# Re CEL Tractors Pte Ltd
# [2001] SGHC 72

**Case Number** : OS 600261/2001

**Decision Date** : 14 April 2001

**Tribunal/Court** : High Court

**Coram** : Kan Ting Chiu J

**Counsel Name(s)** : Vinodh Coomaraswamy and David Chan (Shook Lin & Bok) for the applicants; Tan Cheng Han and Tan Cheng Yew (Tan Cheng Yew & Partners) for Daewoo Singapore Pte Ltd

**Parties** : —

*Companies – Schemes of arrangement – Approval by the court – Whether scheme can discharge liabilities of guarantors of debtors – Position when one creditor objects to scheme – s 210 Companies Act (Cap 50, 1994 Ed)*

: The application before the court was made by CEL Tractors Pte Ltd (`the company`) to approve the scheme of arrangement under s 210 of the Companies Act (Cap 50, 1994 Ed).

Section 210(1) and (3) provide that:

> *(1) Where a compromise or arrangement is proposed between a company and its creditors or any class of them or between the company and its members or any class of them, the Court may, on the application in a summary way of the company or of any creditor or member of the company, or, in the case of a company being wound up, of the liquidator, order a meeting of the creditors or class of creditors or of the members of the company or class of members to be summoned in such manner as the Court directs.*

and

> *(3) If a majority in number representing three-fourths in value of the creditors or class of creditors or members or class of members present and voting either in person or by proxy at the meeting or the adjourned meeting agrees to any compromise or arrangement, the compromise or arrangement shall, if approved by order of the Court, be binding on all the creditors or class of creditors or on the members or class of members, as the case may be, and also on the company or, in the case of a company in the course of being wound up, on the liquidator and contributories of the company.*

The scheme had been considered at a meeting between the company and some of its creditors when it was accepted by a majority of 88.89% of the creditors (8 of 9 creditors) holding 95.62% of the debt ($16,328,825 of $17,076,274).

The sole objecting creditor was Daewoo Singapore Pte Ltd (`Daewoo`). Daewoo claimed against the company the sum of $747,449. Daewoo also had a claim against Lim Chee Seng, a director of the company under a guarantee he gave to Daewoo in connection with the company`s indebtedness to

Daewoo. All the other creditors also held guarantees for the debts owing to them.

Daewoo opposed the scheme because it would discharge the guarantee. Clause 4.3.1 of the scheme provides that

> *Upon the Company fulfilling its obligations under Clause 4.1.1.1 and Clause 4.1.1.2, (a) the Bank Creditors shall fully and completely discharge all and any of its rights under the Deed of Debenture and the Creditors` Mortgage, and save for Keppel TatLee Bank Limited, shall fully and completely release each and every Bank Guarantor from his obligations under any and each Bank Guarantee, and (b) Daewoo Singapore Pte Ltd shall fully and completely release the Daewoo Guarantor from his obligations under the Daewoo Guarantee.*

At the hearing counsel for Daewoo stated that his clients were not against the whole scheme, but they wanted it to be approved with a proviso that the arrangement shall not affect the Daewoo guarantee.

He submitted that a scheme cannot affect the rights of parties other than the creditors and the debtor company. He cited several Australian authorities in support of the proposition. The cases dealt with arrangements under s 181 of the Companies Act 1961 and other Australian provisions which are similar to s 210(1) and (3).

Most of the cases cited traced back to **Hill v Anderson Meat Industries** [1971] NSWLR 868. The brief facts of this case are that five subsidiaries of the defendant company (hereinafter referred to as `Anderson`) were affected by schemes of arrangement whereby their creditors discharged the subsidiaries from their debts in consideration of Anderson making a payment to the scheme trustee. There were no express provisions in the schemes which discharged the guarantees. Some of the subsidiaries` debts were guaranteed by Anderson. The plaintiff Mrs Hill was a creditor who voted against the scheme, and she contended that Anderson was liable to pay her under the guarantee.

The matter came on before Street J. The judge referred with approval to Dixon J`s pronouncement in **McDonald v Dennys Lascelles** [1933] 48 CLR 457that although as a general principle, the extinction of a principal obligation necessarily induces the extinction of the surety`s obligation, the principle does not extend to a discharge of the principal debtor`s personal liability by operation of law when the discharge is for the purpose of liquidating his affairs or transforming the rights of the creditor against him into rights against or in respect of his assets.

Street J went on to find for Mrs Hill on the basis that

> *Where ... a scheme of arrangement is propounded in connection with the affairs of an insolvent company, then the court`s approval under s. 181 will give to the scheme a statutory operation upon the relationship between the debtor company and its creditors, and so far as concerns a guarantor, in the absence of any special provision in the guarantee agreement, the guarantor`s liability subsists ...*

When the matter went on appeal ([1972] 2 NSWLR 704) the Court of Appeal affirmed it. Jacobs P and Hope JA in their judgments stated that the guarantee would remain in force even if Mrs Hill had voted in favour of the scheme.

In another case **Re Glendale Land Development** [1982] 7 ACLR 171, McLelland J came to a similar conclusion by another approach. He held that an arrangement cannot affect third party rights and liabilities because

> *(t)he only effect of approval by the court of an arrangement ... is to render the arrangement binding as between the creditors or relevant class thereof or members or relevant class thereof on the one hand, and the company (and if in the course of being wound up, the liquidator and contributories) on the other hand. A scheme of arrangement cannot thereby be rendered binding as between, eg, the members on the one hand and an outsider on the other. In **Isles v Daily Mail Newspaper** [1912] 14 CLR 193 at 204-5, Isaacs J made a similar point in an analogous context: "The only arrangements which it (ie the court) has jurisdiction to sanction are those between the debtor and the creditor; putting it shortly, none others are stated to be bound, and therefore there are no others with whom by force of the statute operating on the curial order, the minority can be brought into compulsory contractual relation."*

In England matters were in a similar position until the enactment of the Insolvency Act 1986. In **Re Garner`s Motors** [1937] Ch 594, the High Court considered a scheme of arrangement sanctioned under s 153 of the Companies Act 1929 (which is now s 425 of the Companies Act 1985, and is similar to s 181 and s 210). Garner`s Motors Ltd was in voluntary liquidation. Temple Press Ld claimed that Garner`s Motors was jointly and severally liable with Sentinel Waggon Works, Ld to pay it Â£379 5s. Garner`s Motor`s liquidators rejected Temple Press`s proof of debt on the ground that the company was discharged from its liability under a scheme of arrangement between Sentinel Waggon Works and its creditors whereby Sentinel`s liabilities were discharged.

Crossman J overruled the liquidators and explained that

> *It is settled law that accord and satisfaction between a creditor and one of several debtors, who are jointly and severally liable to the creditor, discharges the other debtors unless it appears from the terms of the agreement or the surrounding circumstances that the creditor intended to reserve his rights against them. The law is in my opinion correctly stated in **Halsbury`s Laws of England** (second edition), vol. 7, p. 237, para. 324. But in my judgment a discharge of one of several joint debtors by operation of law does not discharge the other debtors. In my judgment the effect of s. 153 of the Companies Act, 1929, is to give to a scheme when sanctioned by the Court under the section a statutory operation. The scheme when sanctioned by the Court becomes something quite different from a mere agreement signed by the parties. It becomes a statutory scheme. In my judgment, therefore, the discharge of Sentinel Waggon Works, Ld., from the debt to Temple Press, Ld., which was effected under clause 15 of the scheme sanctioned by the Court on March 23, 1936, did not have the effect of discharging Garner`s Motors, Ld., from its liability in respect of the debt.*

The Insolvency Act 1986 provides new and simplified procedures for voluntary arrangements for companies and individuals which do not require the approval of court. Section 5(2) which deals with arrangements of companies states that

> *The approved voluntary arrangement -*
>
> *(a) takes effect as if made by the company at the creditors` meeting, and*

*(b) binds every person who in accordance with the rules had notice of, and was entitled to vote at, that meeting (whether or not he was present or represented at the meeting) as if he were a party to the voluntary arrangement.*

and s 260(2) which relates to arrangements of individual persons states that

*The approved arrangement -*

*(a) takes effect as if made by the debtor at the meeting, and*

*(b) binds every person who in accordance with the rules had notice of, and was entitled to vote at, the meeting (whether or not he was present or represented at it) as if he were a party to the arrangement.*

The passage of the Insolvency Act did not bring an immediate change in the liabilities of third parties, as demonstrated in **RA Securities v Mercantile Credit Co** [1994] 2 BCLC 721[1995] 3 All ER 581. The plaintiffs in this case were landlords who granted a lease to the defendants. The lease was then assigned to a bank which in turn assigned it to another company. That company subsequently entered a voluntary arrangement under the Insolvency Act whereby it was to surrender the lease. The plaintiffs did not support the arrangement but were deemed to be bound by it under s 5(2). In fact the lease was not surrendered, and the plaintiffs sued the original lessees for pre-arrangement and post-arrangement rent.

Jacob J held that a voluntary company arrangement does not release a co-debtor. He stated ([1994] 2 BCLC 721 at 723; [1995] 3 All ER 581 at 584):

*I prefer to consider the matter as a question of principle first. The purpose of voluntary arrangements is to enable a company (or individual, for which case provision is made in Pt VIII) to come to a composition with creditors so that the more drastic step of liquidation or bankruptcy can be avoided, if possible. It is better to keep the show on the road than close it down even if creditors have to accept less than their nominal (but not achievable) entitlement. The whole scheme is not for the benefit of solvent parties who happen to owe debts also owed by the debtor. It would in my judgment be unfair if a solvent debtor escaped liability as a side-wind of the voluntary arrangement system.*

The judge was not persuaded that the plaintiffs were bound by the arrangement. He said ([1994] 2 BCLC 721 at 724; [1995] 3 All ER 581 at 585):

*Turning back to s 5, does `binds every person` have any effect outside the voluntary arrangement? I think not. The effect of the binding is solely as between the parties bound - those entitled to vote, whether they did or not. An outsider ... can get no assistance from the terms of the voluntary arrangement as such.*

He then went on to add ([1994] 2 BCLC 721 at 725-726; [1995] 3 All ER 581 at 586):

> *True it is that the landlords are bound by the voluntary arrangement. But they did not in fact voluntarily accept some other performance. There was no `accord` in truth - just a statutory binding. I do not regard failure to exercise the option to turn up at the creditors meeting and argue for some other arrangement as amounting to an `accord` - a true `acceptance`.*

and concluded ([1994] 2 BCLC 721 at 726; [1995] 3 All ER 581 at 587) that it is an error to turn a statutory binding into a consent.

A change came with the Court of Appeal`s decision in **Johnson v Davies** [1998] 2 BCLC 252[1998] 2 All ER 649. In this decision the court rejected the notion that in principle a voluntary arrangement made under the Insolvency Act cannot release a co-debtor or surety, and ruled that the effect of any arrangement should be determined by construing its terms - see the judgment of Chadwick LJ ([1998] 2 BCLC 252 at 270; [1998] 2 All ER 649 at 666).

Before coming to that conclusion, the learned judge reviewed the case law and the statutory provisions on voluntary arrangements.

Chadwick LJ referred to **Deanplan v Mahmoud** [1993] Ch 151[1992] 3 All ER 945 where Judge Paul Baker QC ruled that where one joint and several covenantor is released by accord and satisfaction, all are released. Chadwick LJ agreed with Judge Baker`s analysis that unless the co-covenantors are also released, they remain liable to the creditor, and when the creditor enforces its rights against them, they have a right of contribution or indemnity against the released covenantor. If this happened, the creditor would be committing a breach of the contract with the released covenantor because the latter would not be fully released from his liabilities inasmuch as he is still under a liability to contribute to or indemnify the co-covenantors.

The learned judge also referred to ***RA Securities*** (supra). The distinction Jacob J made between actual consent and the statutory binding did not find favour with him. He referred to s 260(2) and found ([1998] 2 BCLC 252 at 261; [1998] 2 All ER 649 at 658):

> *There is nothing in that subsection, or elsewhere, which saves a party who is bound `as if he were a party to the arrangement` from the consequences which would follow as a matter of law if he were indeed a party to the arrangement. The statutory hypothesis is that the person who has notice of and was entitled to vote at the meeting is party to an arrangement to which he has given his consent.*

Upon the completion of the review, Chadwick LJ concluded ([1998] 2 BCLC 252 at 270; [1998] 2 All ER 649 at 665) that fundamentally:

> *Whether or not to exclude co-debtors and sureties from the operation, under the general law, of the terms of a composition or arrangement between a debtor and his creditors is a matter of policy. There are, plainly, arguments of policy which point towards exclusion; in particular, that it is in the interest of the debtor and his other creditors that a creditor should not be dissuaded from voting in favour of a voluntary arrangement out of concern that he will lose his rights against co-debtors and sureties. But, equally, there are arguments which*

> *point towards allowing the general law to have effect; in particular, that it is in the interests of the debtor that he should be able to propose a scheme under which he will obtain a complete release from his liabilities, including the rights of contribution of co-debtors. It is also in the interests of other creditors, bound by the scheme, that it should not be frustrated by action by a co-debtor (not so bound) in enforcing rights of contribution.*

I agree fully with that view. I have the advantage of being able to consider the matter without being bound by any decisions on s 210 and its effect on schemes of arrangements and existing guarantees. I considered the Australian and English decisions referred to, and treated them as persuasive authority.

In my view s 210(3) should be given its plain meaning, ie that an approved arrangement binds all the creditors. It cannot matter that an objecting creditor has not consented to be bound because he is nevertheless bound by the operation of law. I do not see any reason why the arrangement has to have his support for the provision to take effect and for the arrangement to bind him.

I do not agree that an arrangement cannot discharge the liability of a party who is not a party to it. That view ignores the commercial framework of such arrangements. It is not unusual for the creditors of a company to hold guarantees from the major shareholders and directors of the company. It is not uncommon for these shareholders and directors to be the main players in seeking an arrangement with the creditors by offering their own assets in satisfaction of the debts owed by the company in return for the release of their guarantees. In such situation the creditors cannot be permitted to take the benefits offered by the arrangement and also retain the benefit of the guarantees.

The better policy is to allow the release of guarantors when that has been expressly provided for, than to refuse it. It should be remembered that a scheme of arrangement must have the support of the majority of the creditors and approved by court before it takes effect. After a scheme is accepted by the creditors, an objecting creditor can persuade the court to withhold its approval, or to approve it subject to such alternatives or conditions as it thinks fit (see s 210(4)). The objecting creditor would succeed if he can show that the creditors did not vote bona fide for the benefit of the creditors or the company as a whole (see **Re Wedgwood Coal and Iron Co** [1877] 6 Ch D 627), or that the scheme is not fair and reasonable (see **Re Dorman, Long & Co** [1934] Ch 635). I find it difficult to agree that as a matter of policy or principle an arrangement cannot be allowed to release guarantors, regardless of its terms.

Reverting to the present case, Daewoo`s objection was purely on a point of law. No argument was made that the other creditors had not voted in good faith, or that the scheme was unfair or unreasonable towards Daewoo. The case was simply that the Daewoo guarantee cannot be released because Daewoo had not agreed to it.

Daewoo failed to make out a case for the court`s approval to be withheld or that the approval be subject to the preservation of the guarantee. Consequently, the scheme was approved.

## Outcome:

Application allowed.