Re Boonann Construction Pte Ltd
[2000] SGHC 128

Case Number : OP 17/1999, SIC 601780/2000

Decision Date : 06 July 2000

Tribunal/Court : High Court

Coram : Judith Prakash J

Counsel Name(s) : Tan Tian Luh (Helen Yeo & Partners) for the Bank of Singapore; Nazim Khan and Chng Bee Peng (Colin Ng & Partners) for the applicants

Parties : —

Companies – Receiver and manager – Judicial management order – Redemption of mortgaged property – Whether interest on amounts secured by mortgage ceasing to run on date of judicial management order -- Whether proof of debt crystallises company's liabilities vis-a-vis its creditors – Whether principles of liquidation applicable to judicial management

Words and Phrases – 'Sums secured by the security' – s 227H(5) Companies Act (Cap 50, 1994 Ed)

: The summons-in-chambers which I had to consider was initiated by Mr Chan Ket Teck and Mr Chew Kia Ngee in their capacity as the judicial managers of Boonann Construction Pte Ltd (`the company`).

The company is the owner of the property known as No 19 Kaki Bukit Industrial Terrace, Singapore (`the property`). In May 1996, the Bank of Singapore (`the bank`) offered the company credit facilities of up to $2.7m on the security of, inter alia, an `All Monies Open Mortgage` over the property. This mortgage was duly executed and served as security to the bank for all credit facilities which it from time to time extended to the company.

The company was put under judicial management on 25 June 1999. At that time, the total sum owing to the bank by the company, inclusive of interest, was $2,265,452.23.

On 11 April 2000, the judicial managers filed this application by which they asked the court for the following orders:

> (1) a declaration that in respect of the intended redemption by the judicial managers of the property, the total sum owing to the bank by the company was $2,265,452.23 as at 25 June 1999 which included interest up to the date of judicial management order only;
>
> (2) that the redemption should operate as a full discharge and extinction of all sums owing to the bank by the company under all credit facilities provided by the bank to the company.

At the hearing before me which took place on 26 April, the judicial managers asked for a further order which was that the court sanction their intended redemption of the property from the mortgage.

The crux of the application was the judicial managers` contention that interest on the amounts secured by the mortgage had ceased to run on the date that the company had been placed under judicial management. I was not able to accept this argument which ran counter to all established principles on the rights of a secured creditor. It was not supported by case authority or by statute.

Accordingly, although I made an order sanctioning the redemption of the mortgage by the judicial managers, I specifically authorised the payment to the bank of all sums due and payable under the mortgage, inclusive of interest, up to the date of payment. Further, I dismissed the judicial managers` prayer for a declaration and ordered the company to pay the legal costs of the bank in connection with the application which I fixed at $800. Also I fixed the judicial managers` costs of the application

at $1,200 and provided that these should be paid out of the assets of the company. The judicial managers have appealed against all these orders except for the one relating to their own costs.

Judicial management regime

The judicial management regime was introduced into the law of Singapore via the enactment of the Companies (Amendment) Act 1987. As commentators have observed (see ***Company Law*** (2nd Ed) by Walter Woon and ***Judicial Management in Singapore*** by Choong and Rajah), the aim of the legislation was to introduce a breathing space for companies in financial difficulty. Under the pre-existing law, such companies could not prevent their creditors from appointing receivers or commencing winding-up proceedings. This meant that even companies which had substantial assets could be wound up because they were not liquid and could not pay their debts as they fell due. Under the new regime, once a judicial manager is appointed, there is a moratorium on enforcement action by creditors and this moratorium period is intended to be used to find a way to save the company without having to liquidate it. The judicial management situation is, however, not intended to be permanent. The initial order is made for a period of six months only and whilst this can be extended, the intention is that if the company cannot be saved within a reasonable time, the judicial management will end and creditors will be allowed to wind it up or take other action to enforce recovery of their debts.

The essential protection received by a company in judicial management is that civil proceedings may not be commenced against it, existing actions are stayed, execution processes may not be carried out and the company may not be wound up: see s 227D Companies Act (Cap 50, 1994 Ed) (`the Act`). Upon the judicial management order being made, the board of directors is deprived of its ability to run the company and its powers and functions are transferred to the judicial managers (s 227G). They are then entitled to do all such things as may be necessary for the management of the affairs, business and property of the company and to do all other such things as the court may by order sanction.

Among the powers granted to the judicial managers by the Act is the power to dispose of any property of the company which is subject to a security as if the property were not subject to the security. The relevant section is s 227H. In the case of property which is subject to a mortgage or a fixed charge (as is the case here), however, the judicial manager can only dispose of the same with the leave of court. Subsection (5) of s 227H specifically provides that it shall be a condition of an order made for the sale of such a property that the net proceeds of sale shall be applied towards `discharging the sums secured by the security` and where the net proceeds of the sale are less than the sums secured by the security, the holder of the security may prove on a winding up for any balance due to him.

It is notable that whilst the Act contemplates that there may be situations in which it would be in the interest of the company in judicial management that its property should be sold although the same is subject to a security, the Act is at pains to protect the interests of the secured creditor. It does this by providing for the net proceeds of sale to be paid to that creditor to discharge the company`s obligation to it in priority to any other application of the funds. The phrase used in the relevant subsection to refer to the company`s indebtedness to the secured creditor is, as pointed out above, `the sums secured by the security`. Practically the same expression appears in s 15(5) of the English Insolvency Act 1986 which gives an administrator of a company (the English equivalent of a judicial manager) a similar power to sell assets subject to a security. This phrase was commented on by Knox J in **Re ARV Aviation** [1988] BCC 708 at 713 in the following terms:

> *In my judgment, the expression `the sums secured by the security` covers not only the capital sum secured by the security but all interest properly payable thereunder and any costs which the proprietor of the security is entitled to add to his security in accordance with the general law and the terms of the instrument in question. Anything less than that would, it seems to me, be an interference which I would not lightly expect Parliament to wish to make with the rights of such a secured creditor.*

I entirely agree with his Lordship`s observations and consider that they apply equally to the expression as it appears in s 227H of the Act.

The Act does not specify the circumstances in which a mortgaged property belonging to a company under judicial management may be redeemed. The situation is covered generally by s 227G(6) which states that the judicial manager cannot make any payment towards discharging any debt to which the company was subject on the making of the judicial management order unless, inter alia, the making of the payment is authorised by the court. No guidance is given to the court by subsection as to when and on what terms the redemption should be permitted and the decision on giving the requisite sanction is left entirely in the discretion of the court. It is not a situation with which a court is often faced since companies under judicial management are rarely in a financial position to redeem properties which they have mortgaged as security for their indebtedness.

It appeared to me that in any event the secured creditor could not be placed in a worse position by the judicial manager`s application for sanction to redeem the security than it would be placed in by the judicial manager`s application for sanction to sell the property. That would have been exactly the result if I had accepted the judicial managers` proposition that for the purposes of redemption of the mortgage, the contractually agreed interest had ceased to accrue on the date of the judicial management order. It would be a startling result if a regime that was intended to afford a company a breathing space in which to re-organise its affairs could, despite the absence of any specific legislative provision to that effect, allow it to escape from the contractual obligation to pay interest embodied in a mortgage document. That would be an interference with the established rights of creditors that can only be accomplished by express legislative action. It should be noted that the judicial managers did not dispute that the mortgage instrument which the company had executed provided for the security so granted to the bank to cover all interest payable on the facilities extended by the bank.

Judicial managers` arguments

The judicial managers argued that based on rr 41, 44 and 50 of the Companies Regulations (Cap 50, Rg 1, 1990 Ed) (`the Regulations`) which deal with proof of debts in judicial management and by drawing an analogy in respect of payments under proof of debts for company in liquidation, a creditor is only entitled to compute interest up to the date of the judicial management order. They pointed out that under r 41, in a judicial management, every creditor was obliged to prove his debt. Such proof had, pursuant to r 44(1), to be in compliance with Form 77 in the Second Schedule to the Regulations. That form provides for the amount of the debt to be calculated as of the date of the commencement of the judicial management. The judicial managers contended that since Form 77 did not provide for proof of interest after the commencement of the judicial management, the bank was

not entitled to make any claim for interest accruing after that date.

I considered the above argument to be misconceived. It was muddling the creditor`s right to charge and recover interest with its right to be involved in the judicial management. As counsel for the bank submitted, the purpose of requiring each creditor to file a proof of debt in a judicial management is to enable the judicial manager to determine each creditor`s entitlement to participate in the scheme of judicial management and the value of voting rights in this participation. As Choong and Rajah state (at p 132):

> *The importance in lodging a proof cannot be overstated. The acceptance of the proof by the judicial manager is a condition precedent to a creditor`s participation in the scheme of judicial management. Only creditors whose claims have been accepted by the judicial manager may vote on whether to approve the judicial manager`s proposals.*

The proof of debt in a judicial management does not crystallise the liabilities of the company vis-.-vis its creditors for the purposes of repayment of debt unlike in a liquidation situation. The fact that Form 77 only calls for the calculation of interest up to the date of the judicial management order does not mean that interest on a secured debt would cease to accrue. What it means is that for the purposes of determining the amount of the secured creditors` debt and in turn his voting rights in the judicial management, an artificial line is drawn on the date of the order and indebtedness accruing after that date is not counted.

Next, the judicial managers relied on r 50 of the Regulations. This reads:

> *On any debt or sum, payable at a certain time or otherwise whereon interest is not reserved or agreed for, and which is overdue at the date of the judicial management order, the creditor may prove for interest at a rate not exceeding 6% per annum to that date from the time when the debt or sum was payable, if the debt or sum is payable by virtue of a written instrument at a certain time, and if payable otherwise, then from the time when a demand in writing has been made, giving notice that interest will be claimed from the date of the demand until the time of payment.*

They argued that if in a case where interest had not been agreed upon, interest would only be calculated up to the date of judicial management order then in a case, as here, where interest had been agreed upon, there would be no reason for such a debt to be treated differently and the interest to be calculated beyond the date of the judicial management order.

I could not accept the interpretation which the judicial managers gave to r 50. In my judgment, it has no effect at all on the period during which interest which had been the subject of a contractual agreement would continue to accrue. It appeared to me that r 50 was designed to allow creditors who had no previous contractual arrangements with the company on interest to include an interest component in their proofs in order to increase their voting rights. The rule embodies the recognition that if such creditors (usually trade creditors) were to start legal proceedings against the company and recover judgment for their debts they would, in all probability, be awarded interest by the court. These creditors had, however, been prohibited from taking such action by the passing of the judicial management order and thus the passing of the rule was, I considered, a way of putting these creditors, notionally, in the situation in which they would have been had the order not been made. It would also help such creditors have a greater say in the judicial management scheme vis-.-vis the

secured creditors with contractually agreed interest arrangements who would otherwise have greater voting rights simply by reason of the accrual of interest up to the date of the order even though the principal sum owing to them was equal or less than that owing to the trade creditor.

Whilst it is always possible for the legislature to abrogate contractual arrangements on interest, this must be done expressly. It cannot be done in the convoluted fashion which judicial managers put forward, ie that the effect of expressly giving people who are not contractually entitled to interest a right to prove for interest at a particular rate up to the date of the judicial management order, is implicitly to deprive people who have such contractual rights to interest from enjoying those rights after the date of the order.

The next argument put forward by the judicial managers relied on the fact that in the liquidation of a company, all interest would cease to run as of the date of the winding-up order. They submitted that the same rule should apply to the judicial management situation. I am afraid that I could not follow their argument on this point at all. 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. It is also not correct that interest ceases to run under all circumstances when the company is put into liquidation. A secured creditor is entitled to contractual interest up to the date of the liquidation of his security notwithstanding the prior winding up of the debtor company. See **Re Securitibank** [1980] 2 NZLR 714. It is only when the creditor is unsecured or wishes to surrender his security and prove in the liquidation as an unsecured creditor that he is subject to the limitations on interest provided by the liquidation regime.

Conclusion

I could not find a legal or a logical basis which justified the judicial managers` application to stop interest on the mortgage running from the date of their appointment. The judicial managers were the agents of the company (see s 227I(1)(a)) and their powers could not exceed that of their principal. Under the contract, the company could not redeem the mortgage except by paying all interest which had accrued up to the date of redemption. The judicial managers, as agents, could not be in a better position than their principal was. I was surprised by the application. I am astonished by their appeal. It is wrong to use the assets of a company which is already in financial difficulty to pursue unsustainable legal proceedings.

Outcome:

Order accordingly.