# Malaysia Overview

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## The current status of Malaysian insolvency law

The year 2016 was a watershed in Malaysian insolvency law. After a gap of 51 years, the Companies Act 1965 (Act 125, Malaysia) (the CA 1965) was repealed and replaced by the Companies Act 2016 (Act 777, Malaysia) (the CA 2016). For the first time, the CA 2016 introduced in Malaysia corporate rescue mechanisms that were common and widely used elsewhere in the common law world. Improvements were made to the winding-up and schemes of arrangement regimes; however, many areas where reform was much needed remained untouched.

## The legislative background to the CA 2016

Legislation governing Malaysian company law and insolvency law has generally followed English and Australian statutory models. By the early 1960s, the earlier colonial era legislation had become outdated, and newly independent Malaysia needed a modern company law statute. Eventually the CA 1965 was enacted. It was based on the 1961 Australian legislation, but with some elements of the 1948 English Companies Act. The draftsman of the Australian Uniform Companies legislation assisted in the preparation of the bill of what was to become the CA 1965. This remained law for 51 years.

By the early 2005, the CA 1965 was outdated and reform was on the cards. In 2004 the Corporate Law Reform Committee (CLRC) was established and charged with making recommendations regarding the modernisation of company law and corporate insolvency law in Malaysia. It published its report in 2008, and the cabinet approved most of its recommendations in 2010. An exposure draft of the proposed Companies bill was published in 2013 for public consultation, and eventually the CA 2016 was passed. It received royal assent in August 2016. All parts of the CA 2016, other than the new corporate rescue provisions, came into force on 31 January 2017. There is no indication of when the corporate rescue provisions will come into force.

## The applicability of English law in Malaysia

By section 3 of the Civil Law Act 1956, the common law of England and the rules of equity continue to be relevant and applied to the Federation of Malaysia, but to differing degrees in West Malaysia and East Malaysia. In West Malaysia, the common law and rules of equity as administered in England on 7 April 1956 apply. In East Malaysia, there is a temporal difference regarding the cut-off date. For Sabah, English common law and rules of equity, and statutes of general application as administered or in force, as the case may be, in England on 1 December 1951 will apply. For Sarawak, the corresponding date is 12 December 1949, subject to some qualifications that are beyond the scope of this article.

The reception of English common law, rules of equity and (for East Malaysia) statutes of general application is permitted only insofar as no other provision has been made under written law in force in Malaysia, and even then only to the extent that the circumstances of Malaysia and its inhabitants permit. This last qualification has allowed the Malaysian courts to not apply the position under common law in England where, for example, local mores do not permit the same.

Also, because English law is theoretically frozen as at the specified dates referred to above, the domestic application of developments in English common law and equity after the cut-off dates is not automatic. In practice, Malaysian courts do take cognisance of such matters and readily apply common law or equity as they stand in present-day England unless one or more of the statutory qualifications prevent the same being recognised and applied.

## A summary of corporate insolvency procedures

Not all corporate insolvency processes are governed by the CA 2016. There are specialised regimes under the Financial Services Act 2013 (FSA) and the Malaysia Deposit Insurance Corporation Act 2011 (MDICA) in respect of the insolvency of licensed financial institutions in Malaysia. Only the MDICA regime will be considered, as the FSA regime is of limited application.

In 2015, an entity-specific restructuring statute – the Malaysian Airline System Berhad (Administration) Act 2015 – was enacted, which facilitated the administration and restructuring of Malaysia Airlines and the transfer of its business to a new entity under statutory protection.

There are six main generally applicable corporate insolvency processes under Malaysian law, namely schemes of arrangement, corporate voluntary arrangements (CVA), receivership, judicial management, administration by a conservator and liquidation.

- Schemes of arrangement are not exclusively intended for insolvent companies and are widely utilised by solvent entities. Nevertheless, the scheme of arrangement process is commonly used by insolvent companies for purposes of restructuring, while receiving the benefit of court-supervised restraining orders restricting various forms of recovery and enforcement actions against the company. A scheme of arrangement allows for the court-approved scheme to be imposed on dissenting creditors and members, provided the statutory voting majorities have been obtained.
- CVA is a newly introduced corporate rescue mechanism under the CA 2016. It provides a consensual statutory restructuring tool that is available to private companies only. Similar to schemes of arrangement, the CVA process permits a proposed voluntary arrangement to be imposed on and thereby bind all creditors, provided the statutory voting threshold is achieved.
- Receivership is primarily a contract-based, private security enforcement remedy against insolvent corporate entities that is supported by established common law principles, which are complemented by statute in Malaysia. Receivership involves the appointment of an insolvency practitioner as a receiver, or as a receiver and manager, under the terms of a security document, usually a debenture containing a fixed or floating charge or both, with wide-ranging rights to take possession of assets of the corporate debtor and realise the same by sale.
- Judicial management is another of the new corporate rescue

mechanisms under the CA 2016 that allows for the appointment by the Malaysian High Court of a judicial manager over an insolvent corporate debtor, in circumstances where it can be shown that there is a reasonable prospect of, inter alia, preserving all or part of the company as a going concern and where interests of creditors would be better served than on a winding up.
- Conservatorship is provided for under the MDICA. It is a procedure that permits the appointment by the Malaysia Deposit Insurance Corporation (MDIC) of a special insolvency administrator known as a conservator over an 'affected person'. By definition, this includes a corporate entity that is indebted to a financial institution which is a member institution under the deposit insurance scheme administered by the MDIC, or has given security to the financial institution for an obligation owed to that institution by another company. It is essentially a form of statutory administration that confers few rights on the affected person or its creditors.
- Liquidation is governed by the CA 2016. It can be voluntary or compulsory and, under the Act, there are separate regimes for each. However, ultimately both regimes facilitate the appointment of an insolvency practitioner as liquidator who will, inter alia, collect and realise assets, undertake a proof of debt exercise to resolve creditor claims, investigate past transactions for potential clawback, distribute dividends to creditors in satisfaction of claims, and eventually to dissolve the company, which thereby ceases to exist.

## Schemes of arrangement

Any company or a creditor of a company, and a liquidator if a company is in the process of being wound up, and a judicial manager if a company is in judicial management, can initiate a scheme.

### Initiating a scheme

Under the CA 2016, the entire process requires court involvement from start to finish. Initiating a scheme requires the applicant to seek an order of court to convene meetings of the members and various classes of creditors of the company. The statutory voting threshold that is necessary to achieve agreement to the terms of a scheme is 75 per cent of the total value of creditors or class of creditors and members, or class of members present and voting at the court-convened class meeting, either in person or by proxy.

### Assessing the viability of a scheme

For the first time under the CA 2016, the High Court has the power to appoint an approved liquidator to assess the viability of the proposed scheme. The approved liquidator will have to prepare a report for submission to the applicant. This report will then be tabled at the court-convened class meetings for the members and creditors to consider prior to voting.

### Court approval

Any scheme that has achieved the requisite statutory voting majorities still needs to be approved by the High Court, as the scheme derives its binding effect from the court order. In considering whether to approve the scheme, a Malaysian court will normally consider whether:
- all procedural requirements have been fulfilled;
- the approved liquidator's report had indicated that the scheme is viable;
- the members and creditors had all the relevant and necessary information they would require to make an informed decision; and
- the scheme is sufficiently fair and reasonable that an honest and intelligent member or creditor, as the case may be, would approve it.

### Restraining orders

Prior to the introduction of the CVA and judicial management processes in the CA 2016, the scheme of arrangement procedure constituted the main formal court rescue process available under Malaysian law. A key feature of the scheme process at that time was the availability of a court-granted restraining order that restrained all forms of legal action by creditors and other parties against the subject company. This was one feature that made the process attractive to debtor companies that had a viable business but needed time to reach a compromise with creditors.

The CA 2016 provisions continue to allow the court to grant restraining orders of an initial period of three months, which may be renewed for a period of up to a further nine months. In order for a restraining order to be granted, the applicant has to ensure that a number of conditions laid down in the CA 2016 are complied with. While a restraining order is in force, the company is not permitted to dispose of any property or to acquire any new property other than in the ordinary course of its business, and if it does, the disposition or acquisition will be void.

### Reform

Despite having the opportunity to overhaul and improve the scheme process, the CA 2016 did not include certain enhancements that would have improved it and made it more attractive as a formal process that did not need management to be displaced, in contrast to judicial management. Among possible improvements would have been the introduction of provisions permitting rescue financing and allowing for new funders to achieve elevated levels of priority over existing lenders, as well as allowing for pre-packaged schemes that would then allow such schemes to be expedited through the Malaysian courts. An opportunity was also missed to give the approving court the power (to be exercised in well-defined circumstances and within narrow parameters to avoid unfair prejudice) to allow a scheme to be approved, notwithstanding that one class of creditors or members did not approve the scheme at a class meeting.

## CVA

### A new corporate rescue tool

For the first time in Malaysia, the CA 2016 introduced the CVA procedure. It is available only to private companies, but also excludes companies that are holders of licences issued under the FSA and the Capital Markets and Services Act 2007 (CMSA). Any company that has created a charge over its assets is also ineligible. This will no doubt significantly reduce the availability of CVA to private companies.

### The nominee

A company under judicial management may make a CVA proposal through the judicial manager. A liquidator of a company under liquidation may also make a proposal. The CVA process starts with the appointment of a nominee, who must be a licensed insolvency practitioner. It is a requirement that the proposed CVA and a statement of affairs must be submitted to the nominee. The nominee is required to monitor the company's affairs during the moratorium. He or she is required to form an opinion as to whether the proposed arrangement has a reasonable prospect of being approved and implemented, and whether the company will have sufficient funds during the moratorium to enable it to carry on business. Where a judicial manager or a liquidator initiates a corporate voluntary arrangement, the judicial manager or liquidator may also take on the role of the nominee.

### The CVA process in outline

There is an initial 28-day moratorium that commences when the

CVA documents are lodged with the High Court. The effects of the moratorium are spelled out in paragraph 17 of the Eighth Schedule to the CA 2016. Meetings of members and creditors of the company are summoned to consider the proposed voluntary arrangement. At these meetings, the members and creditors may extend the moratorium for not more than 60 days.

The CVA voting thresholds have been set at a majority in excess of 50 per cent of members and 75 per cent in value of creditors. Once the statutory meetings approve the proposed voluntary arrangement, it becomes binding on all creditors, regardless of how they voted. The appointment of a supervisor is also provided for, who is charged with implementation of the arrangement. The supervisor may be the original nominee, but may also be any other licensed insolvency practitioner.

A secured creditor's right to enforce its security is preserved, notwithstanding the approval of the CVA proposal. The insertion of this reservation is curious, because a company that has charged its assets is not in fact eligible for the CVA process.

## Receivership

### The appointment of a receiver and manager

While the CA 1965 contained only a few provisions dealing with receivers and managers, this has changed under the CA 2016. Various provisions now cover a whole host of matters. Before the CA 2016, many of these were left to the terms of the debenture and the instrument under which the receiver, or receiver and manager, were appointed.

The CA 2016 also now expressly contemplates the possibility that a receiver, or receiver and manager, may be appointed by court.

### The receiver's powers and duties

Before the CA 2016, the powers of the receiver, or receiver and manager, were typically spelled out in the privately negotiated debenture. The CA 2016 has for the first time introduced a statutory list of powers of a receiver or receiver and manager. These are contained in the Sixth Schedule to the CA 2016, and comprise the typical powers of a receiver or receiver and manager.

The CA 2016 has not changed the nature or extent of the duties of a receiver, or receiver and manager. The position remains largely as before whereby in the case of a private appointment, his or her primary duty is to the debenture holder. His or her duty is principally to take possession of the assets of the company and realise them for the benefit of the debenture holder, subject to a duty owed to the company to obtain the best possible price reasonably attainable under the market conditions at the time of sale. Where the appointment is by the court, the receiver, or receiver and manager, will be regarded as an officer of the court and therefore must act fairly and even-handedly in the interests of all parties.

### Interaction with liquidation

During the many years when the position seemed settled under common law, certain court decisions resulted in uncertainty regarding the extent of a receiver's powers after winding up had commenced. In particular, doubts were cast on the receiver's ability to meaningfully continue in office at all after a liquidator had been appointed, and specifically on the receiver's power to realise property privately without going through a formal judicial sale process, whether before or after liquidation commenced.

The doubts have been dispelled by a series of recent decisions of the Federal Court, Malaysia's highest court. Now the CA 2016 clearly and emphatically provides that, after commencement of the winding up of a company:

- a receiver may continue to act as receiver and exercise all the powers of a receiver in respect of all the assets comprised in his or her appointment under the terms of the debenture in question;
- over and above that, a receiver and manager may exercise all the powers of a receiver and manager for the purpose of carrying on the business of a company provided that the receiver and manager secured the consent of the liquidator, or failing such consent, the consent of the court; and
- if the receiver and manager does obtain the requisite consent, then when carrying on the business of the company, he or she will continue to be an agent of the company.

## Judicial management – a new corporate rescue tool

### Eligibility

Although most companies are eligible, companies holding licences under the FSA, and holders of capital markets and securities industry licences under the CMSA, are ineligible for judicial management.

### The judicial management process in outline

Either the company or a creditor may make an application for the appointment of a judicial manager. Besides inability to pay debts, the applicant must show that there is a reasonable probability of preserving all or part of the company as a going concern, and that the interests of creditors would be better served than with a winding up. A debenture holder may object to the application, and if it signals that it intends to appoint a receiver, or receiver and manager, the court must dismiss the application unless public interest requires that the court should override the debenture holder's objection.

During the period between the application being made and either a judicial management order or dismissal of the application being made, there is a limited stay on certain types of creditor action. Following the judicial management order, a wider range of creditor action is restrained. There is a good balance between protecting creditors and encouraging prospects of a rescue. A judicial management order initially lasts for six months but can be extended for a further six months.

The appointment of a judicial manager displaces the directors. He or she manages the business and must within 60 days (which can be extended by the court) present a proposal to the creditors of the company. He or she has to summon a meeting of creditors to consider and vote on the proposal. The voting threshold is 75 per cent in value of creditors whose claims have been accepted by the judicial manager, present in person or by proxy. Any proposal that is approved is binding on all creditors, regardless of how they voted.

The judicial manager oversees the implementation of the proposal. Once the purpose of judicial management has been achieved, he or she may apply to discharge the order. If a proposal is not approved at the creditor meeting, the court would normally discharge the judicial management order, and either receivership or liquidation beckons.

## Conservatorship

### Background

An insolvency officer known as a conservator was first introduced into Malaysian law under the Malaysia Deposit Insurance Act 2005, when the Malaysia Deposit Insurance Corporation was first established and a deposit insurance scheme covering member financial institutions was first set up.

The Malaysia Deposit Insurance Corporation Act 2005 was repealed in 2001 and replaced with the Malaysia Deposit Insurance Corporation Act 2011 (MDICA). Chapter 2 of Part IX of the MDICA maintains the provisions relating to the appointment of conservators.

## Circumstances in which a conservator can be appointed

A conservator can only appointed by the Malaysia Deposit Insurance Corporation. Under Part VII of the MDICA, Bank Negara Malaysia, which is Malaysia's Central Bank, can inform the Malaysia Deposit Insurance Corporation that a licensed financial institution regulated by Bank Negara, and which is a member institution in respect of the deposit insurance scheme administered by the Corporation, has ceased to be viable or is likely to cease to be viable.

The Corporation may exercise statutory powers under the MDICA to acquire assets from the member institution concerned and vest the assets in it, or to transfer assets of the member institution to a subsidiary of the corporation that has been designated as a bridge institution. Non-performing loan accounts under which debtors and obligors of the member institution have defaulted could be among the assets acquired or transferred, as the case may be. The corporate debtors that owe a duty or liability to the Corporation under non-performing loan accounts that have been vested in the Corporation, and subsidiaries of the debtors, as well as companies that have provided security for those obligations and liabilities, are all known as 'affected persons'.

The Corporation can appoint one or more conservators over an affected person where, among others, it can be shown that (i) the primary affected person is unable to pay its debts or fulfil its obligations to its creditors, or is likely to be unable to pay its debts or fulfil its obligations to its creditors; and (ii) the survival of the primary affected person and the whole or part of its assets as a going concern may be achieved.

## Powers and duties of a conservator

A conservator has very wide-ranging powers that enable the conservator to run the business of the affected person and to realise its assets with the widest possible discretion and with the minimum of interference by and accountability to stakeholders of the primary affected person.

## Moratorium

A statutory moratorium takes effect upon the appointment of a conservator. It will initially last for 12 months, but the Malaysia Deposit Insurance Corporation may extend it for as long as the Corporation considers it necessary. No legal proceedings or insolvency processes of any kind can be initiated or continued with vis-à-vis the affected person, no assets may be repossessed, no debts can be set off, and no security can be enforced.

## Proposal

The principal end objective of the conservator is the preparation of a proposal, which will contain the conservator's plan for the affected person. Only secured creditors are entitled to vote on and approve the proposal. Once approved, the proposal binds the affected person, its shareholders and creditors.

## Liquidation

As was the case under the CA 1965, there are two types of liquidation under the CA 2016, namely voluntary liquidation and compulsory liquidation. The former commences with the passing of a resolution of the members of the company to wind up the company. The latter is court based and is typically, though not exclusively, initiated by a creditor. Occasionally a regulator, such as the central bank or the Securities Commission, may also initiate compulsory liquidation proceedings against entities that they regulate under the FSA and CMSA respectively. The CA 2016 has in some respects modernised the winding-up framework.

## Voluntary liquidation

There are two categories of voluntary winding up – members' voluntary liquidation and creditors' voluntary liquidation. Both types are commenced when a special resolution by members to wind up the company is passed, but the liquidation can only be a members' voluntary liquidation if the company is solvent and its directors are able to make a statutory solvency declaration. Under a members' voluntary winding up, as the company is supposed to be solvent, it is envisaged that all creditors will be paid in full. The members therefore appoint the liquidator. However, if it is not possible for a solvency declaration to be made, or if one is not made for any reason, then the voluntary winding up can only proceed as a creditors' voluntary winding up, in which case, the creditors appoint the liquidator.

## Compulsory liquidation

Compulsory liquidation is typically initiated by the filing of a winding-up petition by a creditor, invariably for non-payment of debts as and when they fall due, though it is also possible for a member to file a petition to wind up the company on various grounds, including shareholder conduct that makes it just and equitable to wind up the company.

## Changes to commencement of winding up by the court

Under the CA 1965, compulsory winding up was deemed to commence from the date of the presentation of the winding-up petition and voluntary winding up from the date the members' resolution is passed. Now, under the CA 2016, the position is changed for compulsory winding up by the court. If the presentation of a petition to wind up a company in court was preceded by a resolution to voluntarily wind up the company, the winding up by the court is deemed to commence from the date of the members' resolution, and in any other case, the winding up by court is deemed to commence from the date of the winding-up order and not the date of presentation of the petition.

## Enhancements to qualifications of liquidators

Under the CA 1965, in order to be eligible for a liquidator's licence, an applicant had to also hold an audit licence. This was seen as unduly restrictive, but remained the position for more than 50 years. Now, the CA 2016 has decoupled the liquidator's licence from the audit licence.

Furthermore, because of the audit licence requirement under the CA 1965, a liquidator could only come from the ranks of licensed members of the auditing profession. Under the CA 2016, however, a previously ineligible professional body can seek to be prescribed as a recognised professional body and, if so prescribed, any member of such a body may apply to be an approved liquidator.

## Revisions to the avoidance of transactions regime

A substantial number of the avoidance provisions contained in the Bankruptcy Act 1967, which regulated the bankruptcy of individuals, had been referentially incorporated into the CA 1965. The CA 2016 has abandoned this approach and those provisions have been redrafted and placed within the Act.

Although many commonwealth jurisdictions frame their preference and avoidance provisions in terms that focus on either the effect of the same on the position of the creditor, or the intentions of the parties, Malaysia's undue preference provisions remain unchanged in the sense that every transaction falling within a specified duration is deemed a preference, regardless of intention or effect. However, there is a provision for carving out transactions that would otherwise be in breach of the CA 2016 if the creditor or other person dealing with the company provided valuable consideration and had no notice of the

company's inability to pay its debts or of the winding-up proceedings having been commenced.

## Cross-border insolvency

Despite the opportunity to introduce reforms in the area of cross-border insolvency, the CA 2016 mirrors the position under the CA 1965 in that there really is no provision for cross-border assistance or cooperation of any kind relating to foreign insolvency proceedings or Malaysian insolvency proceedings that have a foreign dimension.

## Third-party funding arrangements

One area that could have been addressed in the CA 2016 is that of third party funding for liquidators to pursue actions that could potentially increase the company's estate and enhance the recovery for creditors. It is not clear at all under Malaysian law as to whether a liquidator can lawfully enter into valid third-party funding arrangements, although courts in jurisdictions such as Hong Kong and Singapore have been prepared to allow a liquidator to use existing powers under their statutes to engage in a sale of the right of action. Legislative intervention when the CA 2016 was enacted might have clarified the position and helped nudge the Malaysian courts in the right direction and sidestep concerns regarding maintenance and champerty.

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