LHAG Insights

Insolvency Feature

ABOUT THE AUTHORS

Kumar Kanagasingam
Senior Partner
Banking & Insolvency
E: kk@lh-ag.com

Sean Yeow Huang-Meng
Partner
Banking & Insolvency
E: yhm@lh-ag.com

Andrew Chiew Ean Vooi
Partner
Banking & Insolvency
E: ac@lh-ag.com

Mong Chung Seng
Partner
Banking & Insolvency
E: mcs@lh-ag.com

Law and Practice

Contributed by Lee Hishammuddin Allen & Gledhill (Kuala Lumpur – HQ)

1 State of the Restructuring Market

1.1 Market Trends and Changes

Malaysia unfortunately suffered consecutive economic contractions due to the three COVID-19 lockdown measures that have been implemented since March 2020, with small and medium-sized enterprises (SMEs) and micro-enterprises being hit the hardest. Sectors such as travel, leisure, hospitality, tourism, airline and retail were severely impacted.

The Malaysian government encouraged private debt workout arrangements between businesses and financiers, along with implementing aid and economic stimulus packages. In July 2021, the central bank – Bank Negara Malaysia (BNM) – announced that SMEs and micro-enterprises can apply for a moratorium and repayment assistance for loan and financing repayment. Stamp duty exemptions were given on the restructuring and rescheduling of loan/financing agreements.

Notable applications and decisions on voluntary restructuring through schemes of arrangement and judicial management were reported in 2021, involving public listed corporations like AirAsia X Bhd, Scomi Group Bhd, Boustead Holdings Bhd and Top Builders Capital Bhd. Meanwhile, the Securities Commission Malaysia (SC) continued to grant extensions or flexibilities to give capital market intermediaries time to make certain regulatory filings and put regularisation plans in place amid the COVID-19 pandemic (see www.sc.com.my).

LH AG ADVOCATES AND SOLICITORS

2 Statutory Regimes Governing Restructurings, Reorganisations, Insolvencies and Liquidations

2.1 Overview of Laws and Statutory Regimes

The Companies Act 2016 (CA 2016) is the principal legislation setting out the laws relating to insolvency, rescue mechanisms and liquidation for corporations in Malaysia. Judicial management applications and liquidations are regulated by the Companies (Corporate Rescue Mechanism) Rules 2018 and the Companies (Winding-Up) Rules 1972.

Businesses carried out through a sole proprietorship or partnerships of individuals are regulated under the Registration of Businesses Act 1956 and the Partnership Act 1961. The Insolvency Act 1967 (IA 1967) contains provisions relating to the insolvency and bankruptcy of individuals. Section 18 of IA 1967 allows creditors to consider composition in satisfaction of the debts due to creditors by a bankrupt, or for a scheme of arrangement of the bankrupt's affairs. CA 2016 also provides for the winding-up of unregistered companies, including foreign companies and any partnership, association or company consisting of more than five members but not including companies incorporated under CA 2016 or under any corresponding previous written law.

The Limited Liability Partnerships Act 2012 (LLPA 2012) allows the formation of a limited liability partnership (LLP), which is a body corporate that has a separate legal personality from its partners. There is no corporate rescue mechanism available for an LLP; LLPA 2012 merely provides for winding-up and dissolution.

2.2 Types of Voluntary and Involuntary Restructurings, Reorganisations, Insolvencies and Receivership

Restructuring

CA 2016 provides for three types of corporate restructuring involving varying degrees of judicial supervision:

- scheme of arrangement (SA);
- judicial management (JM); and
- corporate voluntary arrangement (CVA).

JM and CVAs are not available to all companies.

The court cannot make a JM order in the following circumstances:

- if a company is a licensed institution or an operator of a designated payment system regulated by the laws enforced by BNM;

- if a company is subject to the Capital Market and Services Act 2007 (CMSA) – the High Court's recent decision on Scomi Group Bhd makes it clear that JM is not available to public companies listed on Bursa Malaysia;

- if a company is in liquidation; or

- if the court is satisfied under section 409 of CA 2016 that:

  a) a receiver or receiver and manager have been or will be appointed over the company; and

  b) the making of the order is opposed by a secured creditor.

A CVA is not available to the following:

- a public company;

- a company that is a licensed institution or an operator of a designated payment system regulated under laws enforced by BNM;

- a company that is subject to the CMSA; and

- a company that creates a charge over its property or any of its undertakings.

Liquidation

An insolvent company may be wound up voluntarily, which involves the company passing the requisite resolution for the company to be wound up. The liquidator is appointed based on nominations by creditors and members of the company

The High Court has the power to compulsorily wind up an insolvent company. Upon the presentation of a winding-up petition, the High Court has the discretion to order the company to be wound up and appoint a liquidator to carry out the liquidation.

Receivership

In Malaysia, receivership is usually brought about by appointment pursuant to private debentures given by the company as security. CA 2016 contains specific provisions regulating the powers of receivers and managers (R&M) and the interplay of the rights of receivers when a company goes into liquidation.

The court has power to appoint R&Ms under section 374 of CA 2016. Court-appointed receiverships are made when there is evidence of imminent danger of loss or dissipation of the company's assets (see *Dato' Sri Andrew Kam Tai Yeow v Tan Sri Dato' Kam Woon Wah & Ors* [2018] MLJU 1470).

2.3 Obligation to Commence Formal Insolvency Proceedings

There is no mandatory provision under which a company is obliged to commence formal insolvency proceedings. However, directors and officers of distressed companies are potentially liable for fraudulent trading and misfeasance proceedings, and potentially liable for damages and to make restitution under sections 540 and 541 of CA 2016. In relation to fraudulent trading, directors and officers could also be liable to imprisonment for a term not exceeding ten years, or to a fine not exceeding MYR1 million, or both.

2.4 Commencing Involuntary Proceedings

Scheme of Arrangement

A creditor can apply to the court to convene a meeting to consider a compromise or arrangement for the company, which can be for all creditors or for a class of creditors. A liquidator, judicial manager or member of a company can also apply.

Restructuring pursuant to an SA is a two-tier process.

- The applicant applies to the court for an order to convene a meeting to consider the proposed scheme.

- The proposed compromise or arrangement has to be agreed to by a majority of 75% of the total value of the creditors or class of creditors or members or class of members present and voting in the meeting. Only “persons who are able to prove in a winding-up” are entitled to vote at the meeting.

The court must approve the proposed compromise or arrangement on such alternations or conditions as it thinks fit.

Judicial Management

A creditor can apply for JM.

A court can make a JM order and appoint a judicial manager if:

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

- it considers that the making of the JM order is likely to achieve one of the following purposes:

  a) the survival of the company as a going concern;

  b) the approval of an SA between the company and any such persons; or

c) a more advantageous realisation of the company's assets than would be achieved in a winding-up.

These items are known as the "Statutory Objectives" of JM.

The court also has the power to make a JM order and appoint a judicial manager if it considers doing so to be in the public interest.

Corporate Voluntary Arrangement

A creditor cannot apply for a CVA. The company, a judicial manager or a liquidator can apply. The applicant needs to submit the following in its application:

- a document setting out the proposed voluntary arrangement, which can be either a composition in satisfaction of the company's debts or a scheme of arrangement of the company's affairs;
- a statement of the company's affairs, which must contain, among others, information, the particulars of the company's creditors, debts and other liabilities, and assets;
- a statement that the company is eligible for a moratorium;
- a statement from the nominee that he or she has given their consent to act; and
- a statement disclosing the full particulars of previous proposed CVAs or an application for a moratorium and the results of the application.

2.5 Requirement for Insolvency

Insolvency is a requirement for a JM application. A court needs to be satisfied that the company is or will be unable to pay its debts. The phrase "inability to pay debts" is found in section 466 of CA 2016, which states that a company shall, among others, be deemed to be unable to pay its debts if:

- the company is indebted to a sum exceeding the amount prescribed by the Minister charged with responsibility for finance (which is currently set at MYR50,000), and a creditor has served a notice of demand requiring the company to pay the sum, but the company has neglected to pay the sum or to secure or compound for it to the satisfaction of the creditor for 21 days after the service of the demand; or
- it is proved to the satisfaction of the court that the company is unable to pay its debts, taking into account the contingent and prospective liabilities of the company.

Insolvency is not a requirement for applications for a CVA or SA.

2.6 Specific Statutory Restructuring and Insolvency Regimes

The following specific legislation confers powers on regulators to intervene in regulated institutions.

The Financial Services Act 2013 (FSA) and the Islamic Financial Services Act 2013 (IFSA) regulate persons licensed to carry out:

- banking business;
- insurance business;
- investment banking business;
- Islamic banking business;
- takaful business;
- international Islamic banking business; or
- international takaful business.

BNM has power under the FSA and IFSA to:

- assume control and appoint R&Ms to manage the businesses, affairs and properties of the licensed institution;
- order the compulsory transfer of the businesses, affairs and properties of the licensed institution; and
- wind up the licensed institution based on CA 2016, whereby the assets of the institution will be made available to meet liabilities based on provisions under the FSA.

The CMSA regulates activities, markets and intermediaries in the capital markets (ie, the securities and derivatives markets). When there is contravention of requirements under the CMSA, SC and Bursa Malaysia have powers to:

- appoint R&Ms;
- order vesting securities; and
- petition to wind up based on CA 2016.

As noted earlier, JM and CVAs are not available to companies that are subject to the CMSA, such as financial and insurance institutions.

LH AG ADVOCATES AND SOLICITORS

3 Out-of-Court Restructurings and Consensual Workouts

3.1 Consensual and Other Out-of-Court Workouts and Restructurings

Consensual workouts and restructurings are not uncommon.

In fact, the Malaysian government has encouraged businesses to enter into workouts with their financial institutions. In July 2021, the government reintroduced a loan moratorium under the "Pakej Perlindungan Rakyat dan Pemulihan Ekonomi" (PEMULIH). Eligible borrowers do not need to make any repayment for six months, and no late payment charges or penalties will be imposed.

There is no specific legislation regulating consensual workouts in Malaysia. A freely negotiated debt restructuring agreement, supported by valuable consideration, is enforceable and binding on parties, but restructuring agreements that contravene the law will be void and unenforceable – for example, an agreement entered into by an insolvent company to prefer a certain creditor would be void under section 528 of CA 2016.

3.2 Consensual Restructuring and Workout Processes

Consensual Workouts

Consensual corporate workouts are ordinarily initiated by the company with the assistance of a restructuring adviser or an insolvency practitioner. A debt restructuring proposal is formulated and negotiated with the company's creditors. Financiers would ordinarily expect a candid disclosure of the company's financial position, justification for the restructuring and often reduced debt obligations and timelines for repayment, as well as the source and means of repayment. In some instances, financiers have insisted on the appointment of an independent financial adviser at the debtor's expense to advise on the viability on the debt restructuring proposal.

Corporate Debt Restructuring Committee (CDRC)

BNM set up CDRC in 1998 as a pre-emptive measure by the Malaysian government to provide a platform for corporate borrowers and their creditors to work out feasible debt resolutions without having to resort to legal proceedings. A public listed company that has an aggregate indebtedness of MYR10 million and involves at least two financial institutions may apply to CDRC to mediate debt restructuring arrangements involving financial institutions.

Under the CDRC Code of Conduct (CDRC Code), after the debtor applies for a workout, CDRC will conduct a preliminary viability assessment, and within one month from the date of the application will notify the debtor and participating institutions of whether it will accept the application. Participating institutions are obliged to

observe a standstill upon receiving notice that CDRC has accepted the debtor's application.

Small Debt Resolution Scheme (SDRS)

BNM separately established SDRS to provide similar assistance to SMEs to restructure their financial commitments with financial institutions. This scheme is managed by Agensi Kaunseling dan Pengurusan Kredit (AKPK, or the Credit Counselling and Debt Management Agency), and commenced on 1 September 2020. A company must be Malaysian-owned (at least 51%) to be eligible for SDRS. The company must also qualify as a SME – ie, it has no more than 200 full-time employees, or its annual sales turnover is not more than MYR50 million.

3.3 New Money

New money is typically injected by white knights and shareholders. It is uncommon for them to be given super-priority liens or rights due to the pre-existing security rights accorded to financiers. Some financing and loan agreements may even contain debt subordination provisions to ensure the financier's debts enjoy priority.

3.4 Duties on Creditors

A debenture holder, being also a creditor, is entitled to bring an action for oppression or unfair prejudice under section 346 of CA 2016. This applies in cases where there is fraud on the minority, or where some commercial unfairness is being perpetrated by the majority shareholders or debenture holders on the minority shareholders or debenture holders.

Section 346 is not available to a sole debenture holder (see *The Bank of Nova Scotia Bhd & Anor v Lion Dri Sdn Bhd & Ors* [2020] MLJU 1987); it is only applicable where a minority within a class has been oppressed by the majority of that class or where the powers of the directors are being exercised in a manner that is oppressive to the minority of said class.

3.5 Out-of-Court Financial Restructuring or Workout

Unless it has been specifically provided for or agreed upon by creditors, it is not possible to cram down an out-of-court workout on dissenting minority creditors.

4 Secured Creditor Rights, Remedies and Priorities

4.1 Liens/Security

Immovable Assets

Rights over immovable properties are commonly taken as securities for financing. Financiers will usually take a statutory charge where the issued documents of title are available. This confers a right on the financier to take possession and/or sell the charged property. A less common form of security over land is the

lien holder caveat. Both forms of security need to be registered under the National Land Code (NLC).

Where the issued document of title is not available, the financier will usually take an absolute assignment over the rights of the immovable property. Assignment over sale proceeds is another common form of security. A valid absolute assignment needs to be created in accordance with section 11 of the Civil Law Act 1956.

Movable Assets

Debentures conferring fixed and floating charges over assets of the company, including shares, stocks, intellectual property, and accounts are a common form of security. Default allows the debenture holder to appoint receivers or R&Ms over the company. CA 2016 introduced various provisions concerning R&Ms appointed to companies, including a specific provision on powers of receivers or R&Ms in liquidation.

Other common securities created over movable properties include:

- absolute assignment over contract proceeds;
- pledge and memorandum of charge over bank fixed deposits;
- memorandum of charge over shares in companies; and
- charges over aircraft and vessels.

4.2 Rights and Remedies

Depending on the nature of the insolvency proceedings brought, a creditor's right to enforce its security can be affected.

Corporate Voluntary Arrangement

The company is protected by an automatic moratorium after an application for a CVA is filed in court. The automatic moratorium remains in force for 28 days, unless it is extended with the consent of creditors.

Among other things, the moratorium prevents any appointment of a judicial manager from being made and any other proceedings and any execution or other legal process from being commenced or continued against the company or its property (except with leave of the court).

Judicial Management

A company is protected by an automatic moratorium during the interim period from the filing of an application for a JM order until

the application is dismissed. However, this moratorium has relatively limited effect, as follows:

- no resolution shall be passed or order made for winding-up of the company;
- no steps to enforce security over the company's property; and
- it prevents the commencement or continuation of legal processes against the company or its property (except with consent of the judicial manager or with leave of the court and subject to any term the court may impose).

A wider moratorium takes effect when a JM order is made, and has the following additional effects:

- no receiver or R&M shall be appointed; and
- no steps shall be taken to transfer any share of the company or to alter the status of any member of the company (except with leave of the court and subject to any term the court may impose).

In fact, upon making of a JM order, any receiver and R&M shall vacate office; and any application for the winding up of the company shall be dismissed.

A moratorium may be extended beyond the initial 28 days at a meeting of the company and a meeting of creditors summoned under section 399 of CA 2016. The moratorium may be extended to a period of not more than 60 days, subject to:

- consent by the nominee and members of the company; and
- consent of at least 75% in value of creditors.

Scheme of Arrangement

There is no automatic moratorium when an application for an SA is made. A restraining order can, however, be sought under section 368(1) of CA 2016 for the company to formulate and finalise a scheme.

4.3 Special Procedural Protections and Rights

The rights of secured creditors are protected in respect of a CVA and JM.

Under section 400(4) of CA 2016, a proposed CVA that affects the right of a secured creditor to enforce its security shall not be approved at the meeting of the company or its creditors, unless the secured creditor consents to the proposal.

Under section 409 of CA 2016, a court will not make a JM order in the following circumstances:

- if a receiver or R&M has been or will be appointed over the company; and
- if the making of the order is opposed by any secured creditor.

5 Unsecured Creditor Rights, Remedies and Priorities

5.1 Differing Rights and Priorities

Generally, secured creditors enjoy priority over unsecured creditors.

For an SA, secured creditors are invariably classed separately from unsecured creditors. In a CVA, it is statutorily prohibited to convene a meeting to approve a proposal that affects the rights of a secured creditor to enforce his security, unless the secured creditor concurs.

A court shall dismiss an application for a JM order if a secured creditor objects to it. Furthermore, a judicial manager can dispose of assets that are subject to a floating charge but the security holder continues to have the same priority. However, a judicial manager cannot dispose of assets that are subject to a security other than a floating charge, which requires leave of the court. Even when leave is granted, it is a requirement that the order stipulates that the net proceeds of the disposal shall be applied towards discharging the sums secured by the security.

When an insolvent company is wound up, section 527 of CA 2016 recognises a preferred class of unsecured debts. The unsecured debts adopt the following order of priority:

- the costs and expenses from the winding-up, the remuneration of the liquidator and the costs of auditing the liquidator's accounts;
- wages and salaries;
- worker's compensation;
- remuneration payable for vacation leave;
- contributions to employees; and
- federal taxes.

5.2 Unsecured Trade Creditors

Unsecured trade creditors are generally kept whole during a restructuring, although there is no strict requirement to do so. For

instance, in relation to a scheme of arrangement, it is possible to propose a scheme for a specific class of creditors only.

5.3 Rights and Remedies for Unsecured Creditors

Voting in Favour

The support of unsecured creditors forming a majority of creditors in a financially distressed company is crucial.

In relation to CVAs, a proposed voluntary arrangement must be approved by 75% of the total value of creditors present and voting at the meeting called to consider the proposal.

For JM, the proposal must be approved by 75% of the total value of creditors whose claims have been accepted by the judicial manager, present and voting at the meeting. This is the same in respect of any revisions to the proposal.

There is no difference for a SA. Section 366(3) requires the proposed compromise or arrangement to be agreed to by a majority of 75% of the total value of creditors present and voting at the meeting.

Separately, there is no automatic moratorium when a distressed company applies for an SA. The support of creditors forms a crucial part of the court's consideration in deciding whether a restraining order should be allowed under section 368(2) of CA 2016.

Judicial Intervention

In relation to a CVA, unsecured creditors dissatisfied by any act, omission or decision of the supervisor carrying out the voluntary arrangement may also appeal to the court for recourse. Among other actions, the court may confirm, reverse or modify any act or decision of the supervisor on appeal.

Creditors in a JM may establish a Committee of Creditors that calls upon the judicial manager to furnish information concerning the functions carried out by the judicial manager. A creditor is entitled to apply to the court for relief if the company's affairs, business and property are being or have been managed by the judicial manager. Among other actions, the court may regulate the future management of the company's affairs, business and property by the judicial manager, require the judicial manager to refrain from doing the act complained of, summon a meeting of creditors, and discharge the JM order and make such consequential provision as it deems fit.

In an SA, an approved scheme or compromise must be sanctioned by the court. At that stage, unsecured creditors can oppose the compromise or arrangement approved.

5.4 Pre-judgment Attachments

Pre-judgment attachments in the form of interlocutory injunctions are available in Malaysia. The courts have power to order Mareva or asset freezing injunctions pending disposal of an action. In cases where there is proof of the dissipation of assets, the courts may also appoint a receiver.

5.5 Priority Claims in Restructuring and Insolvency Proceedings

There is no priority of claims in restructuring and insolvency proceedings.

6 Statutory Restructuring, Rehabilitation and Reorganisation Proceedings

6.1 Statutory Process for a Financial Restructuring/ Reorganisation

Corporate Voluntary Arrangement

An application is made to the High Court by filing the following, among other documents:

- the proposed voluntary arrangement, which can be either a composition in satisfaction of the company's debts or a scheme of arrangement of the company's affairs;
- a statement of the company's affairs, which must contain, among other information, the particulars of the company's creditors, debts and other liabilities, and assets;
- a statement that the company is eligible for a moratorium;
- a statement from the nominee that he has given his consent to act; and
- a statement disclosing the full particulars of previous proposed CVAs or an application for a moratorium and the results of the application.

The nominee will summon a meeting of the company and creditors to decide whether to approve the proposed voluntary arrangement. The nominee must report the result of each meeting to the court and give notice of the results of the meetings to the Registrar and such other persons or bodies approved by the court.

The proposed CVA must be approved by a simple majority of the shareholders of the company and a majority of 75% in value of creditors present and voting at the meeting either in person or by proxy. Once the proposal has been approved, it will be binding on all creditors, including those who have voted against the proposal.

After the voluntary arrangement is approved, a supervisor will be appointed to supervise its implementation. The supervisor can be either the nominee or another insolvency practitioner.

Judicial Management

Upon an application made in court, the judge may make a JM order and appoint a judicial manager if:

- the court is satisfied that the company is or will be unable to pay its debts; and
- the court considers the making of the JM order likely to achieve one of the following purposes:

  a) the survival of the company as a going concern;

  b) the approval of an SA between the company and any such persons; or

  c) a more advantageous realisation of the company's assets than would be achieved in a winding-up.

These items are known as the "Statutory Objectives" of a JM.

The judicial manager is obliged to send a statement of his/her proposal for achieving one or more of the Statutory Objectives to the Registrar of Companies and all creditors of the company, and must present the same before a meeting of creditors within 60 days of the date of the JM order or such longer period as the court may allow.

The proposal must be approved by 75% of the total value of creditors, whose claims have been accepted by the judicial manager, present and voting at the meeting. Once the proposal is approved, it becomes binding on all creditors. If creditors do not approve the proposal at the meeting, the court may discharge the JM order after receiving the judicial manager's report, or may make any consequential provision to the JM order that it deems fit, adjourn the hearing on conditions, or make an interim order.

Scheme of Arrangement

An order needs to be obtained from the court to summon a meeting of creditors and members to consider a proposed compromise or arrangement. The court has the power to order an approved liquidator to assess the viability of the proposed compromise or arrangement and to issue an order to restrain proceedings against the company pending finalisation of the proposed compromise or arrangement.

The proposed compromise or arrangement has to be agreed to by a majority of 75% of the total value of the creditors or class of

creditors. The approved compromise or arrangement must then be approved by the court.

6.2 Position of the Company

The directors of companies under a CVA and SA remain in control of the management of said companies. That is not the case for JM: all powers and duties imposed on directors shall be exercised by the judicial manager so long as the JM order is in force. The judicial manager is responsible for the management of the affairs, business and property of the company.

Companies under a CVA and JM enjoy a moratorium upon filing the application with the court. However, the moratorium is for a limited period and can only be extended upon certain conditions being met. For an SA, the applicants need to apply for a restraining order from the court.

Companies can continue to operate. A judicial manager can borrow money and grant security. However, no steps can be taken to impose security over the property of a company under a CVA during the moratorium except with leave of the court.

6.3 Roles of Creditors

Scheme of Arrangement

Creditors are put into separate classes in respect of compromises and arrangements in a proposed SA. There is no such requirement for JM and CVAs.

Where there are different classes of creditors in a proposed compromise or arrangement, a class must be confined to those creditors whose rights are not so dissimilar as to make it impossible for them to consult together with a view to their common interest to avoid the unnecessary proliferation of classes. The recent decision in *AirAsia X Bhd v BOC Aviation Ltd & Ors* [2021] 10 MLJ 942 makes it clear that the selection of creditors in each class needs to be determined at the convening stage.

Creditors will receive an explanatory statement setting out the details of the proposed compromise or arrangement. The court may appoint an approved liquidator to assess the viability of the proposed SA and prepare a report, which will be presented at the meeting of creditors.

In considering whether to approve a compromise or arrangement, the court will examine whether a class of creditors was fairly represented by those who attended the meeting and whether the statutory majority were acting in a bona fide manner and not coercing the minority in order to promote interests that were adverse to those of the class who they purport to represent.

LH AG ADVOCATES AND SOLICITORS

Judicial Management

A judicial manager is obliged to send a statement of his/her proposal to all creditors, and to present the same before a meeting of creditors within 60 days of the date of the JM order or such longer period as the court may allow. Notice of the proposal must be published in a widely circulated newspaper in Malaysia under the national language and the English language.

Corporate Voluntary Arrangement

The terms of the proposed voluntary arrangement are part of the document filed by the company when it applies for a CVA. The same proposal will be tabled at the meeting of creditors.

6.4 Claims of Dissenting Creditors

There is no cram-down or cram-up procedure.

6.5 Trading of Claims Against a Company

A creditor may sell a debt owed by the company by way of an assignment. The trading of claims against a company may not be enforceable due to strict common law rules on champerty.

6.6 Use of a Restructuring Procedure to Reorganise a Corporate Group

The reorganisation of a corporate group can be achieved through an SA under section 370 of CA 2016. The following needs to be proved to the court:

- that the compromise or arrangement has been proposed for the purposes of, or in connection with, a scheme for the reconstruction of any company or the amalgamation of two or more companies; and

- that under the scheme the whole or any part of the undertaking or property of any company concerned is to be transferred to another company.

The court's approval will be required. When approving the compromise or arrangement, the court will make provision for the following:

- the transfer of the whole or any part of the undertaking, property or liabilities of the transferor company to the transferee company;

- the allotting or appropriation by the transferee company of any shares, debentures, policies or similar interests;

- the continuation by or against the transferee company of any legal proceedings pending by or against the transferor company;

- the dissolution without winding-up of the transferor company;

- provisions for any dissent; and

- such incidental, consequential and supplemental matters as are necessary to secure that the reconstruction or amalgamation shall be fully and effectively carried out.

6.7 Restrictions on a Company's Use of Its Assets

When a company is under JM, the judicial manager can dispose of its properties by public auction or private contract. However, as mentioned in **5.1 Differing Rights and Priorities**, the judicial manager's right to do so is subject to any existing security interest. The judicial manager may also borrow money and grant security over the property of the company.

A company protected by a restraining order obtained pursuant to an SA application cannot dispose of any of its property without leave of the court, other than in the ordinary course of business. Such disposals are void.

There is no such restriction for CVAs.

6.8 Asset Disposition and Related Procedures

In an SA and CVA, the sale of assets or businesses will be executed by the directors of the company. For a company under JM, the judicial manager will effectuate the sale.

6.9 Secured Creditor Liens and Security Arrangements

The rights of secured creditors can be released, provided the secured debt is fully repaid or the secured creditor allows a redemption of the security based on a negotiated redemption sum. However, in the case of JM, the judicial manager can dispose of the secured assets subject to the limitations mentioned in **5.1 Differing Rights and Priorities**.

6.10 Priority New Money

There is no procedure that enables new money to be secured against assets that are subject to a pre-existing security without the consent of the secured creditors.

6.11 Determining the Value of Claims and Creditors

A proof of debt is conducted for an SA and JM to determine the claims and debts of the creditors.

6.12 Restructuring or Reorganisation Agreement

For an SA, the court's approval of the proposed compromise or arrangement is necessary for it to be binding on all creditors. A court is likely to give its approval if:

- the requirements under section 366 of CA 2016, such as the required creditor majority, have been complied with;

- a class (of creditors/members) was fairly represented by those who attended the meeting, and the statutory majority were acting in a bona fide manner and not coercing the minority in order to promote interests that were adverse to those of the class who they purport to represent; and

- the arrangement is such that an intelligent and honest person acting in respect of his/her own interests would approve it.

In certain instances, the judicial manager in a judicial management has power to disclaim the personal liability of contracts entered by the company and adopted by him or her. In cases where the liquidator proposes a compromise or arrangement under a CVA and SA, the liquidator has the power to disclaim an onerous contract.

6.13 Non-debtor Parties

The judicial manager has power to make any arrangement or compromise to release non-debtor parties from liabilities. However, if the release unfairly prejudices the interests of the company's creditors, a creditor or member may apply to the court to restrain the judicial manager, among other actions.

If the liquidator had proposed a compromise or arrangement for a CVA or SA, the liquidator has the power to enter into such compromises with the approval of the committee of inspection or the court.

6.14 Rights of Set-Off

Under sections 430(2) and 526 of CA 2016, a court can order that the provision on mutual set-off applies to the JM. Again, in cases where the liquidator proposes a compromise or arrangement under a CVA or SA, the liquidator can exercise the mutual set-off against creditors.

6.15 Failure to Observe the Terms of Agreements

The judicial manager has a duty to manage the affairs, business and property of the company based on the proposal. Where there is non-observance, the manager could propose revisions and seek approval from creditors. If an approved arrangement cannot be achieved, the judicial manager is obliged to apply for the JM order to be discharged.

In a CVA, the approved arrangement comes to an end under section 402 of CA 2016 if the voluntary arrangement is not fully implemented. If he so wishes, a supervisor can apply to the court for directions when there is non-observance, and is also entitled to apply for the company to be wound up or for a JM order to be made.

For an SA, the approved scheme will usually provide for the termination of the scheme and its effect on the creditors.

6.16 Existing Equity Owners

Equity owners have no right to receive or retain any ownership or other property on account of their ownership interests. This is also unlikely in cases involving the restructuring of an insolvent company.

7 Statutory Insolvency and Liquidation Proceedings

7.1 Types of Voluntary/Involuntary Proceedings

As mentioned earlier, a company can be voluntarily or compulsorily wound up.

A company may be wound up voluntarily when it so resolves by special resolution. The directors are required to make a declaration with a statement of affairs that the directors have made an inquiry into the affairs of the company, and at a meeting of directors have formed the opinion that the company is unable to pay its debts in full within a period not exceeding 12 months from the commencement of the winding-up.

The company and the creditors will nominate a person to be the liquidator, in separate meetings. If the creditors and company nominate different persons, the person nominated by the creditors shall be the liquidator.

A creditor is entitled to petition the High Court to compulsorily wind-up a company that is unable to pay its debts. A company is presumed to be unable to pay its debts when it fails to satisfy a statutory demand issued under section 466(1) of CA 2016 after 21 days.

Creditors and contributories of the company are entitled to appear in court to oppose or support the winding-up petition. The petitioning creditor is entitled to propose an insolvency practitioner to be appointed a liquidator. The Official Receiver otherwise becomes the liquidator of the company.

No action or proceeding can proceed or be commenced against a company after the commencement of a winding-up. Leave of the court is required for such actions or proceedings to continue. In relation to a compulsory winding-up, a company can apply for any pending action to be stayed after the presentation of a winding-up petition.

The liquidator takes over the affairs of the company when it is wound up. The directors of the company in liquidation do not have the power to act on behalf of the company, except as consented to or sanctioned by the liquidator.

A liquidator has power to disclaim the property of a company consisting of estates in land burdened with onerous covenants, shares in corporations, unprofitable contracts or unsaleable property. An application to the court for leave to do so is required.

There is a statutory right to mutual credit and set-off, provided such right existed before the commencement of the winding-up. An account needs to be taken before a set-off.

Every creditor is obliged to prove his debt. A secured creditor is entitled to value his security and claim in a winding-up as an unsecured creditor for the balance. Except for preferential unsecured creditors, all debts rank pari passu and shall be paid in full, unless the property of the company is insufficient to meet the debts, in which case the payment is reduced, and the rate of reduction shall be in equal proportion.

7.2 Distressed Disposals

The liquidator negotiates, executes and authorises the sale of assets. However, as noted earlier, in the administration of the assets and distribution among creditors, the liquidator shall have regard to the wishes of creditors, contributories or the committee of inspection. The liquidator passes good title to a purchaser in such a sale.

The liquidator has wide powers to "sell the immovable property and movable property and things in action of the company by public auction, public tender or private contract with power to transfer the whole thereof to any person or company or to sell the same in parcels." While there is no restriction regarding to whom the liquidator can sell the asset, the liquidator is not unrestricted.

The power is subject to the control of the court: see *North Plaza Sdn Bhd v Equiticorp Holdings Ltd and other appeals* [2013] 3 MLJ 617. As mentioned earlier, the liquidator shall have regard to the wishes of creditors, contributories or the committee of inspection.

7.3 Organisation of Creditors or Committees

If requested by creditors, the liquidator may summon separate meetings of creditors and contributories to determine whether to appoint a committee of inspection. The committee of inspection plays a crucial role in the liquidation. For instance, in the administration of the assets and distribution among creditors, the liquidator shall have regard to any directions given by creditors, contributories or the committee of inspection.

The committee of inspection can authorise the liquidator to exercise selected powers under the 12th Schedule, Part II of CA 2016, which includes carrying on business and making compromises or arrangements with creditors.

8 International/Cross-Border Issues and Processes

8.1 Recognition or Relief in Connection with Overseas Proceedings

The existing insolvency laws in Malaysia do not have extra-territorial effect.

Malaysia is not a party to any international treaty on cross-border insolvency and has not adopted as part of its law the UNCITRAL Model Law on Cross-Border Insolvency (1997) or the UNICTRAL Model Law on Recognition and Enforcement of Insolvency-Related Judgments 2018.

Although an insolvency practitioner who is appointed as judicial manager or liquidator takes custody or control of all property to which the company is entitled, including property outside Malaysia, it is a matter for the court of the relevant foreign jurisdiction to recognise the rights of the judicial manager or liquidator.

8.2 Co-ordination in Cross-Border Cases

The courts do not have protocols or arrangements with foreign courts to co-ordinate proceedings.

8.3 Rules, Standards and Guidelines

There is no applicable rule to determine which jurisdiction's decisions, rulings or law govern or are paramount.

8.4 Foreign Creditors

Foreign creditors are not dealt with differently in proceedings.

8.5 Recognition and Enforcement of Foreign Judgments

A final judgment issued by a superior court from a foreign country can be recognised and registered as a Malaysian judgment under the Reciprocal Enforcement of Judgments Act 1958 (REJA). The reciprocating countries under REJA are:

- the United Kingdom;
- Hong Kong;
- Singapore;
- New Zealand;
- Sri Lanka;
- India (excluding the State of Jammu and Kashmir, the State of Manipur, Tribal areas of the State of Assam and Scheduled areas of the States of Madras and Andhra); and
- Brunei.

Foreign judgments from non-reciprocating countries can be recognised by way of common law action upon judgment.

The court will not enforce a foreign judgment if:

- the foreign court had no jurisdiction;

- the judgment was obtained by fraud;
- the judgment would be contrary to public policy; or
- the proceedings in which the judgment was obtained were opposed to natural justice.

9 Trustees/Receivers/Statutory Officers

9.1 Types of Statutory Officers

The statutory officers appointed by the court are as follows:

- the judicial manager for JM;
- the nominee for a CVA; and
- the liquidator for a winding-up. The Official Receiver will be the liquidator if an insolvency practitioner is not appointed.

9.2 Statutory Roles, Rights and Responsibilities of Officers

Judicial Manager

The judicial manager is deemed to be the agent of the company. His or her principal duties include:

- taking custody or control of the company's assets;
- managing the affairs, business and property of the company;
- preparing a statement of proposal to achieve one of the Statutory Objectives and laying the same before a meeting of creditors for their approval;
- managing the affairs, business and property of the company in accordance with the proposal; and
- applying for the JM order to be discharged if it appears that the purpose specified in the order either has been achieved or is incapable of being achieved.

The judicial manager has extensive powers under the 9th Schedule to CA 2016 to discharge his or her duties, which include:

- taking possession of the company's property;
- taking proceedings on behalf of the company;
- borrowing money and granting security;

- making arrangements or compromises on behalf of the company; and

- dealing with the company's property with leave of the court, except for property that is subject to a floating charge.

In discharging his/her duties, the judicial manager is accountable to the creditors and members of the company, in view of the statutory protection accorded to creditors and members under section 425 of CA 2016.

Nominee

The nominee under a CVA is responsible for:

- summoning the meeting of creditors to consider the proposed voluntary arrangement; and

- monitoring the company's affairs for the purpose of forming an opinion as to whether the proposed voluntary arrangement has a reasonable prospect of being approved and implemented, and whether the company is likely to have sufficient funds available during the proposed moratorium to enable it to carry on business. The nominee is entitled to withdraw his or her consent to act if he or she forms an opinion in the negative.

If the proposed voluntary arrangement is approved by creditors, the nominee becomes the supervisor that oversees the implementation thereof.

If a creditor or any other person is dissatisfied by any act, omission or decision of the supervisor, the company's creditor may appeal against the same to the court.

Liquidator

The liquidator's duties include:

- taking control of and liquidating the assets of the company;

- determining the creditors and contributories of the company;

- paying creditors from the liquidation proceeds; and

- investigating the affairs of the company, particularly for misfeasance.

A liquidator has extensive powers under the 12th Schedule to CA 2016, including making any compromise or arrangement with the company's creditors through a CVA or SA. Any creditor

dissatisfied with any decision of a liquidator can appeal against the decision.

9.3 Selection of Officers

Insolvency Practitioners

Statutory officers must be insolvency practitioners, who are approved liquidators other than the Official Receiver. Section 433(3) of CA 2016 states that a member of a recognised professional body may apply to the Minister of Finance to be an approved liquidator. The Malaysian Institute of Accountants (MIA) and Malaysian Institute of Certified Public Accountants (MICPA) are recognised professional bodies under the Guidelines for Qualification as Liquidator under the Companies Act 2016 issued by the Accountant General of Malaysia.

Judicial Manager

In the application for a JM order, the applicant will nominate a person to act as a judicial manager, who must be an independent insolvency practitioner and is not the auditor of the company. The court may refuse the applicant's nomination and appoint another insolvency practitioner as the judicial manager.

Where a nomination is made by the company, a majority in value of creditors (including contingent and prospective creditors) may be heard in opposition to the nomination and the court may, if satisfied as to the value of the creditors' claims and the grounds of the opposition, invite the creditors to nominate a person who is an insolvency practitioner to act as the judicial manager and adopt the nomination if it deems fit.

A judicial manager can be removed.

Nominee/Supervisor

The nominee is proposed by the directors of the company, who will also nominate the nominee as the supervisor or trustee to supervise the implementation of the CVA. However, if a judicial manager proposes a CVA, he or she may also be the nominee.

The court has powers to replace a nominee. Replacement of nominees can be made by the directors or the Official Receiver where the nominee fails to comply with his or her duties, or where it is inappropriate for the nominee to continue to act.

The court can also replace a supervisor if it is expedient to appoint a person to carry out the function, and if it is inexpedient, difficult or impracticable for an appointment to be made without the court's assistance.

LH AG ADVOCATES AND SOLICITORS

Liquidator

A creditor may propose his choice of an approved liquidator to be appointed in the winding-up petition.

If an approved liquidator is not appointed at the hearing of the petition, the Official Receiver becomes the interim liquidator until he/she or another person becomes liquidator. In such cases, the Official Receiver will summon separate meetings of creditors and contributories to determine whether an application should be made to the court to appoint a liquidator to replace him/her.

Upon cause being shown, a liquidator can be removed by the court.

10 Duties and Personal Liability of Directors and Officers of Financially Troubled Companies

10.1 Duties of Directors

Under CA 2016, an “officer” of a company includes any director, secretary or employee of the company. The word "director" for certain sections of CA 2016 includes the chief executive officer, chief financial officer, chief operating officer or any other person primarily responsible for the management of the company.

Directors and officers are bound by their common law duty of fidelity and fiduciary duties to, among others, act in the best interests of the company, and to exercise reasonable care, skill and diligence in performing their duties. They are also statutorily bound by similar duties imposed under sections 213 to 229 of CA 2016. For instance, directors shall exercise their powers for proper purposes and in good faith in the best interests of the company and shall exercise reasonable care, skill and diligence, and there are prohibitions against improper use of property, position, etc.

Directors and officers of distressed companies can be potentially liable for fraudulent trading and misfeasance proceedings and be ordered to pay damages and make restitution under sections 540 and 541 of CA 2016.

Breaches of directors’ statutory duties attract penal consequences. An officer of a company that is being wound up may also be penalised for actions intended to frustrate the winding-up of the company, such as falsifying documents, failing to keep proper accounts of the company, etc. See sections 536, 538 and 539 of CA 2016.

10.2 Direct Fiduciary Breach Claims

A creditor can bring fraudulent trading and misfeasance claims against a director under sections 540 and 541 of CA 2016.

11 Transfers/Transactions that May Be Set Aside

LH AG ADVOCATES AND SOLICITORS

11.1 Historical Transactions

In JM, any transaction (including the making of any payment or the transfer, mortgage or delivery of goods) by the company with the intention of clearing the debts owed to a specific creditor in preference over another creditor shall be void when the application for a JM order is submitted within six months of the date of that transaction. However, such a transaction will not be void for undue preference if it is carried out in good faith and for valuable consideration.

Likewise, the disposal of the assets of a wound-up company that is unable to pay its debts from its own money within six months is deemed fraudulent and void. The disposal will not be void if it is in favour of any person dealing with the company for valuable consideration and without any actual notice of the contravention.

There is no law on transactions of undue preference entered into before the commencement of an application for an SA and a CVA.

11.2 Look-Back Period

The look-back period is six months from the transaction.

11.3 Claims to Set Aside or Annul Transactions

Proceedings to set aside transactions are brought by the judicial manager and the liquidator.

Authors

Lee Hishammuddin Allen & Gledhill (Kuala Lumpur − HQ) has a team of dedicated insolvency and restructuring lawyers with a wide range of experience in voluntary and contentious restructuring, including administration workouts dating back to 1997/98, during the Asian financial crisis. The team's experience covers workouts in various industries and sectors, including aviation, construction, engineering, hospitality, steel, rail and securities. Over the years, the firm has also acted for various financial institutions, as well as insolvency practitioners, on a range of insolvency matters, including highly contentious insolvency disputes that are recognised as ground-breaking legal decisions. Recent notable highlights include the creditors' voluntary liquidation of one of the largest paper mills in the region and the former owner of the national carrier, the contested receivership of property investment companies owned by an international private equity fund, the contested judicial management of entities in the public infrastructure industry, the liquidation of a major steel manufacturer in Malaysia and a scheme of arrangement for an air transport company.

Kumar Kanagasingam heads the banking and insolvency practice group at Lee Hishammuddin Allen & Gledhill and has almost 40 years' experience, ranging from arbitration to general litigation, focusing on complex high-value recovery matters, corporate and commercial disputes. He has an active insolvency practice that includes the tracing and recovery of assets dissipated overseas, and he has experience in fraud, corporate governance, money laundering and regulatory compliance. Kumar also sits as a council member of the Insolvency Practitioners Association of Malaysia and is a committee member of the joint Insolvency Practice Committee of the Malaysian Institute of Accountants and Malaysian Institute of Certified Public Accountants.

Andrew Chiew Ean Vooi has notable experience in the areas of bankers' liability, civil fraud, corporate insolvency and restructuring, as well as anti-money laundering. He acts for various financial institutions on financing

obligations and security enforcement, involving conventional and Islamic financing, and asset recovery. Andrew's experience in corporate and commercial disputes covers various business sectors, including energy, hospitality, logistics and plantation. He also acts for corporations on matters concerning fraud and breaches of fiduciary and fidelity by senior management and directors.

Sean Yeow Huang-Meng has a diverse and active dispute resolution practice in general civil and commercial litigation, with particular emphasis on banking and financial services litigation and corporate insolvency. He focuses on banking and insolvency litigation, often acting for financial institutions and liquidators. He also acts extensively on civil and corporate matters, including contractual disputes. Sean has seen more than his fair share of heavily contentious matters litigated at all tiers of the Malaysian legal system.

Mong Chung Seng focuses on banking and insolvency, corporate and commercial dispute resolution. He regularly advises and represents insolvency practitioners and financial institutions on matters involving judicial management, liquidation, receivership, debt instruments, letters of credit and conventional and Islamic banking. He also acts for corporations in corporate and commercial disputes. Mong is a contributor to *Law and Practice of Corporate Insolvency in Malaysia*, published by Sweet & Maxwell.

Lee Hishammuddin Allen & Gledhill
Level 6, Menara 1 Dutamas
Solaris Dutamas
No. 1, Jalan Dutamas 1
50480 Kuala Lumpur
Malaysia

Tel: +603 6208 5888
Fax: +603 6201 0122
Email: enquiry@lh-ag.com
Web: www.lh-ag.com

Head Office
Level 6, Menara 1 Dutamas
Solaris Dutamas
No. 1, Jalan Dutamas 1
50480 Kuala Lumpur
Malaysia
Tel: +603 6208 5888
Fax: +603 6201 0122

Johor Office
Suite 21.01
21st Floor, Public Bank Tower
No.19, Jalan Wong Ah Fook
80000 Johor Bahru, Johor
Tel: +607 278 3833
Fax: +607 278 2833

Penang Office
18-33-A3 Gurney Tower
Persiaran Gurney
10250 Georgetown
Pulau Pinang
Tel: +604 299 9668
Fax: +604 299 9628

Email
enquiry@lh-ag.com

Website
www.lh-ag.com

Published by the Banking & Insolvency Practice