STEPHENSON HARWOOD
(SINGAPORE) ALLIANCE

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Going concerns

Restructuring and insolvency

In this eleventh edition of the Going concerns, we touch upon the clarity provided by the Singapore Court of Appeal in the recognition of foreign solvent liquidations in Singapore, a potential new tool against debtors defrauding creditors, and an update on the sanction of an administrative convenience class in the Singapore High Court.

We hope you enjoyed this edition of the Going concerns and we look forward to your continued support in the coming editions of the same. As usual, please feel free to contact us should you like to learn more on any topic.

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Recognition for solvent liquidations

Following up on our previous editions of the Going concerns where we covered, amongst others, the requirements for a proceeding to qualify as a "foreign proceedings" as well as the utility and necessity of the recognition regime under Singapore's adoption of the United Nations Commission on International Trade Law (UNCITRAL) Model Law on Cross-Border Insolvency (30 May 1997) ("**UNCITRAL Model Law**") as set out in the third schedule of the Singapore Insolvency, Restructuring and Dissolution Act 2018 ("**IRDA**") (the "**SG Model Law**"), we provide an update on the latest Court of Appeal decision finding that solvent voluntary liquidations may also be recognised under the SG Model Law.

Under the SG Model Law, the Singapore Courts may only recognise a foreign proceeding where it comes within the meaning of Article 2(h) of the SG Model Law, as follows:

"*collective judicial or administrative proceeding in a foreign State, including an interim proceeding, under a law relating to insolvency or adjustment of debt in which proceeding the property and affairs of the debtor are subject to control or supervision by a foreign court, for the purpose of reorganisation or liquidation*".

The main issue was whether a solvent voluntary liquidation was a "*law relating to insolvency or adjustment of debt*" and the Singapore Court of Appeal found that it was, for, amongst others, the following reasons:

1. The ordinary meaning of Article 2(h) allows the Singapore Courts to recognise solvent liquidations

The SG Model Law did not adopt the UNCITRAL Model Law without modifications and the words "or adjustment of debt" was added to the definition of foreign proceedings in Article 2(h) which tracks Section 101(23) of Chapter 15 of the Bankruptcy Code 11 USC (US) (1978) (the "**US Bankruptcy Code**").

This phrase "*adjustment of debt*" appears in various provisions within Chapter 11 of the US Bankruptcy Code and refers to the preservation of going concerns; the maximisation of property available to satisfy creditors; and the restructuring of a business' finances to pay off creditors and produce a return for shareholders. These situations were not only applicable to insolvent companies but applied to solvent companies. This is in recognition of the great value which may be achieved in allowing a solvent company to take advantage of restructuring tools before it reaches an insolvent state beyond repair.

2. The SG Model Law does not expressly exclude recognition of solvent liquidations

While the original intent of the UNCITRAL Model Law was undeniably intended to be focused primarily on companies that are either insolvent or in severe financial distress, the Court of Appeal did not think that expanding the ambit of the UNCITRAL Model Law to include solvent companies would undermine the purpose of the SG Model Law (or the UNCITRAL Model Law for that matter) nor was there an intention to exclude application of the SG Model Law to solvent companies.

Put simply, the Court of Appeal took the view that if the drafters of the UNCITRAL Model Law wished to exclude its application to solvent liquidation, it would have been simple to include express language to that effect.

Further, the Court of Appeal placed emphasis that a solvent liquidation satisfied the other requirements of a foreign proceeding (see our February 2022 edition of the Going concerns) and therefore still achieved the purpose of the SG Model Law. This was unlike other simple proceedings such as striking a company off the register and proceedings pertaining to the investigation of misappropriated corporate funds which would not be considered a foreign proceeding.

3. There were sufficient safeguards to address practical concerns

One of the main objections raised to the recognition of solvent liquidations was that allowing this would create absurd outcomes such as:

(a) an automatic moratorium to solvent companies when solvent companies typically would not be entitled to such a shield against litigation; and

(b) the solvent company would be presumed to be insolvent under Article 31 of the SG Model Law.

On the first concern – Article 20(6) of the SG Model Law grants the Court wide discretion to modify or terminate any stay or suspension on such terms as the Court thinks fit. The Singapore courts may therefore recognise a solvent liquidation without an accompanying moratorium being maintained.

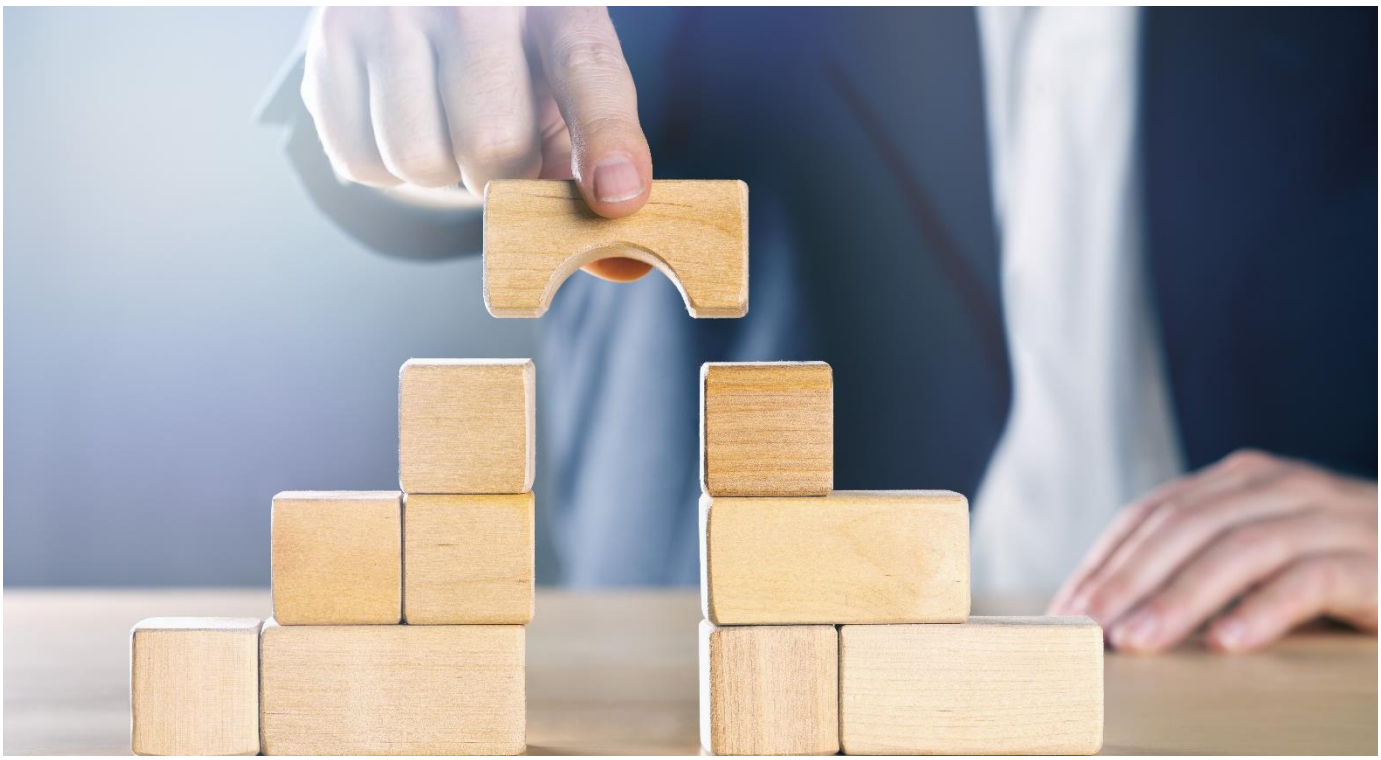
On the second concern – the Court noted that Article 31 of the SG Model Law is qualified by the words "*[i]n the absence of evidence to the contrary*" and it is therefore inconceivable that a solvent company so recognised would be able to invoke the presumption of insolvency.

Conclusion

The judgment brings clarity, in that it is now clear that solvent liquidations may be considered a "foreign proceeding" and recognised under Singapore law.

Potential new tool against debtors defrauding creditors

Section 438 of the Insolvency, Restructuring and Dissolution Act 2018 ("**IRDA**") (Transactions defrauding creditors) is a new creature under the IRDA replacing Section 73B of the Conveyancing and Law of Property Act 1994 (Voluntary conveyances to defraud creditors voidable); and mirroring Section 423 of the United Kingdom's Insolvency Act 1986 (Transactions defrauding creditors). The Singapore Court sheds light on the application of Section 438 of the IRDA in the case of *DDP (in his capacity as the joint and several trustees of the bankruptcy estate of [B]) and another v DDR (a minor) and another* [2023] SGHC 285 ("***DDP***").



Background

In *DDP*, the bankrupt ("**Bankrupt**") had within 3 years prior to the bankruptcy application purchased a property (the "**Property**") and executed a trust deed for him to hold the property on trust for his son for no consideration (the "**Transfer**").

The joint and several trustees of the bankruptcy estate sought, amongst others, declarations that the Transfer was (a) an undervalue transaction (under Section 361 of the IRDA); and (b) was made with the intent to defraud the creditors of the Bankrupt (under Section 438 of the IRDA).

The Court held that the Transfer was an undervalue transaction under Section 361 of the IRDA and vested the beneficial interest of the Property in the bankruptcy estate of the Bankrupt. The Court did not make an order with respect to Section 438 because it did not have the benefit of full arguments from both parties on the same but nonetheless took the opportunity to make some observations on Section 438 of the IRDA.

Under Section 438 of the IRDA, if the Court is satisfied that the transaction was entered into:

(a) at an undervalue; and

(b) for the purposes of (i) putting assets beyond the reach of a person who is making a claim against

the debtor; and (ii) prejudicing the interests of any person in relation to a claim which the person is making or may make against the debtor,

the Court may restore the position to what it would have been if the transaction had not been entered into; and protect the interests of any person who is, or is capable of being, prejudiced by the transaction.

1. Undervalue transaction

Whether a transaction is entered into at an undervalue is to be determined by the same principles and requirements for a transactions an undervalue under Section 361 of the IRDA.

An undervalue transaction is one where the transfer of property is:

(a) a gift; or on terms that provide for the debtor to receive no consideration;

(b) in consideration of marriage; and

(c) in consideration where the value of which, in money or money's worth, is significantly less than the value, in money or money's worth, of the consideration provided by the debtor.

2. Intention to defraud creditors

The debtor must have subjectively intended to put the assets beyond the reach of actual or potential creditors. It sufficed that this was a substantial purpose, though not the sole or dominant purpose.

Remedies to be granted by the Court

In determining the remedies to be granted, the Court considered that the following principles would apply:

(a) The nature of any order and the extent of the relief granted by the Court should take into account the mental state of the transferee, and the degree of his involvement in the fraudulent scheme of the debtor to put assets out of the reach of the creditors.

(b) Where the transferee has no knowledge of the transferor's purpose of defrauding creditors, and the transferee has simply held the asset, the appropriate order would be for the transfer of the asset to the transferor or to the creditors directly.

(c) However, if the transferee has changed his position on the basis of the receipt in a way that would make it unfair to him to repay the money, it would not be appropriate to require the transferee to pay back a sum equivalent to the amount he received.

In this regard, the Court exercises its discretion and engages in a balancing act in considering the remedies for transactions defrauding creditors (Section 438 of the IRDA); but not for transactions at an undervalue (Section 361 of the IRDA) or unfair preference transactions (Section 362 of the IRDA). This may be because Section 438 of the IRDA contemplates a single victim or limited victim cases, which makes it more likely to be possible to strike a balance between the victim of the transferor and an innocent transferee.

Conclusion

It would appear that transactions defrauding creditors are difficult to establish (requiring the subjective intention of fraud on creditors) and may not necessarily lead to the creditors' recovery if the monies pass through an innocent transferee and the innocent transferee changed his position. However, there remains value for section 438 of the IRDA as there is no time limit for its application as compared to statutory clawback provisions in transactions at an undervalue and unfair preference transactions.

Update on the sanction of an Administrative Convenience Class

In our February 2023 edition of the Going concerns, we briefly considered the pre-package scheme of arrangement applications ("**Prepack**") by the Zipmex group of companies (collectively "**Zipmex**") and covered Zipmex's application for approval for its proposed classification of its unsecured customers whose debt values were less than or equal to US$5,000 as a separate class of creditors (i.e. the "**Administrative Convenience Class**") in the Prepack. The Singapore High Court then did not make an order as it was not appropriate to do so at that stage but commented that it did not reject the concept of an Administrative Convenience Class.

The Singapore High Court heard the substantive Prepack applications and has now sanctioned the creation of an Administrative Convenience Class. We discuss further below.

Background facts

To recap the facts in the case briefly, Zipmex operates a cryptocurrency exchange platform which is accessed through an application known as the "Zipmex App" on which various cryptocurrencies are traded.

As part of its Prepack application, Zipmex sought to classify about 67,000 of its creditor customers whose withheld assets were below US$5,000 in value in a different class for purposes of the scheme of arrangement. This was to relieve Zipmex from the administrative burden of soliciting the consent of the 67,000 odd creditors for consent to the proposed scheme of arrangement.

The main question before the Singapore High Court was whether it had the jurisdiction to approve the creation of an Administrative Convenience Class in a Prepack.

Does the Singapore High Court have jurisdiction to approve the creation of an Administrative Convenience Class in a Prepack?

Zipmex referred to Section 1122(b) of the US Bankruptcy Code which permitted the US Courts to allow the creation of an Administrative Convenience Class where it was "*reasonable and necessary for administrative convenience*" as well as pre-Bankruptcy Code cases in the US for the principle that the payment of Administrative Convenience Class claims would benefit the debtor's estate and other creditors by streamlining administration of the estate.

The Singapore High Court found that the pre-Bankruptcy Code cases in the US was not applicable to the Singapore context but illustrated that some compromise of strict rights and equitableness is required for the sake of efficacy and feasibility. In particular, the Singapore High Court acknowledged that a poll of all 67,000 odd creditors would not be workable for Zipmex.

As regards compromising the strict rights and equitableness of creditors in the Administrative Convenience Class, the Singapore High Court stated that it is "*best catered for by some quid pro quo for the deemed consent to be taken from the Administrative Convenience Class, such as full payment*." Further, the Singapore High Court gave its nod of approval to Zipmex's mechanism to allow the creditors in the Administrative Convenience Class to still vote if they wanted to.

As for the jurisdictional basis for the approval of the creation of an Administrative Convenience Class in a Prepack, the Singapore High Court took a liberal reading of Section 71(1) of the Insolvency, Restructuring and Dissolution Act 2018 and Section 210(3AB) of the Companies Act 1967. The effect of which was that Zipmex did not have to show that a majority in number of the Administrative Convenience Class creditors would have voted in support of the scheme of arrangement and the Prepack could be sanctioned.

Conclusion

The approval to create an Administrative Convenience Class in a Prepack or a scheme of arrangement is a very useful tool when dealing with restructurings of large conglomerates with many retail creditors in many jurisdictions. This allows a win-win situation where the smaller retail creditors recover their monies in full, and the restructuring exercise can continue without being bogged down in an administrative nightmare.

Further, the decision demonstrates the Singapore Courts' recognition of the practical difficulties of difficult restructurings. In particular, the decision appears to have kept the requirements for the sanction of an Administrative Convenience Class deliberately loose and leaves it open to restructuring specialists to attempt further creative arguments.

The decision is a welcome addition to Singapore's jurisprudence and the Singapore Courts' willingness to be flexible and innovative when lending support to restructurings will help bolster Singapore's position as a restructuring hub.

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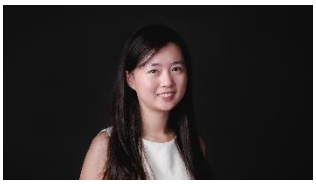

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