THE LAW SOCIETY OF SINGAPORE

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Your Ref: To be advised

9 December 2013

Community Legal Services Divison,
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BY FAX (No. 6332 8842)
& POST

Dear Sirs

Feedback on Insolvency Law Review Committee's Report

We refer to your email dated 9 October 2013 inviting the Law Society to provide feedback on the Insolvency Law Review Committee ("ILRC") Report.

2 The consultation was referred to the Insolvency Practice Committee (the "Committee") and the wider bar. The views of the Committee are set out in Annex A for your consideration.

3 There were no comments from the wider bar.

4 The Council of the Law Society has considered the feedback provided and shares the views of the Committee.

5 We would be grateful for an update in due course.

Yours faithfully

Michelle Woodworth Cordeiro
Director, Representation & Law Reform Department

Encl.

Cc: Council Cc: Insolvency Practice Committtee

ANNEX A

VIEWS OF THE INSOLVENCY PRACTICE COMMITTEE

Chapter 2 – A NEW INSOLVENCY ACT

1 The Committee welcomes an Omnibus Insolvency Act for the reasons given by the ILRC.

2 The Committee agrees that the new Insolvency Act should address "individuals, companies and corporations" generally, and not deal with detailed provisions applicable to particular industries or types of business. Further, the new Act should also address Limited Liability Partnerships, which already shares many of the characteristics of company insolvency and partnerships, for which there are already provisions in the Bankruptcy Act ("BA").

3 The Committee is of the view that there is value in making provisions granting powers to enable the Minister (or other appropriate body) to make regulations to allow carve-outs or safe-harbour provisions either unconditionally or on terms from some or all of the provisions of the New Insolvency Act. In this regard, there are examples of provisions enabling grant of exemptions from certain consequences of bank and financial institutions insolvency. Hence, there exists section 76A of the Banking Act (which should be broad enough to seek exemptions from sections 48 to 55 of the Banking Act) and section 30AAZN(b) of the Monetary Authority of Singapore Act ("MAS Act"), where the Minister may make regulations providing that any arrangement is exempted from any provision of Part IVB of the MAS Act or that the Minister or the MAS shall not exercise any power under Part IVB of the MAS Act in relation to any arrangement. Regulations could also be made to direct the MAS not to exercise its powers under Section 41C of the MAS Act (under which the MAS may, by regulations, exempt any person or class of persons from all or any of the provisions of Part IVA of the MAS Act). In addition, there are specific legislations which provide specific carve-outs. For instance, section 130L of the Companies Act ("CA") and Division IV of Part III of Securities and Futures Act.

4 The Committee noted that in the context of derivatives, the MAS, in its response to the Consultation on Amendments to the MAS Act dated 5 February 2013 has stated its willingness to provide for bilateral netting arrangements and other similar arrangements not to be affected by the exercise of resolution powers under the MAS Act, which may be exercised for instance in the case of insolvency. Part of the reasons for doing so is to protect Singapore's standing as a good netting jurisdiction insofar as derivatives are concerned. To this end, amendments were made to the MAS Act to enable the MAS to grant exemptions by regulations. Although no regulations has been issued to date, the technique of providing exemptions or safe-harbours for certain transactions from the exercise of resolution powers is an example of how the laws relating to insolvency can be flexible enough to accommodate certain commercial transactions.

5 The need for provisions facilitating the possibility of granting exemptions takes added importance given that the reach and consequences of insolvency may be extended with the proposals of the ILRC. For example, to extend judicial management to foreign companies and for there to be an extended moratorium for schemes of arrangements.

6 There are various possibilities in relation to the use of exemptions. Some examples are set out below:

(a) In order to protect Singapore's standing as a good netting jurisdiction consideration should be given to provisions which clearly provides for the powers of disclaimers not to apply, to avoid undermining the "single agreement" principle of ISDA Master Agreements;

(b) For certain approved securitisations using Singapore as a base, consideration should be given to a possible exemption from the moratorium against enforcement of security provided by the Singaporean special purpose vehicle; or

(c) For receivables sales agreements, consideration should be given to a possible exemption from the consequences of non-registration if the agreement is re-characterised as secured lending.

7 These possibilities and others can be better catered for and explored if provisions are set out in the new Act, to enable the Minister to grant exemptions or provide safe harbours; where necessary on appropriate terms. Therefore, the Committeee suggests that suitable provisions be included in the proposed modern and new Act to enable exemptions to be granted by regulations.

8 With regards to paragraph 26 of Chapter 2 on the proposal for the rule against capitalisation and the statutory cap on interest, for the purpose of payment of dividend, to apply to the period of 3 years from the commencement of liquidation or bankruptcy, the Committee raised two points.

(a) First, there is a suggestion in the second sentence of paragraph 26 that the rule should also apply to judicial management. There is a question of whether judicial management stands differently, as there is possibility of saving or rehabilitating the company, and whether the same logic for capping interest in liquidation should apply to judicial management. In *Re Boonann Construction Pte Ltd [2000] 2 SLR(R) 399*, Boonann Construction Pte Ltd was granted credit facilities secured by a mortgage over the company's property by a bank. Interest payable on the facilities was also covered by the security. The company was placed under judicial management, and the judicial managers argued that: (a) based on rr 41, 44 and 50 of the Companies Regulations, the interest under the mortgage could only be computed up to the date of the judicial management order; and (b) as with the winding up of companies, the interest payable ceased to run as of the date of the judicial management order. The judicial managers also sought the court's sanction for the redemption of the mortgage. Justice Judith Prakash said (at paragraph 18), "Liquidation and judicial management are two entirely distinct regimes with distinct legal consequences. There is absolutely no logical reason why simply because interest ceases to run against the company in liquidation it should also cease to run against the company in judicial management."

(b) Second, a distinction is to be drawn between the time of commencement of winding up on one hand and the time of commencement of bankruptcy on the other. In the case of winding up, for instance, commencement could be the date of the making of the winding up application (see sections 255 and 291(6) of the CA). In contrast, the commencement date in the case of bankruptcy is the date of the bankruptcy order (See section 75 of the Bankruptcy Act ("BA")). For consistency, it would make sense to adopt the date of the making of the bankruptcy order, as that is the date in respect of which proofs of debts are to be in relation to. Since as a general rule, the rules in bankruptcy prevail over those in insolvent winding up (for which, see section 327(2) of the CA and section 4(1) of the Civil Law Act), the Committee is of the view that it would make sense to adopt the date of the winding up order or the passing of the resolution of winding up as the date in respect of which the rule against capitalisation and the cap on interest should be calculated upon.

Chapter 3 – BANKRUPTCY

9 The Committee referred to paragraph 19 of Chapter 3, namely ILRC's recommendation to incorporate the Debt Repayment Scheme ("DRS") d into the new Act with no major amendment. One of the issues that has arisen in relation to DRS is under section 65(7)(a) of the BA. Under the section, the court must, unless there are other disqualifying factors, refer the matter to the Official Assignee ("OA") for DRS where the debt(s) "in respect of which the bankruptcy application is made does not exceed S$100,000". In practice, this would mean that even if it is clear that the debtor has aggregate debts well in excess of S$100,000 (which would be a disqualifying factor for DRS under section 67(3)(a) of the BA), the matter must be referred for consideration for DRS by reason of the fact that the debts in respect of which the applicant makes the bankruptcy application does not exceed S$100,000. This in practice has often resulted in delays and additional costs. It is proposed that if it is clear that the total unsecured debts of the debtor exceeds S$100,000 (taking into account the debt the applicant relies upon to seek bankruptcy and any other known established debts), there should be no need to make the reference to consideration for DRS and the bankruptcy application can proceed.

10 At paragraph 54 of Chapter 3, the recommendation is to refrain from making any proposals for automatic discharge. The paragraph further speaks of further review and fine tuning of the current system. Notwithstanding the above, the Committee is of the view that a system which automatically discharges without regard to facts and circumstances would in any event be inappropriate. For example, where a bankrupt absconds, such a person should not have his or her bankruptcy automatically discharged.

11 The Committee is of the view that consideration should be given to cross border recognition of bankruptcy orders made by competent courts, section 43 of the Evidence Act alludes to the possibility. However, this should be expanded on and developed further not only in terms of recognition but also assistance.

Chapter 4 - RECEIVERSHIP

12 The Committee raised that there is a possible inconsistency between the priority conferred to certain preferential creditors under section 226(1) of the CA and section 328(5) of the CA. In the case of the former, the relevant preferential creditors have priority over "principal and interest" out of floating charge assets. This may mean in principle that the costs and expenses of the receivership prevails over the preferential creditors. In contrast, under section 328(5) of the CA, in the case of winding up, the relevant preferential creditors' preferential claims rank ahead of claims of the debenture holder (which may include the costs and expenses of the receiver) out of floating charge assets. It is established that receivership may survive winding up (*Harrick Engineering Pte Ltd* v *Singapore Finance Ltd* [1997] 2 SLR(R) 609). The Committee raised whether priority should be altered simply because a company goes into liquidation, particularly priority of the floating charge (as security holder). In the case of individual bankruptcy, section 76(3) of the BA recognises the basic position that the rights of secured creditor should (as least in general) not be altered by a bankruptcy order. Therefore, by comparison, the question is whether the mere fact of winding up should alter priorities. It is suggested that the priorities should be the same whether or not there is winding up.

Chapter 5 – THE LIQUIDATION REGIME

13 Please refer to paragraph 12 above.

Chapter 6 – JUDICIAL MANAGEMENT

14 While the suggestion of extending judicial management to foreign companies should be encouraged, the Committee is of the view that this should be balanced against the ability to introduce by regulations carve-outs or safe harbour provisions. Singapore may wish for certain foreign entities to use Singapore as a base or place of operations, and judicial management may possibly impede certain transactions and structures being used. For example, in a securitisation where there is security feature and security is provided by a foreign entity, the security may, with the proposals, be subjected to a moratorium and disposals by the judicial manager (if necessary, with court permission). This may not be facilitative of some securitisations in the sense that there is an additional impediment introduced which was never there and this may mean that there is an additional risk that needs to be priced.

15 With regard to recommendation 6.2, the Committee was of the view that a secured creditor who may appoint a receiver over the whole or substantially the whole of the company's assets should continue to have its absolute veto right (subject to public interest). It is unclear how the court can meaningfully weigh the prejudice that unsecured creditors may face in the event that a judicial management order is made against the prejudice that may be caused to such a secured creditor if a judicial management order is made in order to decide if the first type of prejudice is wholly disproportionate to the second type of prejudice.

16 In cases where such a secured creditor exercises its veto right, and the secured creditor intends to, through the receiver, dispose of all or substantially all the company's assets to pay itself off, the unsecured creditors will inevitably be adversely prejudiced. There is a risk that if the court is empowered to decide if the first type of prejudice is wholly disproportionate to the second type of prejudice, the importance of taking a floating charge will immediately be eroded. On the other hand, if the law continues to recognise that a lender who can appoint a receiver should be accorded precedence to (lowly) unsecured creditors, then the question of empowering the court to consider proportionality should, in the member's view, not arise. It is conceded that it will be a policy decision and weight should be given to the views of banks and other similar types of lenders on this issue.

17 If it is necessary to introduce some test, then it should not be based on a comparison between the rights of the secured creditor and the unsecured creditors. It should focus solely on the rights of the secured creditor, for example, a test along the lines of "more than adequately secured".

18 One member expressed concerns on the lack of clarity on the basis/legal requirements regarding the appointment of an *interim* judicial manager ("IJM") as local jurisprudence have not dealt with this issue in detail. The member is of the view that the new Act should take the opportunity to address this issue. This is particularly important since the Report proposes various amendments involving the expanded use of IJMs – i.e. in cases where the Company resolves to place itself under judicial management (see recommendation 6.5 and paragraph 29 of the Report under Chapter 6) and the proposal to allow any creditor of company to appoint IJMs (see recommendation 6.13(a) of the Report).

19 In this regard, the new Act should specify:-

(a) the threshold requirement for the appointment of IJMs – which should be that of "good *prima facie* case" as is the case for appointment of provisional liquidators; and

(b) the situation where IJMs should be appointed – i.e. to prevent dissipation of assets, etc. It appears that the Report already alludes to some of these reasons (see paragraph 57 of the Report). However, these should be specifically set out since there has been no judicial guidance on the matter as yet.

Chapter 7 – SCHEMES OF ARRANGEMENT

20 With the possibility of a wider moratorium, the Committee is of the view that the need for carve outs and exemptions by regulations takes added importance.

Chapter 8 – AVOIDANCE PROVISIONS

21 A defence along the lines of Regulation 6 of the Companies (Application of Bankruptcy Act) Regulations should be introduced to promote transactions entered into in good faith and so forth.

Chapter 10 – REGULATION OF INSOLVENCY PRACTITIONERS

22 Advocates and solicitors should continue in right to be appointed trustee in bankruptcy, as per section 34 of the Bankruptcy Act as there are no strong reasons to remove existing rights of advocates and solicitors.

23 There has been some debate in relation to the duties and standards involving insolvency office-holders and whether there should be a distinction drawn between them. For example, the difference between a court-appointed liquidator and a liquidator appointed in a voluntary winding-up (see *Re Pinkroccade Educational Services Pte Ltd [2002]* and *Korea Asset Management Corp* v *Daewoo Singapore Pte Ltd (In Liq) [2004].*

24 A member is of the opinion that this is an important issue because (as stated above) the Report now proposes a larger role of IJMs / Judicial Managers ("JM") who may be appointed out-of-court by the distressed company. If a distinction is drawn between court-appointed liquidators and liquidators in voluntary liquidation, there lies a question of whether the same distinction would be drawn in the case of IJMs.

25 As it is, the Singapore Court has already expressed reservations on the need to draw a distinction between different types of liquidators (see: Justice Rajah J (as he then was in *Korea Asset Management Corp* v *Daewoo Singapore Pte Ltd (In Liq)* [2004]. In the case of judicial management, this issue has not been (and arguably need not be) addressed since JMs and IJMs are currently only appointed by the Court.

26 However, with the expansion of the routes of commencement of judicial management, it will be important to make clear that the duties/standards of an out-of-court appointed IJM/JM are the same as Court appointed ones, given that the *raison d'etre* for the more expanded use of IJMs (for example) in out-of-court appointments is to give creditors more comfort that the distressed company's assets are preserved. This is the same reason/purpose for the appointment of a Court-appointed IJM and thus the duties/standards expected of an out-of-court appointed IJM should be no different.

Chapter 11 – CROSS-BORDER INSOLVENCY

27 The Committee is of the view that a wait-and-see approach should be adopted in relation to recognition and assistance of foreign bankruptcies; bearing in mind at all times

that there are existing common law principles in addition to sections 43 and 46 of the Evidence Act, which deal with cross-border recognition and assistance of foreign bankruptcy orders. Such a wait-and-see approach is consistent with the approach taken by the ILRC in the final sentence of paragraph 36 at page 238 of the ILRC Report.

28 In relation to paragraph 45(1) of Chapter 11, please refer to paragraph 14 above.