Dear IPAS Associate/Fellow,

We are glad to bring you the IPAS Update on the recent trends and developments in the insolvency profession.

Message from Chairman

Dear Associates/Fellows

This is a series of technical updates for associates and fellows as part of our initiatives on relevant Continuing Professional Education.

On behalf of the Board, we wish to thank Mr Lee Eng Beng, Chairman of the Technical Standards and Practices Committee, and Mr Andrew Chan, Director, IPAS, for their contributions. Members are encouraged to contribute articles of interest.

Yours sincerely,
DON M HO, FIPAS
Chairman

Join IPAS

Invitation to join the Insolvency Practitioners Association of Singapore Limited (IPAS)

Pursuant to the recommendations of the Company Legislation and Regulatory Framework Committee, the Insolvency Practitioners Association of Singapore Limited (IPAS) was incorporated on 12 April 2005 with the support of the Institute of Certified Public Accountants of Singapore

Technical Updates

Injunction Against Commencement Of Winding Up Proceedings

In the recent case of Metalform Asia Pte Ltd v Holland Leedon Pte Ltd [2007] SGCA 6, the Court of Appeal re-affirmed that a winding up application against a company should not be based on a bona fide disputed debt. The court will restrain a creditor from filing such an application and, if it has been filed, the court will stay or dismiss it. The Court of Appeal also held that the same approach will apply where a winding up application is based on an undisputed debt but the company has a cross-claim of substance which exceeds the undisputed debt. Further, where the company has a cross-claim of substance,m it is not necessary to show that the creditor's winding up application is "bound to fail" before an injunction will be granted. The "bound to fail" test only applies when a company is seeking to restrain a shareholder from filing a winding up application based on the "just and equitable" ground.

On the facts, the Court of Appeal found that the appellant company had a genuine cross-claim based on substantial grounds which may be in excess of the undisputed debt owed to the respondent creditor. There were no special circumstances militating against the grant of an injunction against the respondent creditor. In the circumstances, the Court allowed the company's appeal and granted an injunction.

Fraudulent Trading

In The Liquidator of Leong Seng Hin Piling Pte Ltd (In Compulsory Liquidation) v Chan Ah Lek and Others [2007] SGHC 9, the Singapore High Court reiterated that dishonesty is an essential ingredient to proving fraudulent trading under section 340(1) of the Companies Act. The burden of proof of such dishonesty is on the party alleging it, and the evidence required before a court will conclude dishonesty will usually be higher than that in ordinary civil cases. The court made clear that while the test for determining dishonesty was subjective, the objective standard of what an honest person would have done would be relevant in assessing whether or not the defendant had

(ICPAS), the Law Society of Singapore (Lawsoc) and the Official Receiver and Official Assignee. The members of IPAS are ICPAS and the Lawsoc.

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been dishonest.

Unfair Preferences

In Amrae Benchuan Trading Pte Ltd (in liquidation) v Tan Te Teck Gregory [2006] 4 SLR 969, the Singapore High Court helpfully distilled some of the principles applicable to determining whether transactions are unfair preferences. These are (as extracted from the judgment):

> *"A person is taken to intend the natural consequences of his action. As every payment or grant of security potentially has the effect of preferring the payee or the grantee in the event of the paying company's subsequent insolvency, something more has to be shown. Otherwise, the question of preference would be determined in every case simply by undertaking an objective inquiry into whether in effect there had been a preference.*
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> *The legislation in its previous form provided that what had to be shown was that the achievement of the preference was the predominant intention. That is no longer the case. What needs to be shown under the law as it now stands is that the payment was influenced by the desire to improve the creditor's position in the event of an insolvent liquidation.*
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> *The analysis is to be undertaken by reference to the time of the impugned transaction*
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> *Where the challenged transaction involves an associate (in principle, person connected in the company, as well), there is a rebuttable presumption that the company entered into that transaction under the influence of the relevant desire. In such a case, the court will examine all the facts, and determine whether on a balance of probabilities the presumption had been rebutted."*
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> [words in round brackets added.]

These principles were subsequently applied in The Liquidator of Leong Seng Hin Piling Pte Ltd (In Compulsory Liquidation) v Chan Ah Lek and Others [2007] SGHC 9.

In Leun Wah Electric Co (Pte) Ltd v Sigma Cable Co (Pte) Ltd [2006] SGHC 86, a company in liquidation sought to set aside an assignment of retention moneys in favour of a third party creditor on the grounds that it was an unfair preference and a transaction at an undervalue The Singapore High Court rejected the company's application.

The assignment was not a transaction at an undervalue as it had been executed for good consideration, namely, in lieu of direct cash payment to the creditor. Neither could the assignment be set aside as an unfair preference, as the company had not been influenced by a desire to confer the effect of an unfair preference on the creditor. The company had acted to protect its own commercial interests. The execution of the assignment allowed the company to retain the creditor as an important supplier and to continue with its projects and collect payment.

Transaction At An Undervalue

The English Court of Appeal in Hill v Spread Trustee Company Ltd [2006] EWHC Civ 542 decided that it may be possible in certain circumstances for a grant of security in respect of existing indebtedness to constitute a transaction at an undervalue. Previously the decision of Re MC Bacon [1990] BCLC 324 suggests that the provision of security could not amount to a transaction at an undervalue. It is interesting to note that a decade ago, Lee Eng Beng, FIPAS, had suggested in an article entitled The Avoidance Provisions Of The Bankruptcy Act 1995 And Their Application To Companies, Singapore Journal of Legal Studies [1995] 597 – 648, that the giving of security could in appropriate circumstances amount to a transaction at an undervalue.

See also the discussion above on Leun Wah Electric Co (Pte) Ltd v Sigma Cable Co (Pte) Ltd [2006] SGHC 86.

Priorities

The decision of the Australian High Court in Sons of Gwalia Ltd v Margaretic [2007] HCA 1 should be of interest insofar as it suggests that a claim for damages by a shareholder (who had purchased shares from the company) for misleading or deceptive conduct inducing the purchase of the shares would rank equally with the general body of unsecured creditors of the company in the company's insolvency. In reaching its decision, the court held that section 563(A) of the Australian Corporations Act 2001 did not apply to postpone the priority of the shareholder. Section 563(A) reads:

> *"Payment of a debt owed by a company to a person in the person's capacity as a member of the company, whether by way of dividends, profits or otherwise, is to be postponed until all debts owed to, or claims made by, persons otherwise than as members of the company have been satisfied."*

If this decision is applied in Singapore, it may elevate certain shareholder claims arising in relation to the purchase of a company's own shares to the same priority as that of general unsecured creditors of the company. It is not, however, entirely clear whether this decision will gain favour in Singapore. It is worth noting that section 250(1)(g) of the Singapore Companies Act is worded differently. Section 250(1)(g) reads:

> *"a sum due to any member in his character of a member by way of dividends, profits or otherwise shall not be a debt of the company payable to that member in a case of competition between himself and any other creditor not a member, but any such sum may be taken into account for the purpose of the final adjustment of the rights of the contributories among themselves."*

It is arguable that the term "character" mentioned in section 250(1)(g) of the Singapore Companies Act is broader than the term "capacity" in the Australian section 563(A), and if so, a narrower range of shareholder claims would stand in equal priority with that of the general body of unsecured creditors in Singapore as compared to Australia. Appropriate advice should in each case be obtained.

Liquidators

In Amrae Benchuan Trading Pte Ltd (in liquidation) v Tan Te Teck Gregory [2006] 4 SLR 969, the Singapore High Court opined that a liquidator has a special responsibility to retain a measure of detachment in the course of discharging his or her functions. This principle also applies when the costs of liquidation are financed by a single creditor. The Court further reiterated that liquidators should view matters through objective lenses.

The decision of Ee Kee Chai v Chew Joo Song John and Others [2006] SGHC 225, emphasises once again the importance of giving full material disclosure when making an ex parte application for the appointment of a provisional liquidator pending the determination of the winding up application. In the case, the Singapore High Court set aside the ex parte order appointing the provisional liquidators as there had been a failure to disclose material matters and the Court had been misled into making ex parte orders that it would not have otherwise have made.

The decision of the Singapore Court of Appeal in Ho Wing On Christopher and others v ECRC Land Pte Ltd (in liquidation) [2006] 4 SLR 817, contains useful principles

which liquidators should consider before commencing litigation on behalf of the insolvent company. The decision contains a lucid commentary of the principles relating to what liquidators should take into account given the limited resources available to the company and of the estate costs rule. Very briefly, the estate costs rule states that a successful litigant against a company in liquidation was entitled to be paid his costs in priority to the other general expenses of the liquidation, including the costs and remuneration of the liquidator. At paragraph [91] of the judgment (which is useful to reproduce in full), the Singapore Court of Appeal said:

> *"We expect that after our decision in this case, liquidators will be more mindful to protect themselves from potential liability for legal costs when discharging their duties for the benefit of creditors. Liquidators should at all times uphold the existing legal regime affecting corporate insolvency, which includes the estate costs rule. Future liquidators who wish to commence litigation on the company's behalf may want to consider the following points before deciding whether to proceed:*
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> *(a) As a matter of general principle, a liquidator who breaches the estate costs rule will be held personally liable for any shortfall in the company's assets which results from his breach. An order of personal liability will usually follow from such a breach regardless of whether it is the liquidator himself or a third party who receives the money in breach of the rule.*
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> *(b) In the absence of extenuating circumstances, the courts will hold a liquidator liable for breaching the estate costs rule even if the company's moneys were used to pay the company's own costs of sustaining the litigation. Where a liquidator has insufficient assets at his disposal to satisfy both the company's legal costs of maintaining the litigation as well as any potential costs order made against the company, a liquidator would be well-advised to obtain an indemnity from the creditors. If such an indemnity is not forthcoming, a liquidator should only proceed with the litigation if he is prepared to be held personally liable for a successful defendant's costs in the event that he is found in breach of the estate costs rule.*
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> *(c) By way of analogy with the principle in (b), if a company is completely insolvent and therefore has no prospects of satisfying any costs order*

made against it, it would be advisable for a liquidator to refrain from commencing proceedings unless he has managed to obtain a creditors' indemnity. Whilst the position on this issue is not entirely settled, a liquidator who omits to do so in a future case may well be held personally liable for the defendant's costs if the company's claim is unmeritorious.

(d) *In appropriate cases, the courts might exercise its power under s 283(3) of the CA to exempt a liquidator from personal liability for breaching the estate costs rule. In deciding whether to reverse the erstwhile rules of priority, the court will consider whether the liquidator in question is able to show the company's inability to satisfy the opposing litigant's costs did not result from his disregard of that other party's interests.*

Schemes of Arrangement

The English courts have clarified two practical issues in relation to schemes of arrangement. In *In re Cape plc* [2006] EWHC 1446, the English High Court held that a scheme of arrangement can provide for future amendment of the scheme itself or of its ancillary documents without the involvement of the Court. However, the Court felt that it would be exceptional that such a scheme will be sanctioned by the Court. The Court will have to be satisfied that it is fair and reasonable for there to be amendment provisions in the scheme, and that there are proper safeguards for the interests of the creditors or members who may be affected by amendments.

In practice, many schemes in Singapore do provide for amendment without the involvement of the Court. Often, the power of amendment may be exercised by a resolution of the same majority of the creditors or members as that required to initially approve the scheme under section 210 of the Companies Act (that is, a majority in number representing 75% in value). Until the issue is directly addressed by the Singapore courts, it will be prudent to ensure that it is fair and reasonable to have such power of amendment and that there are safeguards for affected creditors or members.

The second issue in relation to schemes of arrangement which has been recently addressed in England is whether there can be a "meeting" of creditors or members to approve a scheme of arrangement if it is attended by only one creditor or member. In *In re Altitude Scaffolding Limited* [2006] EWHC 1401, the English High Court

answered this question in the negative, as the meaning of the word "meeting" is very well-established. There must be a coming together of at least 2 persons before there can be a "meeting". Insolvency practitioners should note this ruling, which may be adopted in Singapore.

Cross-Border Insolvency

Cambridge Gas Transport Corporation v The Official Committee of Unsecured Creditors (of Navigator Holdings plc and Others) UKPC 46 contains important pronouncements on cross-border insolvency law by the Privy Council hearing an appeal from the Isle of Man. The US Bankruptcy Court had ordered the implementation of a plan of reorganization under Chapter 11 of the US Bankruptcy Code for an insolvent group of companies incorporated in the Isle of Man. The plan involved a debt-equity swap which would place the companies under the control of their creditors. The US Bankruptcy Court further sent a letter of request to the courts in the Isle of Man asking for assistance in giving effect to the plan.

The companies applied to the courts in the Isle of Man for an order that the US courts did not have jurisdiction to make orders relating to the ownerships of the shares of companies incorporated in the Isle of Man. The Privy Council rejected this application and held that the courts in the Isle of Man could provide assistance to the plan by ordering the transfer of the shares without having to start domestic parallel insolvency proceedings.

The Privy Council recognised that the common law on cross-border insolvency is underdeveloped and that the unifying principles which apply to both personal and corporate insolvency have not been fully worked out. However, the common law principles are sufficient to confer on the court to jurisdiction to give assistance by recognizing foreign insolvency proceedings and doing whatever it can do in the case of a domestic insolvency. The purpose of recognition is to enable a foreign insolvency office holder or the creditors to avoid having to start parallel insolvency proceedings and to give them remedies to which they would have been entitled if the equivalent proceedings had taken place in the domestic forum. Nevertheless, the Privy Council expressed doubts as to whether judicial assistance can extend to the form of applying provisions of a foreign insolvency law which forms no part of the domestic system.

(Lee Eng Beng, Rajah & Tann and Andrew Chan Chee Yin, Allen & Gledhill)

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