Leun Wah Electric Co (Pte) Ltd (in liquidation) v Sigma Cable Co (Pte) Ltd [2006] SGHC 86

Case Number : OS 415/2005

Decision Date : 23 May 2006

Tribunal/Court : High Court

Coram : Choo Han Teck J

Counsel Name(s) : Conrad Campos (Robert Wang & Woo LLC) for the plaintiff; Gan Kam Yuin and Mark Chee (Bih Li & Lee) for the defendant

Parties : Leun Wah Electric Co (Pte) Ltd (in liquidation) — Sigma Cable Co (Pte) Ltd

Contract – Consideration – Past consideration – Assignment in lieu of direct cash payment – Whether plaintiff's assignment of debt owed to third party to defendant made without consideration or for past consideration – Whether assignment made as partial payment for existing debts

Insolvency Law – Avoidance of transactions – Transactions at an undervalue – Whether plaintiff's assignment of debt owed to third party to defendant constituting transaction at an undervalue – Whether liquidator discharging burden of proving undervalue – Section 98 Bankruptcy Act (Cap 20, 2000 Rev Ed)

Insolvency Law – Avoidance of transactions – Unfair preferences – Whether plaintiff's assignment of debt owed to third party to defendant while plaintiff insolvent amounting to unfair preference – Whether assignment made with intent to prefer defendant over other creditors – Sections 99, 100(4) Bankruptcy Act (Cap 20, 2000 Rev Ed)

23 May 2006 *Judgment reserved.*

Choo Han Teck J:

1 The plaintiff, Leun Wah Electric Company Pte Ltd (in liquidation), was an electrical engineering company that was wound up by an order of court dated 20 August 2004. The effective date of the winding up was 2 October 2003 when a creditor called Cummins Power Generation (S) Pte Ltd filed the petition in Companies Winding Up No 244 of 2003. Mr Tam Chee Tong and Mr Wee Aik Guan of Deloitte & Touche were appointed the liquidators of the company. Prior to its liquidation the plaintiff was a nominated subcontractor of Kajima Overseas Asia Pte Ltd ("Kajima") in the construction of a wafer fabrication facility at Pasir Ris known as the "UMCi Base Project", which was a project of UMCi Pte Ltd. The defendant sold and supplied electrical cables to the plaintiff, some of which were for use in the UMCi project. Dr Foo Yung Kuan ("Dr Foo") and his brother ,Foo Jong Kuan, were the directors of the plaintiff. The UMCi Base Project had been completed and the maintenance period had also expired. The retention sum of US$236,892.24 held by Kajima became due and payable to the plaintiff in the ordinary course of events of the construction contracts. There were no problems in that regard. The dispute before me in this action arose from the claim made by the defendant that it was entitled to the retention money because the plaintiff had assigned the money to it. The liquidators disputed this claim and sought an order declaring that the assignment was void.

2 The defendant's case was as follows. It wrote to the plaintiff on 30 May 2003 demanding payment of money due on outstanding invoices amounting to $1,525,531.77. These were for the supply of electrical cables sold by the defendant to the plaintiff for various projects in which the plaintiff was engaged in, including the UMCi Base Project. The plaintiff claimed that the amount due under the UMCi Base Project was $953,814.51. The remaining $571,717.26 was due from other

projects. The plaintiff claimed that after the assignment the defendant continued to supply electrical cables to the plaintiff, but they were not for the UMCi Base Project.

3 Ms Gan, counsel for the defendant, challenged the basis for this presumption. The only document I had been referred to (DCB 24) showed that this debt was in respect of "UMCi", and since there were two UMCi projects ("Base" and "Hook-Up") I am inclined to accept that the reference was to both. The general reference of UMCi to both projects meant that the plaintiff's assertion, that after the assignment the defendant did not supply any more cables to the plaintiff, was untenable. That, in turn, raised important inferences of which I shall revert to shortly. By a letter dated 27 June 2003 which Dr Foo wrote on behalf of the plaintiff, the plaintiff gave notice of the assignment (of all the money due from Kajima to the plaintiff, estimated at the time to be US$340,000) ("the Notice") to the defendant. The contract of assignment itself was concluded on 26 June 2003 as dated and signed by the defendant on the Notice itself.

4 The liquidators say that all the supplies made by the defendant to the plaintiff after the assignment were paid on a cash-on-delivery basis. Kajima paid a sum of US$47,997.97 to the defendant pursuant to the assignment on 28 November 2003. After the court order of 20 August 2004 putting the plaintiff in liquidation, the liquidators wrote to Kajima (on 2 September 2004) questioning the validity of the assignment. The defendant also wrote to Kajima demanding payment under the assignment. Kajima, not surprisingly, applied by way of an interpleader summons and, consequently, obtained an order on 4 May 2005 to have the dispute resolved between the plaintiff and the defendant directly. The plaintiff's case rested on three grounds. First, the assignment was made without consideration, or was for past consideration, because it was made as a partial payment for existing debts. Second, the assignment was an unfair preference in favour of the defendant. Third, the assignment was a transaction at an undervalue.

5 On the consideration point, the liquidators pointed out that the plaintiff had proposed a scheme of arrangement with its creditors and sought their approval of the assignment, but the creditors rejected that proposal. Mr Conrad Campos, counsel for the liquidators, submitted that the documentary evidence showed that the plaintiff as well as the defendant had treated the UMCi Base Project debts as separate from debts due from other projects, and that the assignment covered only the UMCi Base Project. He further argued that there was no indication of the consideration coming in the form of a forbearance to sue. However, I do not think that this was a valid objection. The assignment was an assignment of a debt owed to a third party, Kajima. It was assigned in lieu of direct cash payment and that, in my view, was good consideration. It need not be adequate, so long as it was different. In any event, consideration moves from the promisee, which, in this case, was the plaintiff. It was not entitled to argue that its promise to pay by assignment of the money due to it from Kajima was not a good consideration to the defendant accepting that promise in discharge of part of the debt owed in respect of the UMCi Base Project.

6 The liquidators claimed that, in any event, the transaction was a transaction at an undervalue within the meaning of s 98 of the Bankruptcy Act (Cap 20, 2000 Rev Ed), and was therefore voidable on that account. Section 98 provides as follows:

> (1) Subject to this section and sections 100 and 102, where an individual is adjudged bankrupt and he has at the relevant time (as defined in section 100) entered into a transaction with any person at an undervalue, the Official Assignee may apply to the court for an order under this section.
>
> (2) The court shall, on such an application, make such order as it thinks fit for restoring the position to what it would have been if that individual had not entered into that transaction.

(3) For the purposes of this section and sections 100 and 102, an individual enters into a transaction with a person at an undervalue if —

(*a*) he makes a gift to that person or he otherwise enters into a transaction with that person on terms that provide for him to receive no consideration;

(*b*) he enters into a transaction with that person in consideration of marriage; or

(*c*) he enters into a transaction with that person for a consideration the value of which, in money or money's worth, is significantly less than the value, in money or money's worth, of the consideration provided by the individual.

I had addressed s 98(3)(*a*) in the preceding paragraph, and s 98(3)(*b*) was clearly irrelevant. It remained only for me to consider if s 98(3)(*c*) applied. The essence of the plaintiff's case on this point was that it believed that "given the financial difficulties of the plaintiff at the time, with liabilities exceeding assets, an equivalent antecedent debt would be worth far less than its face value in the plaintiff's winding up". There was no evidence that the assignment was given in discharge of a greater debt. It was given as part payment to keep the business between the plaintiff and defendant going. I am of the view that the chain of events and the documents bear this out. The plaintiff was short of funds at that time, but whether it was insolvent is a question I shall revert to shortly. It continued to require cables from the defendant who saw it to be in its interests to keep the plaintiff supplied so that the plaintiff could finish its projects. That was important because large amounts of money that would have been released to the plaintiff had been retained pending completion.

7 It is necessary to take reg 6 of the Companies (Application of Bankruptcy Act Provisions) Regulations (Cap 50, Rg 3, 1996 Rev Ed) into account only if the liquidators had discharged their burden of proving that the transaction was at an undervalue. I am of the view that that burden had not been discharged. Regulation 6 provides as follows:

The court shall not make an order referred to in section 98 of the Bankruptcy Act in respect of a transaction at an undervalue if it is satisfied —

(*a*) that the company which entered into the transaction did so in good faith and for the purpose of carrying on its business; and

(*b*) that at the time it did so there were reasonable grounds for believing that the transaction would benefit the company.

The evidence showed that the plaintiff and the defendant continued their business even after the assignment, and for the reasons above, the assignment appeared to me to be an exercise solely for the purpose of carrying on the plaintiff's (as well as the defendant's) business. In reviewing the evidence I did not see any indication of bad faith. Absence of bad faith may not mean that the defendant had satisfied the evidential burden of showing that the plaintiff acted in good faith, of course, but in the circumstances, I was of the view that the enquiry need go no further given that the transaction was not at an undervalue, and that there were no indications of bad faith such as to warrant a deeper study of the transaction.

8 Lastly, the liquidators attacked the assignment on the ground that it constituted an unfair preference within the meaning of s 99 of the Bankruptcy Act. That section provides as follows:

(1) Subject to this section and sections 100 and 102, where an individual is adjudged

bankrupt and he has, at the relevant time (as defined in section 100), given an unfair preference to any person, the Official Assignee may apply to the court for an order under this section.

(2) The court shall, on such an application, make such order as it thinks fit for restoring the position to what it would have been if that individual had not given that unfair preference.

(3) For the purposes of this section and sections 100 and 102, an individual gives an unfair preference to a person if —

(*a*) that person is one of the individual's creditors or a surety or guarantor for any of his debts or other liabilities; and

(*b*) the individual does anything or suffers anything to be done which (in either case) has the effect of putting that person into a position which, in the event of the individual's bankruptcy, will be better than the position he would have been in if that thing had not been done.

(4) The court shall not make an order under this section in respect of an unfair preference given to any person unless the individual who gave the preference was influenced in deciding to give it by a desire to produce in relation to that person the effect mentioned in subsection (3) (*b*).

(5) An individual who has given an unfair preference to a person who, at the time the unfair preference was given, was an associate of his (otherwise than by reason only of being his employee) shall be presumed, unless the contrary is shown, to have been influenced in deciding to give it by such a desire as is mentioned in subsection (4).

(6) The fact that something has been done in pursuance of the order of a court does not, without more, prevent the doing or suffering of that thing from constituting the giving of an unfair preference.

Section 100(4) of the Bankruptcy Act defines the term "insolvent" in two possible ways. The first, known as the "liquidity" test, simply requires proof that the person concerned be "unable to pay his debts as they fall due". The second, known as the "balance sheet" test, requires that "the value of his assets is less than the amount of his liabilities, taking into account his contingent and prospective liabilities". The liquidators do not deny that the management accounts of the plaintiff showed that its net assets exceeded its net liabilities. However, they pointed out that Ernst & Young, the plaintiff's auditors, had recommended that adjustments be made in respect of debts relating to two companies, known as Econ and Neo Corp respectively, and that had such adjustments been done, the plaintiff would have been insolvent under the "balance sheet" test. Ms Gan submitted that there was no necessity for such provisions as recommended. The basis of her remonstration was that the plaintiff's claims against Econ and Neo Corp would have been easily and incontrovertibly proved. That was a strong belief in a fact that may or may not be justified, but until the evidence regarding those claims have been fully tested, I would, on the balance of probabilities in this instance, accept the auditors' report and recommendation. In the present case, I was not persuaded by Ms Gan's arguments to find that the plaintiff's balance sheets ought not to make the provisions recommended by the auditors. In any event, I was of the view that the plaintiff also failed the "liquidity" test. The evidence showed that the plaintiff was pressed for payments at the material time from many quarters and had not been able to pay. It contracted to assign the Kajima debt because it was trying to stave off more serious action from the defendant who was an important supplier. I was satisfied that the plaintiff was insolvent at the time it assigned the Kajima debt to the defendant.

9 That, however, is not the end of the story because the liquidators must then persuade me that the assignment was made with a desire to prefer the defendant to the other creditors, that is, to put the defendant in a better position than the plaintiff's other creditors in the event of the plaintiff's winding up. There is no rigid definition as to what an unfair preference is, or how it might be made. Its principal concept is that there must be a desire, which, translated into conventional and practical usage, would mean "intention", to put the person who is given the preference in a position of advantage over that of other creditors in the event of liquidation or insolvency of the person giving that preference. Another aspect of this is that the preference must be made with the desire of improving the position of the person given the preference. In the present case, the defendant, in my view, knew that the plaintiff was in financial difficulties. It was also conscious that legal action might precipitate a total collapse of the plaintiff, and, in that event, it would have expected to stand in line with other creditors to share the inadequate assets of the plaintiff. The question was whether this was sufficient to show that the plaintiff's decision to assign the Kajima debt was influenced by its desire to give an unfair preference to the defendant.

10 It was thus necessary to examine the documents, especially the letters between the plaintiff and defendant, and those of Kajima. The fact most easily established was that the defendant was a big and long-time supplier of the plaintiff. It was difficult, however, to draw any conclusion as to how much genuine sweetness there was in that relationship. This was borne out by the ambiguity found in some of the letters. The defendant had stated, "our business relationship has always been pleasant and friendly" (letter of 30 May 2003), and "we have been so supportive of your company" (letter of 11 June 2003). However, in the same letter of 11 June 2003, the defendant had also threatened to hand the matter over to its solicitors if no payment was forthcoming. And in its letter of 30 May 2003, the defendant threatened to seek payment directly from the UMCi project owners, a move that would probably lower the plaintiff's standing in the owners' eyes. The plaintiff, in turn, wrote letters stating that it was doing its best to get payment from its debtors such as Kajima and Econ (*eg*, letter of 31 May 2003). Good business relationships often last only so long as payments are made. The parties' long relationship in this case appeared to be floundering by the end of May 2003 because the defendant was not receiving payment.

11 The defendant's letter of 11 June 2003 to the plaintiff concluded with this solemn note:

> Due to our past relationship, we have decided to give you till today 1730hrs to settle this problem. If till then we have not received any payment proposal letter, we will not hesitate in handing your case to our solicitor.

That extracted the plaintiff's reply of 16 June 2003 in which it stated:

> We agree to assign to you the balance of the amount due from Kajima Overseas Asia Pte Ltd to us for the UMCI Project, for the payment of amount due to your company for the same project.

On 27 July 2003 the plaintiff gave notice to Kajima that it was assigning the Kajima debt to the defendant; and on 29 July 2003, Kajima wrote to inform the defendant that the debt due to the plaintiff was US$234,500. Thereafter, the defendant continued trading with the plaintiff and invoices were issued up to 29 June 2004. It will be recalled that when the petition for winding up was filed on 2 October 2003, there were no ostensible indications that the plaintiff was insolvent although it could easily be surmised that it was not paying off some of its debts, such as those to the petitioner, Cummins. I do not have sufficient evidence to form the conclusion that the plaintiff had any desire to give an unfair preference to the defendant when it agreed to assign the Kajima debt. The history then and thereafter showed that the plaintiff was financially tight but was still a viable going concern. The plaintiff was dealt with the defendant's claim for payment in the way it did as the best option in the

circumstances. That is to say that it seemed to believe that the assignment would forestall drastic action by the defendant, and thereby gain time for the plaintiff to collect its own debts. The requirement in law that the assignor must have been influenced by a *desire* to give an unfair preference is an important one, because without that requirement, almost every payment to a creditor during the critical six months preceding a winding-up petition would, *ipso facto*, give rise to preference in favour of those creditors.

12 The desire of the company in this context would have to be reflected from the intentions of the persons who run the company. It was apparent from the submissions of Mr Campos, as well as Ms Gan, that Dr Foo was the principal person from the plaintiff in respect of the decision to assign the Kajima debt. Dr Foo was not called to testify by either party. Ms Gan, however, referred to various affidavits filed by Dr Foo in previous related proceedings such as the petition for winding up, and the plaintiff's application for approval on its proposed scheme of arrangement under s 210 of the Companies Act (Cap 50, 1994 Rev Ed). These affidavits were disclosed by the plaintiff. Mr Campos submitted that the defendant was not entitled to refer to them unless Dr Foo was called and be made available for cross-examination. Ms Gan pointed out that the plaintiff's counsel made a lengthy submission on the question of the plaintiff's desire to make an unfair preference, which submission relied on the state of mind of Dr Foo. I am of the view that the defendant was entitled to rely on the affidavits filed by Dr Foo, subject only to the question of the weight to be given to evidence not tested under cross-examination. In the present case, I was unable to form any opinion just from the affidavits of Dr Foo whether there was an intention to give the defendant an unfair preference by way of the assignment. The burden of proof lay with the plaintiff to show that that was his intention. Furthermore, Dr Foo was obliged to assist the liquidators in the matters concerning the plaintiff in liquidation, and he was, therefore, more a witness of the plaintiff than the defendant in any event. The plaintiff was, of course, not obliged to call Dr Foo or any witness if it did not think the evidence relevant. As it turned out, without evidence from Dr Foo that would support the plaintiff's case, the element of the plaintiff's desire, the burden of which lay with the plaintiff, was not proved in the present case. There was also insufficient evidence from the circumstances that required me to find that the evidential burden had shifted to the defendant. I am of the opinion that when the plaintiff made the assignment, it did so with the intention of paying off a debt that was, in its view, the most pressing at that time and, further, that it was in the plaintiff's commercial interests to do so. The assignment helped it to retain its principal supplier, and that, in turn, enabled it to carry on its projects and collect payment. I am thus reluctant to draw the conclusion that the intention of the plaintiff was to create an unfair preference *vis-à -vis* other creditors. It is not a matter of picking out any one event or situation and inferring from it the statutory requirement of a desire to unfairly prefer one creditor to another. In spite of its debts, the plaintiff seemed positive, at the time the assignment was made, that it was able to carry on its business. That was, at best, a misplaced optimism on the part of Dr Foo.

13 For the reasons above, I am of the opinion that the liquidators' claim failed.