

LHAG Insights

Insolvency Feature

ABOUT THE AUTHORS



Kumar Kanagasigam
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

Trends and Developments

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

COVID-19 Crisis

COVID-19 continued to take its toll on the Malaysian economy in 2021.

On 12 November 2021, Bank Negara Malaysia (BNM) reported that Malaysia's economy contracted 4.5% year-on-year in the third quarter of 2021. This comes after a 5.6% contraction of Malaysia's GDP in 2020, which was the second worst contraction since the Asian financial crisis in 1998.

Notwithstanding that, Malaysia recently announced its largest-ever budget, at MYR332.1 billion for 2022. Malaysia's economic growth is reported to accelerate by 5.5% to 6.5% in 2022. BNM also increased its allocation under its fund for small and medium enterprises (SMEs) by MYR4.5 billion, bringing the total available to support SMEs to MYR11.2 billion.

Moratorium and Non-Performing Loans (NPL)

Since the start of the pandemic, the government has introduced various measures to help micro-enterprises and SMEs (MSME), including announcing an automatic moratorium on loan repayments for six months in March 2020. The moratorium was not extended in October 2020, but was re-introduced in July 2021 when the Malaysian economy was severely impacted by enhanced lockdown measures imposed to stop the third wave of COVID-19. In an article that discussed the second moratorium, Fitch Ratings stated that "Reported NPLs may stay low in 2021 with problematic retail and MSME loans not falling due until 2022, but the challenging economic environment remains."

Insolvency practitioners and financiers will no doubt be keeping an eye on how the second moratorium will pan out in 2022.

Court Restructuring

There have been a significant number of reported cases on schemes of arrangement and judicial managements in 2021, with ten applications for judicial management and 28 applications for restraining orders pursuant to a proposed scheme of arrangement being made. By comparison, there were 36 applications for judicial management and 14 applications for restraining orders in 2020. The statistics show important trends for 2022.

Firstly, judicial management was introduced under the Companies Act 2016 (CA 2016), which came into effect on 1 March 2018, and was not popular. Under judicial management, the directors are not in the driving seat of the company: the judicial manager takes control of the affairs, business and property of the company. Unsurprisingly, there were only 16 applications for judicial management in 2018 and nine in 2019.

During the pandemic, financially distressed companies resorted to judicial management presumably because the company was immediately protected upon filing the application, and shielded from court proceedings and winding-up orders. No steps can be taken to enforce any charge or security over the company, nor to repossess any goods under hire purchase or leasing.

Secondly, there was a significant drop in applications for judicial management in 2021. Interestingly, this followed two reported decisions in late 2020 where the court laid down strict criteria for a judicial management order: *Re Sin Soon Hock Sdn Bhd* [2020] MLJU 1242 and *Re Biaxis (M) Sdn Bhd* [2020] MLJU 1188, and recently applied in *Federal Power Sdn Bhd v Dara Consultant Sdn Bhd* [2021] MLJU 2114.

Thirdly, schemes of arrangement proved to be the popular mode of corporate restructuring for public listed companies in particular in 2021, and this trend will probably continue in 2022. In addition to the existing judicial precedents, recent decisions make schemes of arrangement an obvious and predictable restructuring tool: *Mansion Properties Sdn Bhd v Sham Chin Yen & Ors* [2021] 1 MLJ 527; *AirAsia X Bhd v BOC Aviation Ltd & Ors* [2021] 10 MLJ 942; *Sentoria Bina Sdn Bhd v Impak Kejora Sdn Bhd & Ors* [2021] MLJU 1184; and *Re Top Builders Capital Bhd & Ors* [2021] 10 MLJ 327.

Schemes of arrangement also became the only choice of court restructuring mechanism for public listed companies. In October 2021, the High Court dismissed Scomi Group Berhad's application for judicial management because it was not available to public listed companies.

Amendments to CA 2016

Insolvency practitioners anticipate that the government will make significant amendments to the existing corporate rescue mechanisms – see Companies Commission of Malaysia’s (CCM) Consultative Document on The Proposed Companies (Amendment) Bill 2020. The proposed amendments are discussed below.

Scheme of arrangement

Automatic moratorium upon an application for restraining order

Under CA 2016, an application to convene a meeting to propose a compromise or arrangement is typically accompanied by an application for a restraining order, which is sought so that the intended arrangement can be proposed at the meetings with creditors without the threat of winding-up. However, stringent pre-conditions are imposed before a restraining order is allowed.

The new provisions will introduce an automatic moratorium for an initial period of 60 days. This can be extended for ten months if certain conditions are met.

Restraining orders against related companies

Under the new provisions, where it has made a restraining order, the court may, upon the application of a subsidiary, a holding company or an ultimate holding company of that company (Related Companies), grant an order to restrain an action or proceedings against the Related Companies and also the enforcement of security over the property of the Related Companies.

Upon an application made by any creditor of a company or its Related Companies, the court may make orders to restrain the disposition of property other than disposals in good faith and in the ordinary course of business of the company or its Related Companies, and to restrain the transfer of any shares in or altering the rights of any members of the company or its Related Companies.

Super priority for rescue financing

New provisions have been proposed to encourage financiers to provide distressed companies with rescue financing. Rescue financiers will enjoy “super priority” – ie, rescue financiers will be repaid first in priority to existing creditors. A similar provision will also be introduced for judicial management.

Cross-class cram-down in a scheme of arrangement

Under CA 2016, a scheme of arrangement can only be implemented if 75% in value of creditors approve the scheme, which enables a small number of dissenting creditors to jeopardise the entire scheme. The cram-down mechanism is to compel one or more dissenting classes of creditors to be bound by the scheme while at the same time affording adequate protection to those dissenting creditors.

The new provisions can compel one or more dissenting classes of creditors to be bound by the scheme in the following circumstances:

- if the scheme is approved by a majority in number, representing at least 75% of the value, of those present and voting at the meeting of at least one class of creditors;
- if the scheme is also approved by creditors comprising a majority in number, representing at least 75% of the value, of those present and voting at the meetings of scheme creditors as a whole; and
- if the scheme is “fair and equitable” to each dissenting class of creditors and does not “discriminate unfairly”.

Empowering the court to order a meeting to revote

The court has power under CA 2016 to approve a compromise or arrangement subject to such alterations or conditions as it deems just. There is, however, no power to order a revote.

The proposed provision is intended to assist the court in making better decisions with regard to the proposed scheme. It avoids the whole process from having to start all over and will invariably save costs and time.

Codification of the filing, inspection and adjudication of proofs of debt in relation to a scheme of arrangement

This new provision will introduce procedures for proofs of debt for a proposed compromise or arrangement. Among other matters, the new provision will stipulate a deadline for filing a proof of debt and the appointment of a person to adjudicate the proof.

Empowering the court to approve a compromise or an arrangement without having the meeting of creditors

This amendment allows the court to approve a compromise or an arrangement without first having the meeting of creditors, but only if it is satisfied that the creditors would have agreed to the proposed scheme if the meeting of creditors had been convened.

Empowering creditors to apply to the court for a review of the decisions made by the company during the moratorium

This new provision will empower the court to reverse actions or decisions made by the company if there has been an act or

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

omission that results in a breach of the terms of the scheme of arrangement.

Corporate voluntary arrangement and judicial management

Extending accessibility

The amendments extend corporate voluntary arrangements and judicial management to all companies except:

- a company that is a licensed institution or an operator of a designated payment system regulated by the Central Bank of Malaysia; or
- a company that is approved or licensed by the Securities Commission under the Capital Markets and Services Act 2007 or the Securities Industry (Central Depositories) Act 1991, or that is proscribed upon written request by the Ministry of Finance.

Allowing a secured creditor to recover property other than immovable property during moratorium

This provision will allow a secured creditor to recover property other than immovable property during the moratorium of a corporate voluntary arrangement and judicial management. The power is exercisable only in the following circumstances:

- if the property is not required during the voluntary arrangement;
- if the moratorium poses a high risk to the existence of the property; or
- if the value of the property decreases due to the moratorium.

Continuation of supply of essential goods and services

This proposed amendment will ensure that essential goods and services under existing contracts continue to be provided when the company is under a scheme of arrangement, corporate voluntary arrangement or judicial management. This will ensure the operations of the company are not impacted when the company is restructured.