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## Scheme Of Arrangement: *The Top Builders Capital's Case*

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A Scheme of Arrangement (SOA) is one of the corporate rescue mechanisms. It is managed and controlled by a debtor company that essentially devises a proposal for the approval of its creditors for the fulfillment of its debt obligations. In the recent case of *Top Builders Capital Bhd & Ors v Seng Long Construction & Engineering Sdn Bhd & Ors* [2022] MLJU 1, the High Court granted the sanction order for the approval of the scheme of arrangement.

### Background Facts

Top Builders Capital Bhd, Ikhmas Jaya Sdn Bhd, Ikhmas Equipment Sdn Bhd (collectively known as the Applicants) are construction companies and required urgent debt restructuring and rescue. The Applicants then embarked on a scheme of arrangement.

On 31.12.2020, the High Court granted leave for the Applicants to summon a scheme meeting of the creditors of the Applicants or any class of them (Scheme Creditors). The High Court also granted a restraining order in favour of the Applicants, which through extensions, the restraining order was in place until 31.12.2021.

The Applicants sought sanction for the SOA (Sanction Application). A few creditors opposed the Sanction Application (Opposing Scheme Creditors) and raised various arguments against the same as set out below:

- a) Classification of the creditors was incorrect, where intercompany and/or related creditors should be separately classed or have their votes discounted down to zero.
- b) Insufficient and inadequate disclosure in the explanatory statement for the SOA.
- c) No audio or visual platform for conducting the Q&A session during the Virtual Meetings and a Scheme Creditor, Edwincom contended that the Applicants'

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appointed service provider had prevented Edwincom from attending the virtual meeting and deprived Edwincom of its right to attend and vote.

- d) Objections towards the acceptance of the late submissions of Proof of Debt (PODs) and extension of PODs deadline.
- e) The Scheme Creditors have a right to inspect other Scheme Creditors' PODs.

## General Principles For Sanction of Scheme

The Section 366 process under the Companies Act 2016 (CA 2016) (previously Section 176 of the Companies Act 1965 (CA 1965) is designed to save companies in difficulty. The process aims to assist the restructuring of a company heavily burdened with debts.

The key guiding principles applicable to sanction by our courts in a SOA are as follows:

- a) The statutory requirements set out in Section 366 of the CA 20 16 must have been complied with;
- b) The creditors must have been fairly represented in the court convened meeting and the majority of the creditors voting in favour of the scheme must have been acting bona fide; and
- c) The proposed SOA is such as intelligent and honest man, a member of the class concerned and acting in respect of his interest, might reasonably approve.

## Decision Of The High Court

The High Court granted the sanction order for the approval of the SOA and dealt with several significant legal issues for the SOA, which are discussed below:

### a) **Classification of Creditors**

The High Court confirmed that the test of classification of creditors in the SOA is based on similarity or dissimilarity of legal rights against the company and not on similarity or dissimilarity of interest not derived from

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such legal rights as seen in *Re Telewest and Re UDL Holdings Ltd & Ors* [2002] 1 HKC 172.

**b) Disclosure in a Scheme**

The Court held that the contents of the explanatory statement should be clear, sufficient, and not misleading. There is a need to make full disclosure. In any large or complex proposed scheme of arrangement, there is a need to be selective with the facts and confine it to the facts that are realistically useful for the creditors to make a reasonable judgment.

**c) Validity of Virtual Meetings**

Virtual Meetings were held during the onset of the Covid-19 pandemic which was unprecedented in this country and the world. Physical meetings were not possible and the holding of the Virtual Meetings was to adhere to the Full Movement Control Orders and the relevant standard operating procedures in place at that time.

The Scheme Creditors raised that unlike a physical meeting, questions that were posed had to be typed up and when answers were given to the questions, there was a lack of facility for an immediate follow up to the answers. Further, there was a lack of breakout rooms for participants to discuss among themselves before casting their votes.

The High Court held that the manner in which the Virtual Meetings were held did meet the requirement of a meeting. The Scheme Creditors were fully aware of the details and effects of the schemes and the consequence of the scheme if approved. The disadvantages raised regarding the conduct of the meeting were not such that would compel the Court to withhold the sanction of schemes.

**d) Extension of PODs Submission**

The Scheme Chairman could extend the deadlines for submitting PODs for the scheme. The Scheme Chairman had acted in good faith by trying to ensure that the relevant Scheme Creditors with legitimate

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claims against the Applicants would not be substantially prejudiced by submitting their PODs late and the High Court saw no prejudice to any of the unsecured creditors for allowing the extensions.

**e) Inspection of Other Scheme Creditors' PODs**

Some of the Opposing Scheme Creditors have raised the issue of the inspection of the PODs of other Unsecured Scheme Creditors. The Applicants' SOA has built a mechanism for the adjudication of the PODs of Unsecured Scheme Creditors who dispute the sums admitted by the Scheme Chairman. The decision-making process was carried out as per accepted scheme law and surpassed the requirement by allowing a mechanism of appeal. However, the Scheme Creditors did not provide any prima facie evidence of impropriety in the admission of PODs by the Scheme Chairman. Hence, they were not entitled to inspect other PODs.

**f) Discounting of Related Party Creditors' Votes**

The court held that whether the votes of intercompany creditors and/or related party creditors are to be discounted or disregarded is a matter of discretion for the High Court when considering whether or not to sanction the scheme based on the particular facts of the case.

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Authored by Josephine Chew, a pupil with the firm's Dispute Resolution practice.

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