

SECTION I – INSOLVENCY LAW REGIME

I1. Underlying Philosophy

(a) The objectives of corporate insolvency law of Malaysia would probably be better characterised as follows:

- To provide for rehabilitation where possible.
- To ensure preservation and ranking of secured creditor rights and equal treatment of all other creditors where a company cannot be saved.
- To punish delinquent officers who have contributed to the insolvency.

(b) The insolvency law regime in Malaysia therefore combines elements of the distributive, rehabilitative and penal philosophies.

(c) The aforementioned philosophies find their expression in Malaysian corporate insolvency law in the following ways:

- Rehabilitative philosophy manifests itself in section 176 of the Companies Act, which deals with schemes of arrangement and in the Pengurusan Danaharta Nasional Berhad Act 1998. The recital to the latter statute *inter alia* states that its declared aim is to “*assist the business sector by dealing expeditiously with financially distressed enterprises...*”.
- Evidence of a distributive philosophy can be found in Part X of the Companies Act comprising sections 212 to 318 and in particular, to Division 4 of Part X which deals with priorities.
- There is a penal aspect to corporate insolvency law. Provisions exist to punish wrongful trading and fraudulent trading and to punish non-compliance with the insolvency provisions themselves.

I2. Jurisdiction in insolvency matters

(a)

then advertised in two or more national newspapers and fixed for hearing. Any creditor is entitled to appear on the hearing of the petition to support or oppose the petition provided he has filed a "Notice of Intention to Appear" beforehand. If the winding up order is made, the court will appoint a liquidator, who will oversee the liquidation process to ensure an orderly realisation of assets and repayment of creditors and members.

Court Approved Schemes of Arrangement

- Basically, there is no concept of judicial management in Malaysia, nor any form of Chapter 11 Bankruptcy such as in the United States. The only real alternative is a scheme of arrangement that is proposed pursuant to section 176 of the Companies Act. A scheme of arrangement requires the sanction of the High Court, and before such sanction is sought, the scheme has to be approved of by three-quarters (75%) in value and a simple majority in number of each class of creditors present and voting, creditors being divided into classes according to their communality of interests. Various arrangements can be sanctioned by the High Court, including a sale of various assets to a third party. The advantage of such a procedure in the Malaysian context is that by virtue of sub-section (10) of section 176, the subject company that is proposing a scheme can apply to the High Court to grant an order staying all proceedings against the company whilst the scheme is pending before the court. This would apply to all forms of proceedings. Companies have extended the concept of proceedings to "extra-judicial" measures such as the appointment of a receiver and manager under a debenture. Another advantage is that all creditors of the company are bound by this statutory scheme and must comply with the terms thereof and accept the fruits thereof in satisfaction of what was due to them, and no free-for-all ensues.

Private and Court Appointed Receivers

- A secured creditor may appoint a receiver under the terms of a debenture. The receiver takes possession of the assets that are subject to the crystallised charge in the debenture instrument, and he may sell those assets by private treaty for example, except for the special case of land. As observed earlier, if there is a statutory charge on the land, then notwithstanding that the land is subject to the fixed charge under the debenture, the receiver cannot use his power of sale.

The chargee has to initiate formal court based foreclosure proceedings. A court appointment is made where there is no express contractual power to appoint but assets of the debtor are in danger of being spirited away. The powers of a court appointed receiver are always spelt out comprehensively in the order appointing him. In the case of a private appointment, the object is naturally to ensure the interests of the debenture holder are protected and returns to that particular creditor are maximized. In the case of a court appointment, the receiver must balance the interests of all concerned, both debtor and creditors alike as he is an officer of the court.

Special administration Under the Pengurusan Danaharta Nasional Berhad Act 1998

- Special administration under the Pengurusan Danaharta Nasional Berhad Act 1998 aims to assist in the survival of the company as a going concern. It may be initiated by the Danaharta Corporation (the special asset management corporation set up under the said Act) (“the Corporation”) itself or at the request of the corporate debtor’s management. The Corporation may acquire assets and liabilities, for which there are mechanisms provided in the Act itself, namely, sections 13 through to 17. The Act was enacted to enable the Corporation to acquire non-performing loans and the underlying security rights from banks and other financial institutions, as part of a wider plan to recapitalize banks and financial institutions. The corporate debtor for the purposes of this paper would be known as an “affected person” for the purposes of the Act. The board of directors of the corporate debtor qua affected person can apply to the Corporation to appoint a Special Administrator under section 23. Additionally, the Corporation, through an “Oversight Committee” set up under the Act, may appoint the Special Administrator to administer the corporate debtor’s affairs: section 24 of the Act. For special administration by the Corporation, the requirements are that it would serve the public interest and one or both of the following purposes would be served, namely:

- (1) the survival of the corporate debtor and the whole or any parts of its assets as a going concern; or

(2) a more advantageous realisation of the corporate debtor's assets would be achieved than on a winding up.

The Special Administrator has the powers conferred on him under the Second Schedule to the Act [as to which see section J2 of this Paper].

The Special Administrator cannot be appointed without the approval of the regulatory body concerned where a liquidator has already been appointed over the corporate debtor or where a scheme of arrangement has already been approved by the High Court in relation to the corporate debtor qua "affected person". Also, appointments over affected persons whose businesses are regulated under one of the following statutes will require the approval of the regulatory body concerned:

- The Insurance Act 1996.
- The Banking and Financial Institutions Act 1989.
- The Securities Industry Act 1983.
- The Futures Industry Act 1993.
- Securities Industry (Central Depositories) Act 1991.
- Offshore Banking Act 1990.
- Islamic Banking Act 1983.

Once the special administrator is appointed, then a moratorium shall take effect during the first 12 months duration of the administration (subject to extension under section 41(3)), during which the Act in section 41 provides:

- Any petition to wind up the corporate debtor has to be dismissed.
- There can be no voluntary or compulsory winding up.

- No receiver, manager or provisional liquidator may be appointed except by one of the regulatory bodies named in the Act itself.
- No steps may be taken to enforce a security, or execute upon a judgment or re-possess any asset or set-off any debt except with the prior consent of the corporation.
- No legal proceedings may be commenced or continued and no execution or distress may be levied except with the prior consent of the corporation.
- No proceedings and no execution or other legal process may be commenced or continued against any person acting as a guarantor of the corporate debtor's debt except with the prior consent of the corporation.
- Any application for a scheme of arrangement under section 176 of the Companies Act has to be immediately adjourned sine die and any restraining order granted under section 176(10) has to be immediately discharged and set aside.

(c) **Legislation**

The relevant legislation governing each type of insolvency procedure available for corporate debtors is as follows:

- For liquidation, Part X of the Companies Act 1965.
- For court approved schemes of arrangement, section 176 – 178 of the Companies Act 1965.
- For special administration by Danaharta Corporation, the Pengurusan Danaharta Nasional Berhad Act 1998.
- For court appointments of receivers, the First Schedule to the Courts of Judicature Act 1964 read with Order 30 of the Rules of the High Court

1980.

14. Commencement of insolvency procedures

- (a) It is neither usual nor customary for a corporate debtor to initiate negotiations towards an informal administration before formal insolvency procedures are commenced.
- (b) Commencement of each procedure is by:
- For liquidation under Part X of the Companies Act 1965, the corporate debtor, or a member or a creditor (regardless of whether secured or not) can initiate the process.
 - For court approved schemes of arrangement under section 176 – 178 of the Companies Act 1965.
 - For special administration by Danaharta Corporation, the Pengurusan Danaharta Nasional Berhad Act 1998.
 - For court appointments of receivers, the First Schedule to the Courts of Judicature Act 1964 read with Order 30 of the Rules of the High Court 1980.
- (c) The basis on which the various insolvency procedures referred to can be commenced or the requirements in respect thereof are as follows:
- For liquidation, Part X of the Companies Act 1965, non-payment of debts or inability to pay debts as they fall due.
 - For court approved schemes of arrangement, section 176 – 178 of the Companies Act 1965, a concrete bona fide proposal for a scheme of arrangement.
 - For special administration by Danaharta Corporation under the Pengurusan Danaharta Nasional Berhad Act 1998, the requirements for the

appointment of a Special Administrator are that it would serve the public interest and one or both of the following purposes would be served, namely:

(1) the survival of the corporate debtor and the whole or any parts of its assets as a going concern; or

(2) a more advantageous realisation of the corporate debtor's assets would be achieved than on a winding up.

- For court appointments of receivers under the First Schedule to the Courts of Judicature Act 1964 read with Order 30 of the Rules of the High Court 1980, the basis is that it would be just and convenient that a receiver be appointed and that his appointment is necessary in order to preserve assets which may be in jeopardy.

(d) Each of the insolvency procedures set out below is commenced in the following manner:

- Compulsory liquidation is commenced by the filing in the High Court of a petition for the winding up of the corporate debtor and service of it on the debtor.
- A scheme of arrangement is commenced by the filing of an originating summons seeking leave of court to call and convene meetings of classes of creditors and members of the corporate debtor with a view to considering and voting on a scheme of compromise and arrangement. This is followed by sending notices of class meetings to the creditors and members concerned: section 176 of the Companies Act.
- Special administration by a Special Administrator appointed by Pengurusan Danaharta Nasional Berhad is initiated by either a request being made by the directors of the corporate debtor for such an appointment or by Danaharta making the appointment with the approval of its "Oversight Committee": sections 23 and 24 of the Pengurusan Danaharta Nasional Berhad Act 1998.

- Court appointed receiver's appointment is initiated by an application by a member or creditor of the corporate debtor by summons in a pending action by that member or creditor against the corporate debtor.
- (e) In the context of a scheme of arrangement or liquidation, the time frame would be approximately one year. As previously mentioned there is no concept in Malaysia of formal court based insolvency administration.
- (f) The Courts are only moderately effective in their handling of formal insolvency proceedings as procedures can be cumbersome and there is some

- ***Interests of Shareholders/Owners***

Proprietary interests of shareholders are unaffected by any of the insolvency procedures save that the right to transfer their interests is restricted by section 223 of the Companies Act 1965 which applies once winding up is deemed to have commenced under section 219(1) of the Act.

- ***Contracts to which the debtor is a party***

Under Malaysian law, contracts do not ipso facto terminate when a winding up order is made. However, under section 296 of the Companies Act, the Liquidator can disclaim unprofitable contracts. The counterparty to the contract is relegated to a claim in damages which ranks as an unsecured debt.

Similarly, the Special Administrator under the Pengurusan Danaharta Nasional Berhad Act 1998 can disclaim unprofitable contracts pursuant to section 40(1) of the Act. The counterparty to the contract is relegated to a claim in damages which ranks as an unsecured debt.

A privately appointed receiver can terminate contracts to which the debtor company is a party to except where the goodwill of the corporate debtor would be affected adversely.

- ***Legal proceedings to which the organization is a party***

When winding up proceedings are commenced against a corporate debtor, and before a winding up order is made, the corporate debtor can apply for other legal proceedings against the debtor company to be stayed pending the disposal of the winding up proceedings under section 222 of the Companies Act 1965. Once a winding up order is made, all actions against the corporate debtor cannot be proceeded with unless by leave of court: section 226(3).

When a corporate debtor has applied to court for leave to convene

meetings of its creditors and members to consider and if thought fit approve a scheme of compromise and arrangement under section 176 to 178 of the Companies Act 1965, the court can restrain all legal proceedings against the corporate debtor until the conclusion of the scheme proceedings.

For special administration under the Pengurusan Danaharta Nasional Berhad Act 1998, under section 41 of that Act, a moratorium takes effect for a period of 12 months with the possibility of an extension of such moratorium.

The appointment of a private receiver or a court appointed receiver over a corporate debtor does not have any effect on the continuation or commencement of legal proceedings against the corporate debtor.

- ***Remedies available to persons in contractual relationships with the debtor***

The remedies of specific performance and damages for breach of contract remain available to a contracting party even after a corporate debtor has become the subject of liquidation proceedings subject to the caveat that:

- ◆ in liquidation the liquidator can disclaim the contract; and
- ◆ in receivership, specific performance will be disallowed if performance of the contract would require outlay of funds by the receiver.

- (b) The effect of a second insolvency procedure where another procedure has already been initiated in respect of the same corporate debtor depends on the type of insolvency procedure in question:

Proposal for Scheme of Arrangement where winding up already commenced

- The Court can temporarily restrain prosecution of the winding up petition under section 176(10) of the Companies Act 1965 where the respondent debtor proposes a scheme of arrangement. The winding up petition can be subsequently dismissed

if the proposed scheme of arrangement attains the required statutory majorities and is approved by the High Court.

Special Administration is initiated where scheme of arrangement already initiated

- Any application for a scheme of arrangement under section 176 of the Companies Act has to be immediately adjourned sine die and any restraining order granted under section 176(10) has to be immediately discharged and set aside if a special administrator has been appointed under the Pengurusan Danaharta Nasional Berhad Act 1998.

Special Administration is initiated where winding up proceedings have been commenced

- Any petition to wind up the corporate debtor has to be dismissed if a special administrator has been appointed under the Pengurusan Danaharta Nasional Berhad Act 1998.

Winding up proceedings commenced when private receiver and manager already appointed

- The commencement of winding up proceedings does not affect the powers of a privately appointed receiver and manager.

Winding Up Order granted where private receiver and manager already appointed

- Pursuant to the decision of the Supreme Court of Malaysia in *Kimlin Housing Development Sdn Bhd (In Liquidation)(Receiver and Manager appointed) v Bank Bumiputra Malaysia Bhd* [1997] 2 MLJ 805, the powers of a privately appointed receiver and manager terminate upon the appointment of a liquidator.