Act. Clauses 372 and 373 of the Bill set out the manner of appointing a receiver or a receiver and manager ("R&M") under an instrument or by the Court.

Clause 372(2) of the Bill expressly sets out the agency status of a receiver appointed under a power conferred by an instrument (and presumably, the final version will also spell out the corresponding status of an R&M).

The present legal position is that a receiver or R&M becomes an agent of the debtor company by virtue of the inclusion of provisions to that effect in the debenture under which he is appointed. The codification of the agency status of the receiver and R&M helps to remove some of the present ambiguities on the status of the receiver or R&M. It makes clear the ability of the receiver or R&M to contract on behalf of the company or do any act as an agent of the company to enable him to perform his functions.

In the case of a Court appointment, clause 373 of the Bill lists out three specific grounds upon which the Court may appoint a receiver or R&M, which are essentially where the company has failed to pay a debt due to a debenture holder, or the company proposes to sell the secured property in breach of the charge, or it is necessary to do so to preserve the secured property.

However, the Bill appears to omit other instances under the common law where a Court may appoint a receiver or R&M, such as where there is a management deadlock or oppressive conduct by

the shareholders. It is hoped that these omissions will be clarified in the final version of the Bill so that these common law rights of appointment will not be abrogated.

Personal Liability of the Receiver and R&M

The original recommendation by the CLRC in its Final Report was for the receiver or R&M to be personally liable for debts incurred by him unless there is a specific agreement to the contrary between the contracting parties. However, clause 378 of the Bill does not make this clear and in fact imposes personal liability for such debts incurred by him in the course of receivership "notwithstanding any agreement to the contrary", thereby not allowing the parties to contract out of this provision.

Further, the wordings which impose personal liability described above appear to conflict with clause 379(2) which purports to give effect to the CLRC's recommendation that the "terms of a contract … may exclude or limit the personal liability of the receiver …"

Powers of Receiver and R&M

Clause 380 of the Bill introduces a welcomed codification of the express powers of a receiver or R&M which are set out in the Seventh Schedule of the Bill. Presently, a receiver or R&M would have to derive his powers solely from the provisions of the debenture under which he was appointed, and it is not uncommon to encounter situations where the powers listed in the debenture are inadequate or ambiguous.

WINDING UP

Presentation of a Petition

Clause 447(1)(a) of the Bill increases the threshold of a debt for the statutory demand from RM500 to RM5,000 in order for a company to be deemed unable to pay its debts for the purposes of a compulsory winding up.

This higher threshold attempts to balance the need to ensure that the amount is not too high as to preclude small creditors from initiating legitimate claims whilst being high enough to avoid trivial claims.

Further, clause 447(2) of the Bill states that a winding up petition must be filed within six months from the expiry date of the statutory demand. The aim of this is to reduce the possibility of the statutory demand being abused and to prevent the threat of a winding up petition from continuing to hang over the debtor company for an inordinately long period of time.

Void Dispositions

The void disposition provision as contained in clause 453 of the Bill makes it clear that any disposition of property by the company, other than an exempt disposition, made after the presentation of a winding up petition shall be void, unless the Court orders otherwise. Similar to the equivalent Australian provision, the intent of this amended provision is to list out certain exempt dispositions which would not require a validation order by the Court.

However, the specified exempt dispositions contained in clause 453(2) do not significantly eliminate the need to obtain a validation order as it covers only a disposition by a liquidator or an interim liquidator of the company.

Powers of Liquidators

The powers of the liquidator in a court winding up situation are set out in clause 468 read with the Eleventh Schedule of the Bill. Part I of the Eleventh Schedule lists out the powers that the liquidator may exercise with the authority of the Court or the committee of inspection ("COI") while Part II of the Eleventh Schedule lists out all the powers that may be exercisable with, or without, the aforesaid authority.

In particular, the Bill permits a liquidator to carry on the company's business so far as necessary for the beneficial winding up of the company for a period of 180 days after the making of the winding up order. Thereafter, the liquidator is required to obtain the authority of the Court or the COI to continue with the carrying on of such business. This is a welcomed increase from the present period of only four weeks allowed for under the Act.

Termination of Winding Up

Under the Act, the only way in which a winding up order can be brought to an end is through an order for a stay of winding up under Section 243 (and the provision for a stay of winding up is preserved in clause 476).

The Bill introduces a new clause 477 which allows the Court to also terminate the winding up of a company. In determining whether to terminate a winding up, the Court may consider various factors, such as the satisfaction of the debts, the agreement by both parties, or other facts as it deems appropriate. The termination of winding up, instead of a stay, appears to allow for an easier route to bring to an end the winding up where the debtor company has satisfied the debts owing to the petitioning creditor.

JUDICIAL MANAGEMENT

The judicial management mechanism, modelled after the Singapore model, is a new component under the Bill to provide a further option to rehabilitate a financially distressed company. It allows for an application by a company or a company's creditors for an order to place the management of a company in the hands of a qualified insolvency practitioner. A moratorium which gives temporary respite to the company from legal proceedings by its creditors is put in place automatically both during the time of the application for a judicial management order until the making or dismissal of such an application and during the period that the judicial management order is in force.

Requirements for the Grant of a Judicial Management Order

The Court is empowered under clause 392 of the Bill to grant a judicial management order if and only if -

a) it is satisfied that the company is or will be unable to pay its debts; and

b) it considers that the making of the order would be likely to achieve one or more of the following purposes:
   i) the survival of the company, or the whole or part of its undertaking as a going concern;
   ii) the approval of a compromise or arrangement between the company and its creditors;
   iii) a more advantageous realisation of the company's assets would be effected than on a winding up.

The judicial management order shall, unless discharged, remain in force for 180 days and may be extended on the application of the judicial manager for another 180 days.

Protection of Debenture Holder's Rights

The CLRC had made recommendations to protect a debenture holder's right to appoint an R&M in the situation where a judicial management order is sought. Accordingly, clause 395(1)(b) of the Bill requires the notice of a judicial management application to be provided to any person who has appointed, or may be entitled to appoint, an R&M of the whole or a substantial part of the company's property. However, clause 395(1)(b) limits the type of qualifying R&M as one appointed under the terms of a debenture secured by a floating charge or by a floating charge and one or more fixed charges. It does not seem to apply to a situation where the security is by way of a fixed charge only and is unclear as to whether it applies to a receiver as well.

This provision is significant as clause 396 of the Bill effectively provides a veto right to a person who is entitled to appoint a qualifying R&M. Clause 396(1)(b) of the Bill provides that the Court shall dismiss a judicial management application if the making of the order is opposed by a person who has appointed, or is entitled to appoint, such a receiver or R&M.

The reasoning behind such a veto right is that it is thought not necessary to make a judicial management order when an R&M could achieve substantially the same objectives and clause 396(1)(b) preserves the right of the debenture holder to appoint an R&M.

Approval of Judicial Manager's Proposals

When a judicial manager is appointed, clause 407 of the Bill provides that he has 60 days (or such longer period as the Court may allow) to send to the Registrar, members and creditors of the company a statement of his proposals for achieving the purposes for which the order was made and to lay a copy of this statement before a meeting of the company's creditors.

As a meeting of the creditors must be summoned on not less than 14 days' notice, the judicial manager effectively only has 46 days to come up with the proposal to rehabilitate the company. Therefore, there is the view that the Bill's 60-day period may in reality be too short unless the Court is more flexible in allowing for more time for the preparation of this statement of proposals.

Clause 408(2) of the Bill requires a judicial manager's proposals to be approved by a majority of 75% in value of the creditors present and voting either in person or in proxy whose claims have been accepted by the judicial manager. Once approved by the required majority, the proposals shall be binding on all creditors of the company whether or not they had voted in favour of the proposals.

CORPORATE VOLUNTARY ARRANGEMENT

The corporate voluntary arrangement ("CVA") is modelled after the corresponding provisions under the UK Insolvency Act. The CVA is a procedure which allows a company to put up a proposal to its creditors for a voluntary arrangement. The implementation of the proposal is supervised by an independent insolvency practitioner who would report to the Court on the viability of the proposal. There is minimal Court intervention in the process.

Initiation of CVA

To initiate a CVA, the directors would have to submit to the nominee, being a person who is qualified to be appointed as an approved liquidator, a document setting out the terms of the proposed voluntary arrangement and a statement of the company's affairs.

Under clause 422 of the Bill, the nominee shall then submit to the directors a statement indicating whether or not in his opinion:

a) the proposed CVA has a reasonable prospect of being approved and implemented;

b) the company is likely to have sufficient funds available for it during the proposed moratorium to enable the company to carry on its business; and
c) that meetings of the company and creditors should be summoned to consider the proposed CVA.

Under clause 421 of the Bill, once the directors have received a positive statement from the nominee, they can then file this statement with the Court together with the other necessary documents, such as the nominee's consent to act and the document setting out the terms of the proposed CVA.

Moratorium and Required Majority to Approve the Proposal

Upon the filing of the relevant documents pursuant to clause 421, the Ninth Schedule of the Bill provides that a moratorium commences automatically and shall remain in force for a period of 28 days.

Clause 423 of the Bill also provides that once the moratorium is in force, the nominee is to summon a meeting of the company and its creditors within the period specified in the Eighth Schedule of the Bill. The reference in clause 423 to the Eighth Schedule appears to be a typographical error and the correct reference should be to the Ninth Schedule of the Bill.

Under the Ninth Schedule, such a meeting of the company and creditors must be called within 28 days of the date of the filing of the documents in Court. At the company's meeting, a simple majority is required to pass a resolution to approve the proposed CVA while at the creditors' meeting, the required majority is 75% of the total value of the creditors present and voting in person or by proxy.

If more time is needed for the stakeholders to decide, and in order to extend the moratorium period beyond the initial 28-day period, a meeting can be summoned to extend the moratorium for not more than 60 days if there is approval of 75% majority in value of the creditors and with the consent of the nominee and the members of the company.

CONCLUSION

The Bill brings many welcomed changes in revamping the corporate insolvency and rehabilitation framework in Malaysia. It is hoped that the final Bill will reflect the feedback and comments received through the public consultation process.

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