



Schemes of Arrangement

Given the current situation brought about by the coronavirus pandemic, the Malaysian economy has been badly affected with serious supply chain disruptions due to the nationwide lockdown. This has resulted in the tightening of companies' cash flows and has given rise to an urgent need for companies to implement rescue mechanisms and restructure their businesses.

One such mechanism under the Companies Act 2016 ("Act") is a scheme of compromise or arrangement under section 366 of the Act that permits compromises and arrangements with the creditors and/or members of the company. This section allows for a variety of arrangements that may be used to effect a reorganisation of a company or a corporate group, restructure debt or implement a plan for settlement of outstanding claims. This article will briefly explain the scheme mechanism and its advantages.

The Mechanism and Requirements for carrying out a scheme

1. A scheme under section 366 is initiated by an application to court for leave to convene a meeting of the company's creditors and/or members ("scheme meeting"). The court in granting leave will consider several preliminary issues including the correct classification of creditors¹, whether the proposed scheme meets the definition of a "compromise or arrangement" and whether the company is insolvent to the extent that even the "post-scheme" company would not be able to survive as a going concern². The company is further

¹ In determining whether creditors are properly classified within a class, the court will consider if the persons within the class have rights that are not so dissimilar as to make it impossible for them to consult together with a view to their common interest (Francis a/l Augustine Pereira v Dataran Mantin Sdn Bhd & 6 Others [2014] 1 CLJ 161).

² Ong Chee Kwan JC in Airasia X Bhd v BOC Aviation Ltd & Ors [2021] MLJU 189.

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required to present an outline of the scheme in the form of a draft explanatory statement to sufficiently justify the court granting leave to convene the scheme meeting³.

2. As comprehensive stand still or forbearance agreements with all creditors, in most cases, is impractical, a company will also apply for a restraining order to restrain legal suits, winding up petitions and enforcement proceedings. This may be normally granted by the court pursuant to section 368(2) of the Act for an initial period of not more than 3 months but may be extended for not more than 9 months.

Section 368(2) of the Act sets out the 4 requirements for granting a restraining order which are:

- that the court is satisfied there is a proposed scheme of compromise and arrangement between the company and its creditors or any class of creditors representing at least one half in value of all the creditors;
- that the court is satisfied the restraining order is necessary to formalise the scheme;
- that a statement of affairs of the company made up to 3 days before the application is lodged is filed together with the application for the restraining order; and
- the court approves or appoints as a director, the person nominated by the majority of the creditors in the application for the restraining order.

³ Re Kuala Lumpur Industries Bhd [1990] 2 MLJ 180

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3. Upon the court granting leave to convene a scheme meeting, the company must then ensure that the compromise or arrangement is agreed by a majority of at least 75% of the total value of the creditors or class of creditors or members or class of members present and voting at the scheme meeting. The aforementioned means that where there are separate classes of creditors and/or members, a majority of at least 75% of the total value of each class will be required to approve the Scheme. The following are the steps involved in obtaining approval of the scheme:

- Firstly, a timeline for when the scheme meeting must be held and when the members and/or creditors are to be notified must be set out;
- The time, date, venue, and chairperson of the scheme meeting has to be determined by the company;
- A notice to attend the scheme meeting and an explanatory statement⁴ must be provided to the members and/or creditors. Sufficient notice must be given to ensure all the members and creditors have a chance to attend. The explanatory statement serves to ensure those voting on the scheme have sufficient information to make an informed decision;
- During the scheme meeting, voting is typically carried out by poll and the rules applicable to proxy members and corporate representatives will apply; and
- For the proposed scheme to succeed at the scheme meeting, a majority of at least 75% of the total value of the creditors or class of creditors or members or class or members present and voting at the scheme meeting must approve the proposed scheme.

⁴ Section 369 Companies Act 2016

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4. The final step is to obtain the court's approval of the scheme. Case law⁵ tells us that the courts consider the following when determining whether to approve a proposed scheme:

- that the provisions of the Act have been complied with;
- that the class of creditors and/or members was fairly represented; and
- that the scheme is fair and reasonable that is to say, it is a scheme that an intelligent and honest person, being a member or creditor of the class may reasonably approve⁶.

Advantages of the scheme:

1. A scheme provides a **flexible mechanism** which may be used by ailing companies for restructuring by allowing the company to bring about a standstill while putting in place plans to turn the business around.
2. Upon approval a scheme **binds the parties** involved including any non-consenting creditors and/or members, the company and any liquidators.
3. Unanimous **approval** at the scheme meeting is not required.
4. It is available to companies who may be **unable to rely on other rescue mechanisms** under the Act.
5. The **restraining order** which restrains legal suits, winding up petitions and enforcement proceedings, allows the company to focus on implementing the scheme.

⁵ Re Sateras Resources (Malaysia) Bhd [2005] 6 CLJ 194 and Re Noble Group Limited [2018] EWHC 3092 (Ch) which included a fourth requirement that the court must consider in approving the scheme - whether there is any defect in the scheme.

⁶ Buckley on the Companies Act (13th edn, 1957), p. 409.

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6. The court may pursuant to section 370 of the Act make provisions for the transfer in whole or in part of the undertaking, property or liabilities of a company to facilitate a scheme for the reconstruction of the company. This avoids separate consensual arrangements that may be difficult to secure.

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