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Corporate Insolvency

## COVID-19: Interim “Immunity Booster” for Financially Distressed Companies

### Introduction

In fighting against our common enemy, COVID-19, the Government of Malaysia has implemented a Movement Control Order (“**MCO**”) commencing on 18 March 2020 and currently extended until 12 May 2020 (“**MCO Period**”).

It is inevitable that beyond the MCO Period, the global and domestic economies will continue to be severely impacted due to reduced socio-economic activities – with each passing day, many business entities are struggling to survive.

In this Update, we are specifically considering the practical and legal issues pertaining to the interim measures taken by the Government of Malaysia in an attempt to assist financially distressed companies from being wound up by the Court.

### Increase in Debt Threshold for the Issuance of a Statutory Demand from Above RM10,000 to Above RM50,000

The issuance of a statutory demand is an important step in the winding-up process. Prior to the events that are the subject of this Update, the clear position was that non-payment within 21 days of the receipt of a statutory demand resulted in the debtor company concerned being deemed to be unable to pay its debts.

With effect from 23 April 2020, the Minister of Domestic Trade and Consumer Affairs (the Minister charged with the responsibility for companies) issued a direction (“**Direction**”) pursuant to Section 466(1)(a) of the Companies Act 2016 (“**CA**”) prescribing the amount of the debt forming the basis of a statutory demand to be an amount exceeding RM50,000 (previously RM10,000), with the Direction being applicable for the period between 23 April 2020 and 31 December 2020 (“**Period**”).

The intended effect of the Direction is that during the Period, a creditor may only issue a statutory demand against a company for a debt which is more than RM50,000.

While the debt threshold during the Period is now five times more than the threshold previously prescribed by the Minister, it remains relatively low and may not have a significant impact in assisting

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many SMEs. This position should be contrasted with that of Singapore which also introduced a similar measure where the debt threshold was increased from SGD10,000 to SGD100,000 (a tenfold increase).

### **Increased Timeframe from 21 Days to 6 Months for Responding to a Statutory Demand**

The Minister has also exercised his power under Section 615(1) of the CA and gazetted the Companies (Exemption) (No. 2) Order 2020 (P.U. (A) 123) on 23.4.2020 (“**Exemption Order No. 2**”) which revoked and replaced the Companies (Exemption) Order 2020 (P.U. (A) 122).

Exemption Order No. 2 has the obvious intention to provide a lifeline to financially distressed companies by seeking to grant a 6-month period for a company to respond to a statutory demand.

#### **Impact of the Direction and Exemption Order No. 2**

The collective impact of the Direction read together with Exemption Order No. 2 is that a company will only be deemed to be unable to pay its debts under Section 466(1)(a) of the CA where the company neglects, for more than 6 months, to pay the debt demanded which has to be more than RM50,000.

The Period gives financially distressed companies some breathing space to resolve debt(s) following the receipt of statutory demand(s) including considering suitable corporate rescue mechanisms available under the CA such as a corporate voluntary arrangement or a scheme of arrangement. Further, a financially distressed company which has an aggregate debt of at least RM10 million with at least two financial institutions (amongst other criteria) may apply to the Credit Debt Restructuring Committee (“**CDRC**”) established by the Bank Negara Malaysia to attempt to arrive at a viable restructuring arrangement with the financial institutions concerned without resorting to legal proceedings.

### **Practical and Legal Issues with Exemption Order No. 2**

#### **Practical Issues**

While Exemption Order No. 2 may have the intention to provide financially distressed companies with some breathing space, it does not stop a creditor from seeking to wind up a financially distressed company by resorting to other provisions of the CA such as Section 465(1)(e) of the CA, read together with Sections 466(1)(b) or 466(1)(c) of the CA (for example where it can prove to the satisfaction of the Court that the company is indeed unable to pay its debts).

It is also pertinent to note that Exemption Order No. 2 does not bar a creditor from commencing legal proceedings, obtaining a judgment and thereafter seeking to enforce the judgment by attaching the available assets of the company concerned.

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### Legal Issues

The recourse of the Minister to issue Exemption Order No. 2 pursuant to Section 615 of the CA is debatable.

Section 615(1) of the CA only enables the Minister to exempt, amongst others, any corporation from all or any of the provisions of the CA. Under Exemption Order No. 2, not only has the Minister exempted all companies from Section 466(1)(a) of the CA, the Minister has also gone on to effectively provide that a company is only deemed to be unable to pay its debts if it neglects to make payment within a period of 6 months after the statutory demand is served.

The legal issues that arise from a reading of Exemption Order No. 2 are:

- (a) whether the Minister can on the one hand exempt Section 466(1)(a) of the CA and thereafter reimpose Section 466(1)(a) of the CA with some modifications (that is giving an extended 6-month timeframe to satisfy the debt demanded under the statutory demand); and
- (b) whether the Minister is effectively amending the requirements of Section 466(1)(a) of the CA (by substituting the original 21-day timeframe with the now extended 6-month timeframe), and therefore acting beyond the powers conferred on the Minister (which only confers a power of exemption).

### Concluding Words

In the light of the above legal issues, it is always possible that a creditor may take the stand that the original 21-day timeframe to comply with a statutory demand continues to apply and the creditor may proceed to issue a statutory demand requiring compliance within 21 days and, upon failure to do so, to proceed to file a winding-up petition against the debtor company.

In the event a creditor takes the above position, the debtor company may have no alternative but to seek the assistance of the Court to restrain the creditor from filing a winding-up petition after the expiry of the 21-day timeframe on the basis that a 6-month timeframe should be given. It is only at this juncture that the Court will have the opportunity to consider whether Exemption Order No. 2 has the effect that it is intended to have.

Visit our [COVID-19 Resource Centre](#) for views from our lawyers across the region on common issues and legal implications brought about by COVID-19. For specific inquiries, please reach out to your relationship partner or send an email to our [COVID-19 Legal Team](#).

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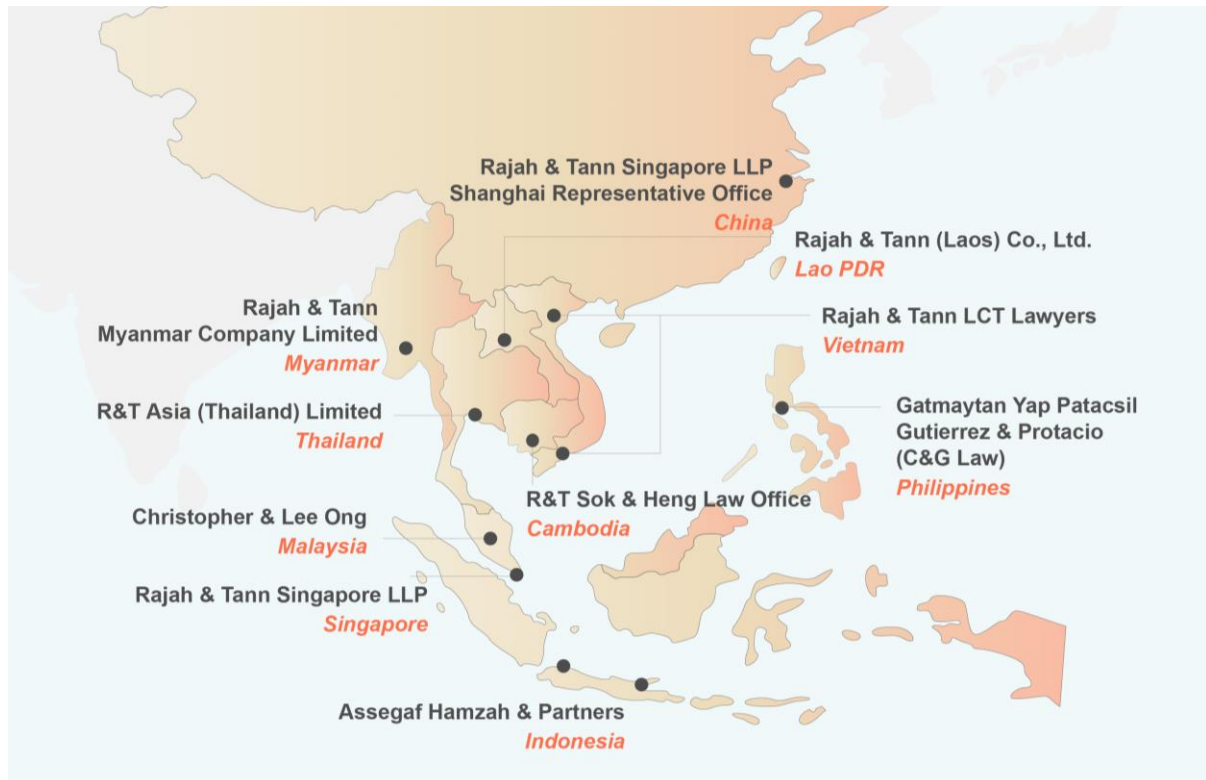
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