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COVID-19: RECESSION IS INEVITABLE. LET US, LAWYERS, BE YOUR IRON MAN. LET'S RESCUE YOUR COMPANY!

On 10 April 2020, the Government of Malaysia decided to extend the Movement Control Order (“**MCO**”) by another 14-days to 28 April 2020. This is the second extension to the MCO, which was originally imposed for a two-week period from 18 March 2020 to 31 March 2020, and was extended to 14 April 2020.[1]

Earlier, on 25 March 2020, Malaysian Institute of Economic Research (“**MIER**”) estimated that Malaysia’s real gross domestic product (“**GDP**”) may shrink by about 2.9% for 2020 compared to 2019. MIER further estimated that any additional two-week extension of MCO may amplify the contraction of real GDP by 3% to 4%, relatively to the 2020 baseline[2].

Kristalina Georgieva, the Managing Director of International Monetary Fund (“**IMF**”) stated that “*the outlook for global growth: for 2020 it is negative—a recession at least as bad as during the global financial crisis or worse.*”[3]

Many reputable economists have spoken on the potential recession, Paul Krugman stated “*...we’re going into the economic equivalent of a medically induced coma, in which some brain functions are temporarily shut down to give the patient a chance to heal.*”[4]

Joseph Stiglitz stated “*This is a different kind of crisis than normal crises. It’s just not a problem of aggregate demand.... Because of the disease, people are shutting down their businesses...More demand is not going to save that particular problem.*”[5]

Worrying? Of Course.

Recession is, as per the famous last word of Thanos[6] in the movie Avengers: End Game, inevitable.

Having said that, as we all know, the movie didn’t end there. Iron Man then said, “I am Iron Man” and snapped his fingers which save half population of the world[7].

This time around there will be no Iron Man, but let us lawyers save you! Let’s rescue your company. Let’s restructure!

Corporate Restructuring Mechanism under Companies Act 2016 (“**CA 2016**”) is an effective tool in facing the current tough economic environment. This is with a view of giving companies the opportunity to re-strategize, reorganise the management, ownership and operations as well as to make the necessary financial adjustment to cater to their assets and liabilities. This would help companies to survive in the long run.

Judicial Management

Companies facing the possibility of being insolvent may resort to this judicial management mechanism where they shall be managed by a judicial manager appointed by the Court.[8]

In order for the Court to make a judicial management order, the Court needs to be satisfied[9] that:

(a) The company is or will be unable to pay its debts; and

(b) The making of the order would be likely to ensure the survival of the company, the approval of a compromise or arrangement between the company and its creditors or members or a more advantageous realisation of the company's assets would be effected than on a winding up.

The filing of a judicial management application triggers an automatic moratorium[10] which allows company to restructure its debts. This moratorium is crucial as this will give you a lifeline.

The Court may then grant a judicial management order which shall remain in force for a term of six months; another six months may be extended on the application of the judicial manager[11].

However, a judicial management order shall not be made after a company has gone into liquidation.[12] The Court may also dismiss an application of a judicial management order if it is opposed by a secured creditor.[13] This could be a disadvantage for this rescue option.

Corporate Voluntary Agreements

A corporate voluntary arrangement (“**CVA**”) is where a company is allowed to present a proposal to its unsecured creditors under the supervision of an insolvency practitioner with minimal intervention from court.

The directors of a company may propose a CVA by submitting its proposal to the company and its creditors[14]. This may also be done by a judicial manager or a liquidator[15].

A nominee, who is an insolvency practitioner, appointed by the directors of the company, shall submit to the directors, a statement[16] –

(a) indicating whether or not, in his/her opinion, the proposed CVA has a reasonable prospect of being approved and implemented;

(b) whether the company is likely to have sufficient funds available for the company during the proposed moratorium to enable the company to carry on its business; and

(c) that the meetings of the company and its creditors should be summoned to consider the proposed voluntary arrangement.

Upon filing of all relevant documents, a moratorium automatically applies[17] and remains valid for 28 days where the nominee shall summon the meeting of the company and its creditors separately[18].

At the meeting of the company, only a simple majority is required to approve the CVA[19] whereas the required majority to approve the CVA in the creditors' meeting shall be 75% of the total value of creditors present and voting at the meeting either in person or by proxy[20]. Once approved, the proposal will then be binding on all the creditors of the company[21].

Scheme of Arrangement

Another useful rescue mechanism is the famous scheme of arrangement[22] that allows a company to propose an arrangement with its creditors. The arrangement shall be binding on the company, its members, its creditors and the liquidator if it is agreed by a majority of 75% of total value of creditors.[23]

Unlike in CVA and judicial management, there is no automatic moratorium for this scheme. For this purpose, the company may apply for an order to restrain further proceedings in any action or proceedings against the company ("**Restraining Order**") [24].

To enable this, the court must be satisfied that the Restraining Order is necessary to enable the company and its creditors to formalise the proposed scheme[25]. The court may grant a Restraining Order to a company for a period of not more than 3 months and the court may on the application of the company, extend this period for not more than 9 months if the Court is satisfied:

- (a) that the proposal is representing at least one-half in value of all the creditors;
- (b) that the restraining order is necessary to enable the arrangement to be formalised for the approval of the creditors or members;
- (c) a statement of affairs of the company made up to a date not more than three days before the application is lodged together with the application; and
- (d) the Court approves the person nominated by a majority of the creditors to act as a director.

Finally, the company will apply to court to sanction the scheme. Once approved, it will then be binding on all creditors.[26]

Conclusion

During this unprecedented crisis, a company should not hesitate to ride on the rescue mechanisms provided under CA 2016. Why close down when the Law allows you to rescue your company.

Remember, after the rain, comes the sun and hopefully the better days will be back again and your company will be back on track soon!

- 1 Perutusan Khas YAB Perdana Menteri, Prime Minister's Office of Malaysia <https://www.pmo.gov.my/2020/03/perutusan-khas-yab-perdana-menteri-25-mac-2020/>
- 2 Malaysia will face recession if partial lockdown extended, MIER warns <https://www.edgeprop.my/content/1665588/malaysia-will-face-recession-if-partial-lockdown-extended-mier-warns>
- 3 IMF Managing Director Kristalina Georgieva's Statement Following a G20 Ministerial Call on the Coronavirus Emergency <https://www.imf.org/en/News/Articles/2020/03/23/pr2098-imf-managing-director-statement-following-a-g20-ministerial-call-on-the-coronavirus-emergency>
- 4 The Covid-19 Slump Has Arrived <https://www.nytimes.com/2020/04/02/opinion/coronavirus-economy-stimulus.html>
- 5 The coronavirus outbreak is a 'different kind of crisis,' says Nobel laureate Joseph Stiglitz <https://www.cnbc.com/2020/03/17/joseph-stiglitz-coronavirus-outbreak-is-a-different-kind-of-crisis.html>
- 6 A fictional supervillain appearing in Marvel Cinematic Universe (MCU)
- 7 A scene in the box office movie Avengers: Endgame
- 8 Section 404 of CA 2016
- 9 Section 405(1) of CA 2016
- 10 Section 410 of CA 2016
- 11 Section 406(1) of CA 2016
- 12 Section 405(6) of CA 2016
- 13 Section 409 of CA 2016
- 14 Section 396(1) of CA 2016
- 15 Section 396(3) of CA 2016

- 16 Section 397(2) of CA 2016
- 17 Section 398(1) of CA 2016
- 18 Section 399 of CA 2016
- 19 Section 400(3) of CA 2016
- 20 Section 400(2) of CA 2016
- 21 Section 400(5) of CA 2016
- 22 Section 366 of CA 2016
- 23 Section 366(2) of CA 2016
- 24 Section 368 of CA 2016
- 25 Section 368(2) of CA 2016
- 26 Section 366(3) of CA 2016

Important Information

Azmi & Associates has set up Azmilaw Task Force to look into all issues arising from COVID-19 and MCO. Clients are welcomed to contact their usual Partner who will bring their issues to Azmilaw Task Force for our further action.

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