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CASE UPDATE: CREDITORS' DECISION IN LIQUIDATION GOVERNED BY MAJORITY IN VALUE?

In the High Court decision of ***Coca Cola Refreshments Malaysia Sdn Bhd v Leejin Capital Sdn Bhd*** [2021] MLJU 1700 by Nadzarin Wok Nordin JC, the Judicial Commissioner invalidated the appointment of the liquidator in a creditors' voluntary winding up.

The Court ordered for another liquidator candidate to be appointed instead, where that candidate was nominated by a creditor holding a majority in value of the debt of the company.

This decision may cause uncertainty for future creditors' voluntary winding up as well as other forms of winding up.

Summary of the Decision and Significance

This case concerned a creditors' voluntary winding up. A creditors' voluntary winding up is an out-of-court process and where the company is insolvent.

I first set out the process of the creditors' voluntary winding up and the relevant provisions.

Summary of the Creditors' Voluntary Winding Up Process

First, the directors sign and file the necessary statutory declaration to state that the company is unable to continue with its business due to its liabilities (section 440 of the Companies Act 2016 (CA 2016)). The directors will also appoint an interim liquidator. This interim period would, by default, last for 30 days pending the next steps to be taken.

Second, a meeting of the members of the company must be held within those 30 days (section 4401(1)(b) of the CA 2016). The members must pass the special resolution for the winding up of the company and the members shall also nominate their choice of liquidator. Often, the members will nominate the interim liquidator to continue as the liquidator.

Third, a meeting of the creditors of the company must be held within those 30 days (section 449(1) of the CA 2016). The creditors themselves do not decide or vote on whether the company should be wound up or not. However, the creditors are also able to nominate their choice of liquidator. The creditors' choice of liquidator will prevail over the members' choice. However, if no person is nominated by the creditors, the members' nomination shall be the liquidator (section 450(2) of the CA 2016).

The CA 2016 itself is silent on what is the voting threshold for the creditors to be able to vote for their liquidator candidate. For instance, would it be a majority in number, a majority in value, or a majority in number and value?

Rule 119 in the Companies (Winding-Up) Rules 1972 (Rules) sets out that at a meeting of creditors, a resolution is passed when a majority in number and value of the creditors present in the meeting vote in favour of the resolution. Rule 119 also falls within the section of the Rules titled '*General Meetings of Creditors and Contributories in Relation to Winding-Up by the Court and of Creditors in Relation to a Creditors' Voluntary Winding-Up*'.

Hence, Rule 119 applies to creditors' meetings in both a creditors' voluntary winding up and a court winding up.

Summary of the Decision

The company in question, Leejin Capital Sdn Bhd, undertook a creditors' voluntary winding up. The company only had two creditors.

At the members' meeting, the members nominated the first liquidator candidate. However, at the creditors' meeting, the creditor (with a majority in value of the debt) nominated a second liquidator candidate. But the creditors' resolution was not passed as the chairman of the meeting held that a majority in number and a majority in value was needed.

The creditor was aggrieved by this decision and made a court application. The High Court held that a majority in value was determinative for the purposes of the creditors' vote. The High Court applied a provision in the CA 2016 to override the requirement under Rule 119.

This decision will have to be read cautiously. This decision may have repercussions on creditors' resolutions at creditors' meetings in creditors' voluntary winding up as well as in court winding up situations.

Background Facts

The Plaintiff, Coca Cola Refreshments Malaysia Sdn Bhd (Coca Cola), is a creditor of the company, Leejin Capital Sdn Bhd (Company). Coca Cola was owed a debt of approximately RM1.4 million.

On 17 July 2020, the Company commenced a creditors' voluntary winding up and with an interim liquidator appointed. As part of the creditors' voluntary winding up, the members' meeting was held and where the members had resolved for the winding up of the Company. The members also nominated the first liquidator candidate to be the liquidator.

On 14 August 2020, the creditors' meeting was held. The creditors were informed that the Company's assets amounted to approximately RM135,000 and total liabilities were approximately RM2.4 million. The Company had only two creditors: Coca Cola and an individual, Tan Sri David Cheng (TSD). TSD was said to be a related party to the Company, and where TSD used to be a director and shareholder of the Company.

Coca Cola's proxy at the meeting nominated an alternative liquidator candidate to be the liquidator. The chairman of the meeting then asked for a seconder from the floor but there was none. The Company's lawyer at the meeting advised that there appeared to be a need for a proposer and seconder for the nomination, and there needed to be a majority in number and value for the motion to be considered. Coca Cola's legal adviser at the meeting took a different position. The adviser then stated that Coca Cola had a majority in value of the debts and Coca Cola's vote should carry through.

As a result of the stalemate, the chairman then made the decision that since there was no seconder for the nomination of the alternative liquidator put forward by Coca Cola, that proposal was not carried. Coca Cola's proxy at the meeting also stated that there was a concern over TSD as a creditor since there was a conflict of interest.

The minutes of the creditors' meeting recorded that Coca Cola had voted in favour of the alternative liquidator candidate while TSD had voted in favour of the first liquidator candidate. There was no majority in number and value by the creditors for the nomination to be considered.

Aggrieved by the decision at the creditors' meeting and with the appointment of the first liquidator candidate, Coca Cola filed a Court application in January 2021. The application was made under section 450 of the CA 2016 and for declarations. Coca Cola essentially sought a declaration that the first liquidator candidate appointment was invalid and that consequently, he be removed. The alternative liquidator candidate should then be appointed as liquidator of the Company or alternatively, as joint liquidator.

Decision

Majority in Value to Prevail

First, the Court considered the statutory provisions.

Section 450 of the CA 2016 sets out that in a creditors' voluntary winding up, there may be two different nominations. The creditors' nomination of the liquidator shall prevail. If no person is nominated by the creditors, the company's nomination shall be liquidator.

450. Liquidators in creditors' voluntary winding up.

(1) The company shall and the creditors may at their respective meetings nominate a person to be a liquidator for the purpose of winding up the affairs and distributing the assets of the company.

(2) If the creditors and the company nominate different persons, the person nominated by the creditors shall be liquidator and if no person is nominated by the creditors, the person nominated by the company shall be liquidator.

(3) Notwithstanding subsections (1) and (2), where different persons are nominated, any director, member or creditor may apply to the Court for an order directing that the person nominated as liquidator by the company shall be the liquidator or jointly with the person nominated by the creditors within seven days from the date on which the nominated as made by the creditors."

Next, the Court considered **section 521 of the CA 2016** on matters relating to the winding up of a company.

> *"521. Meetings to ascertain wishes of creditors or contributories*

> *(1) The Court may, as to all matters relating to the winding up of a company, have regard to the wishes of the creditors or contributories as proved to the Court by any sufficient evidence, and may if the Court thinks fit for the purpose of ascertaining those wishes direct meetings of the creditors or contributories to be called, held and conducted in such manner as the Court directs, and may appoint a person to act as chairperson of any such meeting and to report the result of the meeting to the Court.*
>
> *(2) In the case of creditors, regard shall be had to the value of each creditor's debt."*

Finally, **Rule 119** of the Rules:

> *"At a meeting of creditors or contributories a resolution shall be deemed to be passed when a majority in number and value of the creditors or, as the case may be, contributories present, personally or by proxy, and voting on the resolution, have voted in favour of the resolution, the value of the contributories being determined according to the number of votes conferred on each contributory by the regulations of the company."*

The Court applied the case of ***QB Khidmat Teguh Sdn Bhd v Pembinaan Legenda Unggul*** [2017] 8 MLJ 376 (***QB Khidmat***).

At [94] of ***QB Khidmat***, Mohd Nazlan JC (as he then was) commented that at the creditors' meeting "*the creditors will vote for the appointment of a liquidator, with the voting being based on the value of creditors' claims*."

Further, the Court also held that where there are only two creditors in a creditors' meeting, the application of Rule 119 must be read subject to section 521(2) of the CA 2016. Section 521(2) provided that "*regard shall be had to the value of each creditor's debt*."

The Court held in such a situation, section 521(2) of the CA 2016 shall prevail over Rule 119. The Rules do not provide for a situation where there can never be a majority in number voting due to the fact that the company only has two creditors in number. There will be an obvious impasse when the creditors are unable to agree with one another.

Other Findings against the Conduct of the Creditors' Meeting

The Court also made other findings.

First, the Court commented that TSD was not only a related party but also a creditor of the Company. This would lead the Court to the inescapable conclusion that TSD is an interested party in ensuring that the choice of the members of the Company, i.e. the first liquidator candidate, would be voted to be the liquidator of the Company.

Second, the Court held that there was no legal authority put forward that required a seconder in any meeting for a proposal to be carried through or to be voted upon. Even if such a requirement for a seconder does exist, based on the facts of this case, it would be unfair for the Company to insist on there being a seconder. Insisting on a seconder, when there were only two creditors, would deprive Coca Cola of its statutory and legal right under section 521(2) of the CA 2016 to have regard to the majority in value of its debt.

Third, the Court held that the first liquidator candidate was never nominated by any party at the creditors' meeting. His candidacy as liquidator was pushed through purely on the basis of the chairman putting his name to a vote and TSD voting on the same. The minutes of the creditors' meeting did not mention that a nomination was made at the creditors' meeting to nominate the first liquidator candidate as the liquidator.

With section 450 of the CA 2016 using the term "*nominate*", there must be a nomination at the creditors' meeting. With the absence of the first liquidator candidate being nominated by any party at the creditors meeting, the Court found that this was a further reason that the appointment was invalid.

Comments

I make a few observations on this decision.

First, when Coca Cola's application was filed against the Company, it is not clear whether permission had first been obtained to allow for the filing of such an action against the Company. Section 451(2) of the CA 2016 requires leave of the Court before any action or proceedings are commenced against the company after a company has commenced creditors' voluntary winding up.

Hence, like in the case of ***QB Khidmat***, the decision was on whether to grant leave against the wound-up company. The creditors had to apply for leave under the previous section 263(2) of the Companies Act 1965 to challenge the conduct of the creditors' meeting in the creditors' voluntary winding up. Without leave, the application would have been defective.

Second, the case of ***QB Khidmat*** did not comprehensively find that only a majority in value of the creditors can carry through the nomination of the liquidator. One of the issues in ***QB Khidmat*** was whether there was a need for a positive resolution to adjourn the creditors' meeting for the creditors to further consider the liquidator candidate. In reading ***QB Khidmat*** in its entirety, especially at [120] and [121], Mohd Nazlan JC (as he then was) was aware of the need under Rule 119 for there to be a majority in value and number of the creditors.

In that case, only five (out of 70 creditors) had objected to the adjournment and where these five creditors held a minority in value of the total debts. Hence, Mohd Nazlan JC (as he then was) held that "*the majority in value and number of the creditors at the meeting could rightly be said to have consented to the adjournment.*"

The English High Court case of ***In re Caston Cushioning Ltd*** [1955] 1 WLR 163 also held that where a resolution is not passed by a majority in value as well as in number, the creditors are deemed to have not nominated a liquidator. Therefore, the liquidator nominated by the company was the liquidator. That case applied the similar worded section 294 of the English Companies Act 1948 and Rule 134 of the English Companies (Winding Up) Rules 1949.

Third, on the issue of section 521(2) of the CA 2016 overriding the requirement in Rule 119, it may be that this finding is to be confined to the facts of this case with only two creditors. Rule 119 also applies to court winding up matters along with creditors' voluntary winding up. Hence, there may now be uncertainty if this case is more widely applied.

In my respectful view, there should always be the plain application of Rule 119 in the first place. As held by Justice Lee Swee Seng in ***QI-PMC Sdn Bhd v Asia Petroleum Hub Sdn Bhd*** [2012] 1 LNS 783: "*There is much wisdom for the twin requirements of both a majority in value of the debt and a majority in numbers to be met so that no one creditor may complain that it has not been heard and its interest not appreciated meaningfully*."

In essence, Rule 119 is a double-edged sword. It may very well frustrate a creditor holding a majority in value of the debt. At the same time, the rule gives minority creditors with small debts to have their say through the majority in number requirement. If there is a need to remove the majority in number rule, then an amendment to Rule 119 should first be made.

Fourth, in the context of creditors voting in any winding up, the winding up regime is silent on the issue of a related party creditor. Any creditor can file a proof of debt and can vote on its debt. There is no argument on whether that creditor is to be treated as a related party or not. This is unlike in a scheme of arrangement where there is a need to classify creditors based on different legal rights. And even in a scheme of arrangement, related party creditors with the same legal rights can still vote with other creditors.

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