Metalform Asia Pte Ltd v Holland Leedon Pte Ltd
[2007] SGCA 6

Case Number : CA 48/2006

Decision Date : 13 February 2007

Tribunal/Court : Court of Appeal

Coram : Andrew Ang J; Chan Sek Keong CJ; Andrew Phang Boon Leong JA

Counsel Name(s) : Chelva Retnam Rajah SC, Moiz Haider Sithawalla and Lavinia Rajah (Tan Rajah & Cheah) for the appellant; Davinder Singh SC, Adrian Tan, Valerie Tan, Angie Han and Vanita Jegathesan (Drew & Napier LLC) for the respondent

Parties : Metalform Asia Pte Ltd — Holland Leedon Pte Ltd

Companies – Winding up – Creditor of undisputed debt presenting winding-up petition against debtor company – Debtor company applying to court for injunction to restrain filing of winding-up petition – Whether debtor having bona fide cross-claim on substantial grounds which exceeding undisputed debt – Whether creditors having collateral purpose in presenting winding-up petition – Whether presentation of petition would cause irreparable harm to debtor company's ongoing business – Whether court should grant injunction restraining filing of winding-up petition

13 February 2007 Judgment reserved.

Chan Sek Keong CJ (delivering the judgment of the court):

Introduction

1 This appeal raises an important issue of practice as to when the court may restrain a creditor of an undisputed debt from presenting a winding-up petition against the debtor company.

2 The appellant, Metalform Asia Pte Ltd ("MA"), owes the respondent, Holland Leedon Pte Ltd ("HL") two sums of US$16,877,641.93 and S$112,677.17 (collectively, about S$25m and hereinafter collectively referred to as "the undisputed debt") for steel supplied by HL to MA between July 2004 and June 2005.

3 On 11 November 2005, HL served a statutory demand on MA under s 254(2)(*a*) of the Companies Act (Cap 50, 1994 Rev Ed) ("the Act") requiring payment of the undisputed debt by 3 December 2005.

4 On 2 December 2005, MA applied to court for an injunction to restrain HL from presenting a winding-up petition until MA's claim for about S$34m in damages against HL arising under a sale and purchase agreement dated 13 June 2004 ("the SPA") had been determined. MA's claim is based on HL's alleged breach of certain warranties under the SPA. On being served with the application, HL gave an undertaking not to present a winding-up petition pending the determination of the application.

Background

5 Prior to 2004, HL, then known as Metalform Pte Ltd, was carrying on the business, *inter alia*, of manufacturing metal covers for disk drives. HL was at all material times controlled by Anthony Ser and George Ser (collectively "the Sers"). Together they own 67% of the shares in HL. The other shareholders are related to the Sers. HL sold its business and assets to MA at the price of about

US$267m (or S$470m) on the terms and conditions set out in the SPA. The price was determined largely on the basis of HL's earnings before interest, tax, depreciation and amortisation ("EBITDA"), multiplied by a factor of seven, *ie*, EBITDA x 7.

6 MA is wholly-owned by Metalform International Ltd ("MI"), a company incorporated in Mauritius. MI is in turn a wholly-owned subsidiary of MPL(I) Ltd ("MPLI"), also a Mauritian company. MPLI is owned 51% by JPMP MPL Holdings Ltd ("JPMP MPL", which itself is owned by various funds managed by JP Morgan Partners) and 49% by Leedon Ltd ("Leedon", which is owned by the Sers). Both JPMP MPL and Leedon are also Mauritian companies. The corporate structure of the group was so designed to maximise tax efficiency. Through the group shareholding structure, the ultimate shareholders of MA are JPMP MPL (51%) and Leedon (49%). MA was at all material times the principal operating company in the group.

7 The purchase of HL's business and assets by MA was a leveraged buyout ("LBO"). The purchase price and the related transactional costs were raised in the following manner:

(a) US$152m by way of a loan from MI;

(b) US$6m by way of a cash injection from MI; and

(c) US$110m by way of a banking facility under a facilities agreement dated 28 June 2004 with DBS Bank Ltd.

8 The sums from MI referred to in [7](a) and [7](b) above came from a cash injection by MPLI into MI. The sources of MPLI's funds were JPMP MPL (around US$80m) and Leedon (around US$77m). It is apparent that the Sers sold HL's business and assets for US$267m and reinvested US$77m of the proceeds of sale in MPLI as a partner of JPMP MPL.

9 Apart from the SPA, there were several other agreements entered into between the parties, including a shareholders' agreement and service agreements, under which Anthony Ser and George Ser were appointed, respectively, the chairman of the board of directors and chief technical officer of MA. The appointments were terminated by mutual agreement on 3 May 2005, but the Sers remained directors of MA to this date. Under these agreements, the Sers, *inter alia*, covenanted not to set up a competing business within a specified period after the LBO. The agreements also gave JPMP MPL preferential rights in the event of the liquidation of MPLI.

How the undisputed debt arose

10 The bulk of the undisputed debt was incurred through the purchase of raw materials in the form of steel before and after the completion of the LBO in July 2004. According to Anurag Mathur ("AM"), a director of MA, HL agreed to sell steel to MA at a discount in order to offset the extra US$7m–US$8m that MA had allegedly overpaid for HL's business under the SPA. This sum arose because the purchase price payable by MA was determined by HL's EBITDA x 7 for the financial year ending 30 June 2004 and HL recorded higher than normal revenues and earnings in that financial year by arranging for one of its customers to pull greater than normal levels of product shipments in the last week of June 2004. HL's response to this allegation was that such practice was normal in the industry.

11 Thus, by a letter dated 27 July 2004, HL agreed to sell an initial stock of 5,000mt of steel at a discounted price of US$6.5m to MA, with a discount of almost US$6.5m, which according to AM, was close to the adjustment that had to be made for the excess price paid by MA under the SPA. AM

claimed that the parties had also agreed that this stock of 5,000mt of steel would form part of the assets sold by HL to MA under the SPA.

12 HL agreed to sell further stocks of steel to MA at either the prevailing market price or at its historical cost (whichever was lower). The sales were at a discounted price lower than the prevailing market rate as the steel, having been purchased by HL according to certain specifications, could not be sold in the open market but only to MA's competitors.

1 3 Although cl 5.7 of the SPA provided that the steel supplied by HL would be paid within 30 days of delivery, AM alleged that there was a clear understanding between MA and the Sers that MA would not have to pay HL for the purchases until its working capital position improved to a level when inventories on hand had been brought down and when the time taken to collect trade receivables from customers had been reduced. This was the reason why HL did not demand payment until May 2005, some ten months after the first delivery was made.

Attempts to settle the undisputed debt

14 Some months before HL served its statutory demand on 11 November 2005, MA had in March 2005 considered various ways to pay the undisputed debt. MA's projected cash flow then would not have been sufficient to pay the undisputed debt unless MA carried out two financial transactions, *viz*, the sale and leaseback transaction of MA's leasehold properties in order to reduce its bank debt by about US$28m–US$30m to US$81m–US$82m and the refinancing of the existing loan (collectively, "the refinancing proposals"). MA had during this period negotiated successfully with its bankers to refinance its loan upon the completion of the sale and leaseback transactions.

15 Sometime in May 2005, MA proposed to repay HL the undisputed debt by instalments up to January 2006. HL rejected this proposal on 11 May 2005 and demanded full payment by 31 May 2005. MA replied the next day with a specific proposal to pay the debt of US$17,412,601.21 in six instalments, beginning from July 2005 to December 2005, contingent upon the completion of the refinancing proposals.

16 MI approved the refinancing proposals at a board meeting held on 12 May 2005. However, on 21 June 2005, Anthony Ser wrote to MI to deny that any such resolution had been approved as he had not been asked to vote on it. By a separate letter sent on the same day, HL also rejected MA's offer to pay the undisputed debt in six instalments, and counter-proposed that it be paid in four equal instalments of US$4.25m each, and in default of any instalment, the whole of the balance would become payable immediately.

17 On 23 June 2005, JPMP MPL wrote to Leedon to explain the benefits of the refinancing proposals to the business of the Metalform group of companies, and their relevance to MA's proposal to pay the undisputed debt, *viz*, there would be a greater cushion in the financial covenants, lower interest rates, reduced debt amortisation pressure, higher capital expenditure allowances, and bigger working capital. In response to HL's proposal that the debt be paid in four instalments, JPMP MPL also explained that unless the refinancing proposals were effected, MA's cash flow projections would not even allow MA to pay the undisputed debt in the next six months, much less in the four months that HL had wanted.

18 On the same day, MA also wrote to HL proposing to repay the undisputed debt in six instalments as follows: (a) a first payment of US$2m on or before 1 July 2005; and (b) followed by five monthly payments of US$3.1m each at the end of each calendar month starting from 31 July 2005, up to and including November 2005 (and for the avoidance of doubt the monthly payment on

31 November 2005 would be US$3,114,663.13). MA reiterated that its proposal was contingent on the refinancing proposals being effected. As a gesture of good faith, MA paid US$2m to HL on 24 June 2005.

19 In a written reply on 28 June 2005, HL rejected MA's offer and demanded payment of the undisputed debt within seven days, failing which it would refer the matter to its solicitors. In the same letter, HL disputed the amount given by MA and stated that it would be taking steps to verify the amount, including certain deductions made by MA for sums which had allegedly been erroneously paid by two customers, *viz*, Seagate and Maxtor, to HL instead of MA.

20 On 5 July 2005, MA replied to HL's letter seeking an opportunity to meet to explain MA's current financial situation and the obstacles MA faced in effecting payment of the undisputed debt. As a further demonstration of its commitment to honour the repayment of the undisputed debt, MA also wished to discuss with HL the possibility of a parent company guarantee extended by a fund directly advised and managed by JP Morgan Partners Asia LDC. An MA directors' meeting was scheduled for 7 July 2005 to discuss MA's proposed repayment schedule for the undisputed debt and also the refinancing proposals.

21 On 6 July 2005, Anthony Ser wrote to MA saying that he would be unable to attend the meeting as he was away from Singapore. However, the other directors proceeded with the meeting on 7 July 2005, but could not make any decision in the light of Anthony Ser's objections to the proposed transactions. On 8 July 2005, MI also held a directors' meeting at which MA directors were also present. MI also postponed its decision on the proposed transactions.

22 On 13 July 2005, at a meeting of MI's directors, MA provided a detailed response to the issues raised by Anthony Ser in his letter of 6 July 2005, *viz*, the necessity of refinancing the bank loan, the extent of the problems faced by MA and whether there were any other alternatives or solutions to MA's financial problems, and the need for a careful evaluation of the proposed sale and leaseback transactions and the alternatives, if any. MA explained that the refinancing proposals were necessary to ensure that MA would not breach one of its financial covenants (the ratio of senior debt to EBITDA) for the quarter ending 30 June 2005 on account of the financial under-performance and lower than expected EBITDA for FY2005. According to MA's calculations, MI's shareholders would have to inject curative equity of up to US$23.4m to cure the projected breaches in the senior debt:EBITDA ratio for the next three quarters if the current bank loan was not refinanced. In addition, refinancing would provide other benefits such as a greater cushion in the financial covenants, reduced interest rates, a reduction in the repayment pressure on MA, allow for an expansion in the working capital facility to MA and an increase in the annual capital expenditure limit.

23 On the sale and leaseback proposal, MA explained that it was integral to the refinancing of the bank loan as DBS Bank Ltd was only willing to lend up to US$79m to refinance MA's existing loan of US$97m, leaving a deficit of US$18m. It was also explained that two alternatives were available to MA to bridge this deficit: (a) MA's shareholders could inject an additional US$18m in fresh equity; or (b) MA could enter into a sale and leaseback transaction of its Singapore properties. Although the annual rental of the properties was US$1.4m for a 12-year leaseback period, MA was of the view that the transaction would still be in the best interests of MA and its shareholders as the current interest rate on the term loan of 6.3% per annum meant that MA would have to pay approximately US$6.1m annually in interest.

24 On 22 July 2005, MA received a letter from HL's solicitors demanding payment of US$18,614,288.90 within seven days. On 29 July 2005, MA replied, disputing the amount demanded by HL, and stating that the undisputed debt was then US$15,514,663.13.

25 An MA directors' meeting fixed for 29 July 2005 could not be convened due to a lack of a quorum in the absence of the Sers. At the adjourned meeting held on 8 August 2005, Anthony Ser informed the other directors that he needed to appoint a financial advisor to assist Leedon in deciding whether or not to support the refinancing proposals.

26 In the light of the Sers' continued refusal to agree to the refinancing proposals, MA began to consider alternative ways to restructure its finances. JP Morgan Partners proposed a rights issue offer ("Rights Issue") at the MPLI level to its existing shareholders, *ie*, JPMP MPL and Leedon were to raise curative equity of US$18m (which amount would have been raised under the refinancing proposals) in the form of ordinary and preference shares, and JPMP MPL and Leedon were expected to subscribe for both types of shares in proportion to their shareholdings in MPLI. JPMP MPL subscribed for both types of shares (valued at about US$9m), but Leedon subscribed for only the ordinary shares (at the total price of US$87,326.73).

27 Because of Leedon's partial subscription, JPMP MPL refused to take up the preference shares on the ground that Leedon's partial subscription was invalid in that a shareholder was not permitted to take up just one class of shares without the other, and that Leedon's action totally frustrated the sole purpose of the Rights Issue to raise curative equity of US$18m to avoid breaching MPLI's financial covenants under its term loan. In these proceedings, Anthony Ser has alleged, in his affidavit filed on 13 January 2006, that JPMP MPL's refusal to pay for the preference shares demonstrated its lack of confidence in MA's future performance. This allegation was unfounded because in spite of the failure of the Sers to take up their shares in full, JPMP MPL had taken steps to raise from CITIC-Ka Wah Bank a US$18m loan for MPLI, to be "fed" down to MA. This loan was secured by a guarantee extended by the investment funds controlling JPMP MPL. It would appear that the Sers have been given a free ride on this loan.

28 In the meantime, MA received an email on 15 August 2005 from the Sers alleging that the management presentation of MA's accounts for the financial year 2005 was inaccurate and that they would be appointing auditors to examine MA's financial records. The Sers also confirmed that they would not agree with the refinancing proposals or the Rights Issue until their auditors, Deloitte & Touche ("D&T"), had completed their review of MA's accounts and other records. An audit was done by D&T in late August 2005 up to October 2005. We should add that in relation to this audit HL has not referred to it in the present proceedings. It would therefore be reasonable to infer that the audit did not support the Sers' allegation of inaccuracy in relation to the management presentation done by MA for the financial year 2005.

29 According to MA's chief financial officer, Rainer Gumpert ("RG"), and AM, the Sers were again asked at a board meeting of MPLI held on 7 November 2005 if they would agree to the refinancing proposals. George Ser's response was that if MPLI were to send a formal letter to Leedon, it would respond within 24 hours. MPLI sent the letter on the same day and Leedon, as promised, replied on 8 November by e-mail. In its reply, Leedon reiterated its refusal to agree to the sale and leaseback and the refinancing proposals, *unless* JPMP MPL agreed to release the Sers from various restrictions and covenants which they had agreed to with JPMP MPL in connection with the LBO and to release/vary the restrictions on Leedon and its shares in MPLI.

30 JPMP MPL rejected Leedon's demands, following which on 11 November 2005, HL served a statutory demand under s 254(2)(*a*) of the Act on MA, resulting in the present proceedings.

How the cross-claim arose

31 The management of the business of HL before and after the SPA was signed was under the

control of the Sers. It was only in early May 2005 that their services were terminated by mutual agreement between the parties. In early March 2005, William Merrell Fulton ("WF") was appointed the chief executive officer, but he reported to Anthony Ser as chairman of the board of directors. MA has claimed that it was soon after WF's appointment that it was alerted to possible non-compliance by HL with certain contracts, licences and permits that could amount to breaches of warranties by HL under the SPA. AM has claimed that in May 2005, at a meeting of the MA directors, he had raised the breaches of warranties by HL. These breaches are set out in paras 25 to 30 of the first affidavit of RG and may be summarised as follows:

(a) failure to follow product management processes ("PMP");

(b) failure to monitor manufacturing processes to meet specifications;

(c) failure to carry out the destructive testing of products;

(d) generating false test results to give the impression of the monitoring, extent and results of product testing;

(e) using non-approved subcontractors and vendors to supply goods and services at lower prices than customer-approved subcontractors and vendors to increase profits; and

(f) failure to comply with environmental and safety laws and permits.

32 In July 2005, MA began a more detailed investigation into the extent of breaches of warranties. On 6 September 2005, MA engaged Ernst & Young ("EY") to examine the heads of claims and quantify the damages MA had suffered by reason of HL's breach of warranties. These damages included the cost of rectifying the breaches and the effect some of the breaches had on the EBITDA used to calculate the purchase price of the business and assets of HL. EY completed its report on 27 September 2005. In it, EY quantified the total damages to be S$34,472.740 under 12 categories as follows:

(1) Building regularisation

(2) Environmental, Health & Safety Compliance

(3) State of equipment and facilities

(4) Unusable equipment

(5) Equipment and computer systems to meet and monitor specifications in PMP requirements

(6) Additional cost of destructive test to meet PMP requirements

(7) Leak testers, conveyor system and jumpsuit bags and labour-customer specs

(8) Production labour hour and loss of output during customer audit

(9) Use of non-approved sub-contractors

(10) Use of non-approved vendors

(11) Additional workers in QA department

(12) Claim under ERM Report (capped at S$50,000).

In calculating the damages under categories (2), (6), (9), (10) and (11), EY applied a multiple of seven on the basis that if HL had complied with its obligations and duties under these categories, the EBITDA on which the purchase price had been calculated would have been correspondingly lower.

33 MA sent EY's report to HL on 28 September 2005 together with the summary prepared by EY on MA's claims for breaches of warranties. MA notified HL that it intended to use the S$25m, including all accrued interest thereon, in the escrow account set up under the SPA to settle part of the claim.

34 On 18 October 2005, HL's solicitors replied rejecting MA's claims, and on 11 November 2005, HL's other solicitors served a statutory demand on MA to pay the undisputed debt within 21 days, failing which HL would be entitled to wind up MA. A second notice dated 30 November 2005 was sent to MA asking whether MA had appointed solicitors to accept service of the winding-up petition. This demand triggered these proceedings.

Proceedings in the High Court

35 In the court below, MA relied on three grounds in support of its application for an injunction to restrain HL from filing a winding-up petition against MA, as follows:

(a) that MA had a *bona fide* cross-claim of S$34m on substantial grounds which exceeded the undisputed debt of S$25m;

(b) that HL (*ie*, the Sers) had a collateral purpose in presenting the winding-up petition; and

(c) that the presentation of the petition would cause irreparable harm to MA which has an ongoing business.

36 In relation to ground (a) above, the trial judge held that in a case where the company has a *bona fide* cross-claim based on substantial grounds which is equal to or exceeds the creditor's undisputed debt, the court has a discretion whether or not to restrain the creditor from presenting a winding-up petition against the company, citing *Re Sanpete Builders (S) Pte Ltd* [1989] SLR 164 ("*Sanpete*") and *In re Bayoil SA* [1999] 1 WLR 147 ("*Bayoil*").

37 In relation to whether the cross-claim was *bona fide*, the trial judge held that, although MA had only raised its cross-claim in September 2005, there was evidence to show that MA had looked into various possible breaches of covenants by HL some months before that date, and that accordingly, he could not conclude that the cross-claim was not *bona fide*.

38 In relation to whether the cross-claim was based on substantial grounds, the judge rejected HL's argument that MA's cross-claim was unsustainable because it was based on estimates and not on the actual costs of steps taken to rectify the breaches. However, he agreed with counsel for HL that because MA's alleged claim for breach of warranties totalling S$34m was secured to the extent of S$25m and if that amount was taken into account, the net amount of the cross-claim would fall far short of the undisputed debt of S$25m. Although counsel for MA offered to release to HL an amount from the escrow account sufficient to equalise the cross-claim and the undisputed debt, the judge held that such release was not permitted because (a) MA had agreed to look to the escrow account to meet its claims under the warranties; and (b) MA could not unilaterally vary the terms of the SPA

and effectively seek to substitute the security it had for the counterclaim. The judge held that this ground was sufficient to dismiss MA's application for an injunction.

39 In relation to EY's computation of MA's cross-claim at S$34m, the trial judge did not rule on the submission made by counsel for HL that EY's computation was legally wrong on the ground it had applied a multiplier of seven for the majority of MA's claims that were categorised as of a recurrent nature. But for this method of computation, the cross-claim would not exceed S$10m. Instead, the trial judge held that MA's cross-claim could not be made out, as a matter of law, since MA had not made any claim for breach of warranty under Sched 4, cl 3.1 of the SPA, which warranted that the accounts of HL reflected a true and fair view of its assets, liabilities and state of affairs and of its profits and losses. The trial judge also commented that unless MA sought to set aside or challenge the EBITDA in the arbitration proceedings, it would not be sufficient for MA to show that other breaches would in turn affect the profit and loss of HL at the material time and that this would affect EBITDA. The trial judge however cautioned that nothing he had said would bind the arbitrator who would be determining the validity of the cross-claim.

40 In relation to [35](b) above, the trial judge concluded that the Sers did not have a collateral purpose in not agreeing to the refinancing proposals as they were concerned about the economic benefits of the sale and leaseback proposal since MA would no longer need factory space once the business was gradually relocated to Wuxi, China. The trial judge held that, on the contrary, it was MA who was using the cross-claim as a collateral purpose, *ie*, to restrain HL from presenting a winding-up petition.

41 In relation to [35](c) above, the trial judge held that MA, instead of paying US$10m to MI for interest due under the loan from MI, should have used it to pay the undisputed debt. He rejected MA's argument that the payment to MI was for investment in a new factory in China and that the revenue generated by the new business would accrue to the benefit of MA as part of the group operations. He held that this was not equitable to HL. In his view, MA, logically, should have received payment for the sale of its products and should have been able to pay the undisputed debt unless the purchase moneys were diverted elsewhere and/or the prospects of the businesses were not as good as MA was suggesting.

42 In the result, the trial judge dismissed MA's application.

43 After MA's application was dismissed, the Sers obtained a report from D&T ("the D&T report") on or about 24 April 2006 to support its opinion that MA was insolvent. In response to the D&T report, MA engaged PriceWaterhouseCoopers ("PWC") to advise MA on its financial position. PWC issued its report on 11 July 2006 stating that while MA was facing financial difficulties, there was no conclusive evidence to show that it was technically insolvent. Anthony Ser responded by applying to court (Originating Summons No 1407 of 2006) for disclosure of MA's terms of engagement of PWC and drafts of the PWC report. The application was dismissed on 31 August 2006 on the ground that the documents were protected by legal advice privilege, and further that the applicant was in a position of conflict as a director of both MA and HL.

44 On 7 July 2006, just after MA filed its appeal against the decision of the trial judge, the Sers commenced an action (Suit No 427 of 2006) for a declaration that MA was insolvent and that the other four directors of MA were in breach of their fiduciary duties to MA. The action is still pending.

Issues for determination in the appeal

45 In this appeal, the issues this court has been asked to determine are as follows:

(a) Whether MA has a genuine cross-claim based on substantial grounds ("Issue A").

(b) Whether MA's cross-claim is equal to or in excess of the undisputed debt (ie, whether the S$25m security held in escrow has reduced MA's cross-claim to S$9m) ("Issue B").

(c) Whether HL had a collateral purpose in threatening to wind up MA ("Issue C").

(d) Whether the filing of a winding-up petition against MA would cause irreparable harm to MA's business and reputation ("Issue D").

We will consider these issues now.

Issue A: Whether MA has a genuine cross-claim based on substantial grounds

46 The judge found that MA did not invent a cross-claim in order to ward off the threatened winding-up proceedings. There was evidence that MA had raised the issue of breach of warranties by HL some months before the service of HL's statutory notice and that it had engaged EY to quantify its claim based on such breaches. However, before us HL has made the following points:

(a) MA's case is an abuse of process in that it had stalled, delayed and bought time for itself;

(b) MA had contrived grievances and misled the court;

(c) MA changed its position and is now using the court to force HL to agree to a variation of the SPA;

(d) in order to teach HL a lesson, MA did not raise its staggering cross-claim of S$34m for more than a year as it allowed MA to continue to delay paying the debt and to deprive HL of the early recovery of the escrow sum of S$25m;

(e) while MA was refusing to pay HL the undisputed debt, it was paying off other creditors instead of HL; and

(f) MA was never serious about its cross-claim as it took its time in referring the cross-claim to arbitration and also in failing to comply with the timelines as stipulated under the SIAC rules.

47 In our view, HL has overstated its case with respect to all these allegations. Having regard to the evidence before the court, we agree with the judge that MA's cross-claim was a genuine cross-claim based on substantial grounds. In respect of points (a) to (f) of [46] above, we summarise our findings below.

Point (a) – Delay

48 It cannot be denied that HL did give MA time to pay the undisputed debt, but much of the time was taken up by the unsuccessful efforts of MA and MI in trying to persuade the Sers to agree to the refinancing proposals. These were serious business proposals to reduce MA's operational costs which the Sers could not agree for their own reasons, even though they have a 49% ownership of MA. The Sers rejected MA's proposal to pay the debt in six instalments and insisted on payment in four instalments, even though MA had stated that its cash-flow would not allow it to pay in six

instalments unless the refinancing proposals were implemented. The Sers also showed no interest in JPMP MPL's proposal to give a guarantee to HL to secure MA's proposal to pay in six instalments. Finally, after much delay, the Sers agreed to the refinancing proposals in return for a *quid pro quo* in the form of a release from a series of covenants given by them and Leedon as part of the terms of the LBO.

49 It is also pertinent to point out that MA has never denied its financial inability to pay the undisputed debt in one lump sum. Long before HL demanded full payment, MA had been looking for alternative financing to pay the debt, even though the debt was incurred as part of the LBO (which was completed by July 2004), and not an ordinary trade debt. The evidence shows that HL did not make any demands for payment until after Anthony Ser had retired as chairman of MA's board of directors in May 2005, some ten months after the bulk of the undisputed debt had arisen. Anthony Ser has given no explanation why HL delayed seeking repayment until 11 May 2005, which was also the day before MI's directors were due to vote on the refinancing proposals.

Point (b) – Misleading the court

50 The contention that MA had misled the court when it applied for an *ex parte* injunction is based on HL's own interpretation of the effect the S$25m security held in the escrow account. HL is of the view, which the judge accepted, that the security had effectively reduced MA's claim by S$25m, thereby reducing it to S$9m. Hence, when MA claimed, through RG's affidavit, that its cross-claim far exceeded the undisputed debt, it had misled the court. We do not agree with this argument, which will be considered later. MA's claim was not misleading nor was the judge misled by it.

Point (c) – MA's election

51 On point (c), HL's argument is that MA having elected to look to the escrow sum to meet its cross-claim is bound by it as its election has "locked up the Escrow monies to deprive HL of them". At the hearing, MA tried to change its position by seeking the court's approval to return to HL an amount from the escrow account sufficient to effect an equalisation of the cross-claim with the undisputed debt, thereby allowing it to argue that it had a cross-claim equal to the debt. In our view, this argument has no merit, as we will explain later.

Point (d) – Cross-claim not bona fide

52 The evidence shows that MA's cross-claim took time to surface and crystallise into a tangible claim. The Sers retained management control over MA's business for about a year after the LBO. Anthony Ser remained as chairman of MA's board of directors and was in charge of the operations of MA until May 2005. Operational line managers in the company continued to report to him, including WF who was appointed the CEO in March 2005. MA only became aware of possible breaches of warranties under the SPA after WF's appointment. MA was able to crystallise its cross-claim against HL after it obtained from EY at the end of September 2005 an assessment of its potential losses arising from HL's alleged breach of warranties under the SPA. This enabled MA to apply to court for the injunction.

53 EY's computation of MA's loss of about S$34m is equivalent to 7% of the LBO price of about S$470m. The judge did not find that it was unsustainable. Nor did he find the cross-claim wildly inflated even though HL had argued that EY had wrongly applied a multiplier of seven to a large number of recurrent claims. The judge held that these are issues for the arbitrator to decide; it cannot be said that all of MA's claims for breaches of warranties were clearly unsustainable, if they were properly pleaded and there was an express challenge to the value of the EBITDA. We have no reason to disturb the judge's finding on this point.

Point (e) – Paying other creditors

54 HL's main grievance in this respect is the payment by MA of US$10m to MI for accrued interest on MI's loan to MA. MA has explained that the payment was to enable MI to expand the group's business in Wuxi for the benefit of the group. However, there is evidence (a letter from MA's counsel dated 17 April 2006 to HL's counsel) that US$9,307,395.92 has been remitted by Metalform Wuxi to MA during the period from August 2005 to March 2006. HL's response to this remittance is that although it could be said that it benefited the Sers indirectly, it did not benefit HL. HL has also contended that the payment to MI was a fraudulent preference, and that it would not be recoverable for the benefit of HL and other creditors if HL was restrained from presenting a winding up petition. However, apart from MA's failure to pay HL's debt, there is no evidence to show that MA was insolvent or that any other creditor has taken any action against MA.

Point (f) – MA was not serious about cross-claim as evident by its delay in commencing arbitration proceedings

55 This argument is based on MA's delay in making its cross-claim and proceeding with the arbitration. This argument is no longer relevant. The cross-claim was referred for arbitration on 9 December 2005. On 24 August 2006, the day after this court reserved judgment in this appeal, MA applied to the arbitrator to amend its statement of claim to plead breach of warranty in respect of Sched 4, cl 3.1 of the SPA. The arbitrator gave leave to MA to amend the statement of claim to plead HL's alleged breach of warranties that had induced MA to buy the assets and business of HL at an inflated price based on the EBITDA x 7, and suffering a loss in reliance thereof.

Issue B: Whether MA's cross-claim is equal to or in excess of the undisputed debt (ie, whether the S$25m security held in escrow has reduced MA's cross-claim to S$9m)

56 HL has argued that the S25m security held in escrow reduced MA's cross-claim to S$9m, and that MA therefore did not have a cross-claim equal to or in excess of the undisputed debt. In our view, HL's argument on this issue has no merit. A security for a claim does not reduce the claim. It functions as a security and not as a payment. Therefore, the S$25m held in escrow as security for MA's claims against HL arising under the SPA cannot and does not reduce the quantum of MA's cross-claim of S$34m. A partially secured cross-claim is still a cross-claim for the amount claimed. A security is a security until the occurrence of the relevant contingency when it would then be used to pay the actual liability. It is only when it is paid that it will reduce the amount of the claim. If the escrow sum had the effect of reducing the cross-claim, it would have meant that it had been paid to MA. In that situation, MA would have S$25m to pay the undisputed debt. HL's argument fails simply because it cannot have its cake and eat it.

57 Counsel for MA tried to counter HL's argument by offering to release S$10m from the escrow account to HL in order to notionally equalise the debt with the cross-claim. The offer was innovative but it was rejected in any event on the ground that it would prejudice HL's reliance on the undisputed debt as the basis for presenting a winding-up petition against MA. The judge held that MA could not be allowed to make such an offer as it would have meant allowing MA to rewrite unilaterally the terms of the SPA. HL had argued that the terms of the escrow agreement meant that this could not be done without the consent of the escrow agent. In the ordinary case, the beneficiary of a security is entitled to waive his security, but given our holding that the cross-claim is not reduced by the escrow amount, it is not necessary for us to decide whether the judge's finding or HL's argument is correct. HL has also argued that by electing to lay claim to the security in its letter dated 28 September 2005, MA was contractually bound to do so, citing *The Pacific Vigorous* [2006] 3 SLR 374. In our view, the election argument has no merit. MA did not make any election as it was entitled to look to the

security for its cross-claim under the existing arrangement.

Issue C: Whether HL had a collateral purpose in threatening to wind up MA

58 MA's submission is that HL and the Sers had a collateral purpose in threatening to present a winding-up petition against MA in that it was to extract benefits for itself and the Sers in the form of a release from their covenants given in connection with the LBO under the SPA, and was not to obtain payment of its debt. In our view, the evidence shows that initially the purpose of HL in demanding payment and later in giving the statutory notice was to put pressure on MA to pay the undisputed debt. It was only much later that HL decided to take advantage of MA's repeated requests to HL to agree to the refinancing proposals to seek the release of the covenants given by the Sers and Leedon as the price for its agreement. We are unable to find that HL had a collateral purpose in threatening to wind up MA.

Issue D: Whether the filing of a winding-up petition against MA would cause irreparable harm to MA's business and reputation

59 MA has argued that in the present case irreparable harm would be caused to MA if HL was not restrained from filing a winding up petition against MA. Reference was made to the following cases: *L & D Audio Acoustics Pty Ltd v Pioneer Electronic Australia Pty Ltd* (1982) 7 ACLR 180 ("*L & D Audio*") and *Fortuna Holdings Pty Ltd v The Deputy Commissioner of Taxation of the Commonwealth of Australia* [1978] VR 83 ("*Fortuna*"), where the courts took into account this consideration. In our view, however, whether this would be the case or not is not a sufficient basis to grant an injunction. Otherwise, few companies would be wound up if they failed or refused to pay their debts when they became due, and consequently few companies would pay their debts. Irreparable harm is only one factor, albeit a significant factor, that a court takes into account in exercising its discretion whether or not to restrain a creditor from presenting a winding-up petition, or to restrain the advertising of such a petition or to stay such a petition. But it may be neutralised by other factors, such as that the company is insolvent, or that a winding-up petition is the only means whereby a creditor could get the company to pay the debt or any part thereof. In *Bayoil,* the UK Court of Appeal explained that in cross-claim cases, irreparable damage to the company is only one of the considerations that justify the practice of the English courts in restraining a creditor from filing a winding-up petition. Another reason is that the *locus standi* of the petitioner may be put in doubt where the company has a serious cross-claim on substantial grounds equal to or exceeding the creditor's debt, whether the latter is disputed or not.

Jurisdiction of court to restrain filing of winding-up petition

60 We will now examine the law. The main argument of HL that it should not be restrained from presenting a winding-up petition against MA is that it cannot be an abuse of the process of the court for a creditor of an undisputed debt to present a winding-up petition against a company which has failed to pay the debt. It is contended that the court may only do so if the debtor can show that such a petition is bound to fail. It is accordingly argued that whether or not a debtor company should be wound up is a matter for the companies court to decide when the petition is heard.

Where the debt is disputed and where it is undisputed

61 The law is well established where the company fails to pay an undisputed debt after being served with a statutory demand under the Act. In *Malayan Plant (Pte) Ltd v Moscow Narodny Bank Ltd* [1980-1981] SLR 8 ("*Malayan Plant*"), the Privy Council, in an appeal from Singapore, approved (at 11, [13]) the following passage from *Buckley on the Companies Acts* (Butterworth & Co (Publishers)

Ltd, 13th Ed, 1957) at 450:

> A creditor who cannot obtain payment of his debt is entitled as between himself and the company *ex debito justitiae* to an order if he brings his case within the Act. And, notwithstanding a voluntary winding up, on proving his debt and that it remains unsatisfied he will be so entitled.
>
> "It is not a discretionary matter with the Court when a debt is established, and not satisfied, to say whether the company shall be wound up or not … *One does not like to say positively that no case could occur in which it would be right to refuse it but, ordinarily speaking, it is the duty of the Court to direct a winding up*."
>
> [emphasis added]

The statement of the law in the second paragraph was itself a quote from *Bowes v Hope Life Insurance and Guarantee Co* (1865) 11 HL Cases 389; 11 ER 1383 at 402; 1389.

62 The law is equally well established where the company disputes the debt claimed by the creditor. In such a case, the court will restrain a creditor from filing a petition to wind up the company, or if the petition has been filed, to stay or dismiss it on the ground that the *locus standi* of the petitioner as a creditor is in question, and it is an abuse of process of the court for the petitioner to try to enforce a disputed debt in this way. In *Mann v Goldstein* [1968] 1 WLR 1091, Ungoed-Thomas J said, at 1093–1094:

> It is well established that this court has jurisdiction to restrain the presentation or advertising of a winding-up petition and restrain all further proceedings on it. That jurisdiction is a facet of the court's inherent jurisdiction to prevent an abuse of the process of the court. It will be exercised where a winding-up application is presented, or prosecuted otherwise than in accordance with the legitimate purpose of such process.

At 1098–1099, he said:

> For my part I would prefer to rest the jurisdiction directly on the comparatively simple propositions that a creditor's petition can only be presented by a creditor, that the winding-up jurisdiction is not for the purpose of deciding a disputed debt (that is, disputed on substantial and not insubstantial grounds), since, until a creditor is established as a creditor he is not entitled to present the petition and has no locus standi in the Companies Court; and that, therefore, to invoke the winding-up jurisdiction when the debt is disputed (that is, on substantial grounds) or after it has become clear that it is so disputed is an abuse of the process of the court. … Indeed, the prevention of the abuse of the process of the court is the very essence of the whole of this court's jurisdiction to restrain the presentation of a winding-up petition.

Where there is a cross-claim equal to or exceeding the undisputed debt – English and Singapore practice

63 In the present case, MA is seeking to restrain HL from filing a petition to wind up MA based on an undisputed debt on the ground that it has a cross-claim on substantial grounds which exceeds the undisputed debt.

64 In *Bayoil* ([36] *supra*), the debtor did not dispute the debt but sought a stay or dismissal of the petition on the ground that it had a genuine and serious cross-claim equal to or exceeding the debt. The judge accepted the company's contention as to the status of its counterclaim but ordered

the company to be wound up. On appeal, Nourse LJ explained that the practice of the Companies Court to dismiss a petition where the petition debt was disputed in good faith on substantial grounds (which he categorised as a "disputed debt" case) was not, initially, a matter for the discretion of the court but founded on the creditor's inability to establish his *locus standi* to present the petition. However, the case of an undisputed debt with a genuine and serious cross-claim (which he categorised as a "cross-claim" case) was different, in that the dismissal or stay of the winding up petition was a matter for the discretion of the court. *Bayoil* was a cross-claim case. The question was how the court, in the exercise of its discretion, should deal with a cross-claim case.

65 Nourse LJ examined two previous Court of Appeal decisions, *viz*, *In re Portman Provincial Cinemas, Ltd* (1964) 108 Sol J 581 ("*Portman*") and *In re L H F Wools Ltd* [1970] Ch 27 ("*Wools*"), which were both cross-claim cases, and concluded that this practice in cross-claim cases was established by *Portman* and affirmed in *Wools* (*Bayoil* at 154). Nourse LJ held that *Portman* was clear authority for the proposition that the petition ought to be dismissed in cross-claim cases, except in special circumstances (at p 152). In *Bayoil*, Nourse LJ held that neither the potential commercial insolvency of the company nor the ability of the petitioning creditor to levy execution against the company amounted to a special circumstance that entitled him to have it wound up. He explained the rationale thus (at 155):

> [A]n order that a company be wound up, unlike a bankruptcy order, is often a death knell. Nor can it be certain that a liquidator, even with security behind him, will prosecute the company's claims with the diligence and efficiency of its directors.

66 Ward LJ, agreeing with Nourse LJ, gave the following reasons: (a) s 125 of the UK Insolvency Act 1986 [which corresponds to s 257(1) of the Act] dealing with the "Powers of court on hearing of petition" gave the court a wide discretion, which must be exercised judicially; (b) both *Portman* and *Wools* were authorities, from which the Court of Appeal should not depart, that winding up should not be allowed where there was a genuine cross-claim except in special circumstances; (c) there was little difference between the disputed debt and a cross-claim which did not constitute a set-off – citing the Privy Council's statement in *Malayan Plant*; and (d) a winding-up order was a draconian order: if wrongly made, the company had little commercial prospect of reviving itself and recovering its former position. If there was any doubt about the claim and the cross-claim, the court should proceed cautiously.

6 7 *Malayan Plant* was an undisputed debt case where there was no cross-claim by the debtor company. The winding-up petition was granted at first instance and an appeal to the Court of Appeal was dismissed. An appeal to the Privy Council was also dismissed. After referring to *Wools* and stating that the court had a wide discretion under s 225(1) of the UK Companies Act 1948 (which corresponds to s 221(1) of the Act) whether or not to order the winding up of a company, the Privy Council said at 12, [18]:

> There is no distinction in principle between a crossclaim of substance (such as in the *Wools* case) and a serious dispute regarding the indebtedness imputed against a company, *which has long been held to constitute a proper ground upon which to reject a winding up petition.* [emphasis added]

68 Although in *Malayan Plant* the debt was undisputed, it was not a case of the debtor seeking to restrain the creditor from presenting a winding-up petition. It was a case of the debtor seeking to dismiss the petition after its presentation on the ground that the Court of Appeal had exercised its discretion wrongly. Accordingly, the statement of the Privy Council that there was no distinction between a cross-claim of substance and a seriously disputed debt might be said to be *obiter*.

However, two points should be noted. First, even if what the Privy Council stated in *Malayan Plant* was *obiter*, the approval of this principle in *Wools* meant that the law in Singapore practice would be that as administered in England by virtue of s 5(1) of the Civil Law Act (Cap 43, 1988 Rev Ed). Secondly, and equally important, the Privy Council's statement equating a cross-claim with a seriously disputed debt called into question the *locus standi* of the creditor in such a case to present a winding-up petition against the debtor.

69 The practice established by *Portman* and affirmed by *Wools* was followed by the High Court in *Ng Tai Tuan v Chng Gim Huat Pte Ltd* [1990] SLR 903 ("*Ng Tai Tuan*") to stay a winding-up petition on the ground that the debtor had a genuine and substantial cross-claim exceeding the debt. Chao J in *Ng Tai Tuan*, also referred to Australian and New Zealand authorities in support of his decision.

70 In *De Montfort University v Stanford Training Systems Pte Ltd* [2006] 1 SLR 218, the High Court stayed a winding-up petition which was presented before the company commenced an action against the creditor claiming an unliquidated sum, applying the Privy Council's statement in *Malayan Plant.* Tay J held that in the light of the alleged counterclaim, the debt was disputed on substantial grounds and it could not be ascertained whether the petitioner's alleged debt would exceed the statutory minimum of S$10,000 provided for under s 254(2)(*a*) of the Act in order to make the winding up order.

71 It may also be useful to note that *Bayoil* was adopted and applied in Hong Kong by the Court of Appeal in *Re S Y Engineering Co Ltd* [2002] HKCA 61, which in turn was followed by the Hong Kong High Court in *Re Keen Lloyd Resources Ltd* [2003] HKCFI 671*.*

72 It may be noted at this point of our discussion that all the cross-claim cases were concerned with situations where winding-up petitions had been filed, and the only question in each case was whether the petition should be stayed or dismissed. We now consider two divergent English decisions on the court's jurisdiction to grant an injunction to restrain the presentation of a winding-up petition. In *Re a Company (No 006273 of 1992)* [1992] BCC 794, Millett J refused to restrain the presentation of a winding-up petition based on an undisputed debt where the company had a cross-claim which exceeded substantially the debt due to the petitioning creditor but had not been litigated. Millett J held that there was no abuse of the process of the court as the presentation of the petition was for a purpose that was entirely proper, *ie*, to bring pressure for the payment of a debt which was indisputably due. He did not regard the Court of Appeal's decisions in *Portman* and *Wools* as preventing the court from making a winding-up order where there is a serious cross-claim on substantial grounds. However, in *Bayoil,* Nourse LJ rejected Millet J's interpretation of *Portman* on the ground that the transcripts of the judgments in *Portman* were not before Millett J*.*

73 In his judgment, Millett J had also referred to the observations of Morritt J in *Re Leasing and Finance Services Ltd* [1991] BCC 29 that it could not be said at the preliminary stage when an application was made for an injunction to restrain the application of a petition, that the existence of the cross-claim meant that the petition was *bound to fail* when it came to be heard after the advertisement of the petition and in the light of the available evidence. This appears to be the first reported English decision that the "bound to fail" test was applied in a cross-claim case where the debt was undisputed. The Court of Appeal in *Bayoil* made no reference to this issue. Neither did the Privy Council in *Malayan Plant.* But, as we have mentioned earlier, in *Fortuna*, McGarvie J held that the standard of proof in such a case was not that the petition is bound to fail, but that it is unlikely to succeed in the circumstances existing at the time.

74 In *Re a Company No 1122 of 2003* [2003] ALL ER (D) 338*,* a cross-claim case where the debt was undisputed, the court developed this point further. There, Etherton J said:

> Where a debt was undisputed, but it was alleged that there was a cross claim, the court would *generally* restrain presentation or advertisement if; (i) the cross claim was substantial; (ii) the company had been unable to litigate the claim; and (iii) the claim was greater in value than the claim of the respondent. The claim for misrepresentation had no basis. The claim for damages for breach of cl 5 of the transfer agreement [the cross-claim] raised issues of law and fact that were relevant to the outcome of the applicant's claim under cl 5, and were not properly to be determined on a summary application of the kind before the court. In order to succeed on the instant application, *the applicant had to show that its claim had a real prospect of success*. On the facts, *the court could not say, in the absence of oral evidence or cross- examination, the applicant's claim had no prospect of success.* Accordingly, the court would grant the order sought. [emphasis added]

The Australian practice

75 Counsel for HL accepts that the Australian practice on cross-claims is the same as that of the English and Singapore courts. In *Ng Tai Tuan,* the relevant Australian decisions were referred to by Chao J, including *Glenbawn Park Pty Ltd, Re* (1977) 2 ACLR 288 ("Glenbawn Park"). In *Bayoil,* Nourse LJ also referred to the same in holding that dicta in Commonwealth decisions supported the English practice. In *Fortuna*, a cross-claim case, McGarvie J, after reviewing the existing Australian, English and New Zealand authorities, said at 87–88:

> When a court restrains the presentation of a winding up petition to that court it exercises it as part of its inherent jurisdiction to prevent abuse of its process: [*Mann v Goldstein* at 1093–1094]. Usually a court acts against abuse of its process after proceedings have been commenced. Thus, existing proceedings may be stayed or dismissed, or documents delivered as a step in the proceedings may be struck out ... The law has long recognized that with proceedings to wind up a company, intervention after the commencement of proceedings would often be too late to relieve the company of oppression and damage. The courts have recognized that irreparable damage may be done to a company merely through public knowledge of the presentation of a petition. Usually the damage flows from the loss of commercial reputation which results. The courts have also been conscious of the pressure which may be put on a company, by a person with a disputed claim against it, threatening to present a winding up petition unless the company meets his claim. While that threat exists, the company, in order to avoid the damage involved in the presentation of a petition, is pressed to meet the claim although it may have substantial and genuine grounds for regarding itself as not required to do so.
>
> The decisions of the courts have established the principle that the presentation of a winding up petition may be restrained by injunction where its presentation would amount to an abuse of the process of the court. The courts apply this principle similarly to restrain the advertisement of a petition already presented. The principle enables companies to be protected from threatened or apprehended oppression and damage from abuse of court process.
>
> The basis on which the courts have intervened in the cases cited by counsel, has been that presentation of a winding up petition might of itself cause irreparable damage to the company. Given that basis, the application of the principle which entitles the courts to intervene to prevent abuse of process depends on the existence of different elements in two distinct situations considered in the authorities. For convenience, I will refer to the application of the principle as the first and second branches of the principle.

At 93–94, McGarvie J said:

> The first branch applies to cases where the petitioner is incapable of success as a matter of law or through absence of supporting evidence. Where the petitioner is not entitled to present a petition or where the ground alleged is not a ground which can found a winding up order, the petitioner is incapable of success as a matter of law. If there is no sufficient evidence to establish an otherwise sufficient ground the petitioner is incapable of success for that reason. …
>
> The second branch applies to cases where there is a more suitable alternative means of resolving the dispute involved in a disputed claim against the company. … Thus the second branch applies where, because of the availability of a suitable alternative procedure, the petition is unlikely to succeed in the circumstances existing at the time.

McGarvie J further stated (at 95) that the second branch of the principle has often been applied to creditors' petitions where: (a) the debt is genuinely disputed on substantial grounds, in which case, the court may restrain the presentation of the petition, citing *Cadiz Waterworks Co v Barnett* (1874) LR 19 Eq 182; (b) the debt is not disputed but the company has a genuine cross-claim on substantial grounds equal to or exceeding the petitioner's debt, in which case the court has the discretion to dismiss the petition, citing *Wools*; and (c) a creditor intends to present or advertise a petition and the company has a genuine cross-claim based on substantial grounds, which equals or exceeds the creditor's debt, a court may grant an injunction restraining the presentation or advertisement of the petition, citing *Cercle Restaurant Castiglione Co v Lavery* (1881) 18 Ch D 555, and *Tranquility Holdings Pty Ltd v Glass Pools Pty Ltd* (1974) CLC ¶40-133.

Standard of proof in cross-claim cases

76 With respect to the standard of proof, McGarvie J said (*Fortuna* at 103–104):

> I consider that before restraining the presentation of a petition against a plaintiff company I would need to be satisfied on the material before me, that it is unlikely that a winding up order would be made by any judge in the exercise of his discretion … I do not accept the submission that before granting an injunction I would need to be satisfied that the Deputy Commissioner had no chance of success in obtaining a winding up order. The present case is to be determined upon the second branch of the general principle, where the presentation of a petition may be restrained despite the fact that there is a chance that a winding up order may be made. This chance may exist in at least two ways. First, the test that it is unlikely that a winding up order would be made by any judge in the exercise of his discretion, does not exclude all possibility of such an order being made. Second, if the test is stated in different words, the position is that an injunction may be granted where it is likely that if a petition were presented, any judge would either dismiss it or stand it over. The purpose of standing over a petition is to enable the disputed claim to be determined in other proceedings. If the other proceedings result in favour of the petitioning creditor, the court may then make a winding up order.

77 Having regard to the decisions mentioned above, the propositions as stated by Etherton J (see [74] above) represent the current practice in England, Australia and Singapore in such cases. The company does not have to show that the winding-up petition is bound to fail, but that there is a likelihood that it may fail or that it is unlikely that a winding-up order would be made. Furthermore, in such a case, where the court is unable to say that there is no prospect of success without oral evidence or cross-examination, the court will grant the injunction.

New Zealand practice

78 Counsel for HL has referred us to the New Zealand practice in cross-claim cases. Prior to the

decision in *Re Julius Harper Ltd, ex parte Winkler & Co (Hong Kong) Ltd* [1983] NZLR 215 ("*Julius Harper*"), the New Zealand approach was the same as that of the Australian and English courts. However, in *Julius Harper* the New Zealand High Court departed from its previous practice. There, the debtor, who did not dispute the petitioner's debt, sought an injunction to prevent the *advertising* of the petition on the ground that it had a genuine cross-claim based on substantial grounds exceeding the petitioner's debt. Hardie Boys J held that where the creditor's debt was undisputed, there was no question of the creditor's *locus standi* in presenting the winding up petition and that its so doing was not an abuse of process of the court since it had a statutory right to do so. He further held that such a cross-claim was not an automatic bar to a winding-up order. Hardie Boys J, after referring to *Charles Forte Investments Ltd v Amanda* [1964] Ch 240 ("*Charles Forte*"), and *Bryanston Finance Ltd v De Vries (No 2)* [1976] Ch 63 ("*Bryanston*"), said at 220:

> It is to be noted that the English cases dealing with the situation where the company asserts a counterclaim do not proceed on the basis that the dispute necessarily puts in question the locus standi of the petitioner. Indeed, *if that were the basis*, consistency with the cases where the debt is disputed would require the Court to refuse to make a winding up order at all; but that is clearly not the approach that is taken. If therefore the making of a winding up order is in the discretion of the Companies Court, it is difficult to see how proceedings upon a petition to bring the matter before that Court, in order that it may itself determine how its discretion should be exercised, can amount to an abuse of process, and so justify the issue of an injunction. [emphasis added]

Hardie Boys J acknowledged that there were Australian and New Zealand decisions which adopted the view that a substantial counterclaim does raise the question of whether the petitioner has sufficient *locus standi*, referring to, *inter alia*, *Glenbawn Park* (which was approved by Chao J in *Sanpete*) where Yeldham J held that a counterclaim on substantial grounds destroys the locus standi of the petitioner. After examining these and other cases, he concluded as follows at 223:

> As the debt upon which the petition here is based is not disputed, the petitioner has the locus standi to bring its petition. The counterclaim asserted by the company, even though it be bone fide and based on substantial grounds, is in my opinion no automatic bar to a winding up order. Thus I do not think it is an abuse of process for the petition to be presented or proceeded upon. I do not consider it a proper function of the Court in the exercise of its inherent jurisdiction to embark upon a consideration of matters relevant to the exercise of a discretion – and indeed to exercise the discretion – which is conferred by the Companies Act and properly belongs to the Court when hearing the winding up petition itself. I would accordingly dismiss the present motion as being without foundation in law.

79 *Julius Harper* was approved by the New Zealand Court of Appeal in *Anglian Sales Ltd v South Pacific Manufacturing Co Ltd* [1984] 2 NZLR 249 ("*Anglian Sales*"). McMullin J, after examining Australian, English and New Zealand authorities, concluded at 252:

> It follows that where the existence of the debt on which the petition is founded is unchallenged it cannot be said with the same confidence that the proceedings amount to abuse of process by reason of an alleged counterclaim. Where therefore the debtor, while admitting the debt, advances a counterclaim in attempted answer to a petition, the latter should *normally* proceed to determination, with the Court retaining a discretion as to whether it ultimately makes a winding up or not. [emphasis added]

Greig J, after examining the conflicting New Zealand decisions, said at 254:

There is a clear distinction between the exercise of the discretion on hearing the petition and the exercise of the inherent jurisdiction to restrain or stay the presentation of or further proceedings on a petition. What the appellant invokes in this case is the latter; to stay proceedings as vexatious or an abuse of the Court's process. That is a general inherent jurisdiction which is exercisable in appropriate cases in any proceedings, including a petition for winding up brought under the Companies Act. It is a jurisdiction which is to be exercised with great circumspection. *The test is whether it is impossible for the party concerned, in this case the petitioner, to succeed in its claim.* That, in my view, is the basis for the decision in [*Charles Forte*] and [*Bryanston*].

In cases where there is a disputed debt, that is to say, a substantial dispute that the debt is payable at all, then in accordance with the ordinary rule the petition *is bound to* fail because the petitioner has not shown he is a creditor and the Court on hearing the petition will not enter into the dispute.

…

Other considerations apply when the debt is not disputed in whole, as is the situation in this case, but there is a cross-claim or counterclaim which is alleged to equal or exceed the amount of the creditor's debt. In that case the creditor is still a creditor.

On the hearing of the petition it remains a matter of discretion as to whether the petition will be granted or not. That is clear from [*Wools*], but it is not a discretion which is invariably or inevitably exercised against the petitioner. *That being the case it cannot be said in these proceedings that the petitioner is bound to fail even though there may be some doubt as to whether the petitioner will be granted.* That, however is a matter for the exercise of the Court's discretion on the hearing of the petition and raises different considerations to those which apply on the hearing of a motion to restrain, such as this.

Reference has been made in this and other previous High Court decisions in New Zealand to a number of Australian decisions which display a conflict between the view that a substantial counterclaim raises a question of locus standi resulting in a preference for an exercise of the inherent jurisdiction against the petitioner and the view that, on the other hand, the existence of a counterclaim does not affect the locus standi. *I think that those who prefer the former view have failed to make the distinction between the inherent jurisdiction to prevent in special cases an abuse of the Court's process and the exercise of the discretion on the hearing of the petition.*

[emphasis added]

Standard of proof in New Zealand cases

80 The New Zealand cases require the company to show that a winding-up petition against it is bound to fail before the court will exercise its inherent jurisdiction to restrain the creditor of an undisputed debt from presenting a petition against it. What policy reasons justify the imposition of such a high standard of proof on the company in such cases? In *Julius Harper,* Hardie Boys J referred to both the "bound to fail" test in *Bryanston* and the "likely to fail" test in *Fortuna* without deciding which test he should apply in dismissing the application to stay the winding-up petition. However, in *Anglian Sales,* McMullin J, whilst referring to the discussion in *Bryanston* on the differences between a disputed debt and a cross-claim, did not specifically endorse the "bound to fail" standard of proof. It was Greig J who had held, relying on Wilmer LJ's judgment in *Charles Forte* and Buckley LJ's judgment in *Bryanston,* that the test whether the court should exercise its jurisdiction in restraining a winding-

up petition was whether it is impossible for the party concerned, in this case the petitioner, to succeed in its claim.

Should this court follow the New Zealand approach?

81 HL has invited the court to reconsider the legal position in Singapore in the light of the practice in New Zealand. Counsel has pointed out that this is an issue of law as well as policy, and that the High Court has made reference to some policy concerns in *Tang Choon Keng Realty (Pte) Ltd v Tang Wee Chong* [1992] 2 SLR 1114 ("*Tang Choon Keng Realty*"). The policy concerns may be stated to be as follows. First, a creditor who has an undisputed debt has a statutory right to file a winding-up petition against a company which has failed to pay the debt. It is not an abuse of the process of the court for him to invoke his statutory rights. Therefore, there is no basis for the court to restrain him from filing his petition. Secondly, as there is also no abuse of process even where the company claims that it has a serious cross-claim on substantial grounds, the court should not prevent the petition from being filed but determine whether it should be stayed or dismissed on hearing the petition. Otherwise, the company would be allowed to litigate the same issue twice, leading to an unnecessary prolongation of such proceedings. Furthermore, such restraining orders have the potential of defeating the rights of creditors who may not have the same financial resources as the company, thereby denying them equal access to the court after a pre-emptive strike.

8 2 In our view, we do not think that these matters outweigh the policy consideration that the commercial viability of a company should not be put in jeopardy by the premature presentation of a winding-up petition against it where it has a serious cross-claim based on substantial grounds. Such a petition may adversely affect the reputation and the business of the company and may also set in motion a process that may create cross-defaults or cut the company off from further sources of financing, thereby exacerbating its financial condition. So long as the court is satisfied that on the evidence there is a distinct possibility that the cross-claim may exceed the undisputed debt, it should give the company the opportunity to prove its claim rather than to allow a winding-up petition to be filed, with all the normal consequences attendant upon the filing of such a petition. Businesses that have a chance of recovery should not be pushed into a state that makes it difficult for them to recover.

8 3 In *Tang Choon Keng Realty*, the High Court applied the "bound to fail" test, following *Charles Forte and Bryanston*. However, it is necessary to point out that *Tang Choon Keng Realty* was an oppression case under s 216 of the Act and also a "just and equitable" case under s 254 of the Act where the would-be petitioner was a shareholder of the company, which was also the case in *Bryanston* under the corresponding provisions of the UK Companies Act. Similarly, *Charles Forte* was a "just and equitable" case arising from disputes between shareholders. The position of a shareholder is different from that of a creditor. It is necessary to recognise this distinction. A shareholder always has *locus standi* to present an oppression petition or a winding-up petition on just and equitable grounds. An aggrieved minority shareholder has no recourse to any course of action to redress the wrongs allegedly done to him by the majority except by petitioning the court, either to seek a buy-out order or to wind up the company pursuant to s 216 of the Act. However, he is not entitled to such an order except as a last resort, as was held in *Tang Choon Keng Realty* (and recently held by this court in *Lim Swee Khiang v Borden Co (Pte) Ltd* [2006] 4 SLR 745). The court will not grant him a winding-up order unless there is no other way of bringing an end to or remedying the matters complained of. That, in our view, is a reasonable basis for the court not to restrain him from filing his petition without giving him a full hearing, unless the petition is bound to fail.

8 4 In *Bryanston,* Buckley LJ recognised that the presentation of a winding-up petition might cause great damage to a company's business and reputation, although he was of the view that the

potential damage might have been exaggerated. His comments were apt in the context of a shareholder's petition for oppression or winding up of a company on just and equitable grounds, where the issue is normally whether there has been an abuse of power by the majority shareholder. Such a petition does not damage the company's business, in contrast with a creditor's winding-up petition based on the company's inability to pay its debts. A creditor's winding-up petition implies insolvency and is likely to damage the company's creditworthiness or financial standing with its other creditors or customers. In the contemporary business environment, practically all businesses are financed in varying degrees by debt. An LBO entity, such as MA, is highly leveraged from the time of its existence. Modern loan arrangements inevitably contain financial covenants which, if breached, might trigger other cross-default clauses. The presentation of a winding-up petition against the company is invariably such an event of default. In the present case, it would appear that MA would have 60 days to set aside a winding-up petition to avoid a default that would enable the bank to recall its loan. If other cross-default clauses are triggered, it would merely compound the company's problems. The prospect of the company's business being ruined in this way is very real. These consequences do not ordinarily occur in s 216 or s 254 petitions under the Act since they are not related to the company's financial standing.

85 In our view, in relation to an application to restrain the filing of a petition to wind up a company, the courts should make a clear distinction between a shareholder's petition and a creditor's petition. We may add that in the Malaysian case of *Pembinaan Lian Keong Sdn Bhd v Yip Fook Thai* [2005] 5 MLJ 786, Vincent Ng J considered the relevant authorities and came to the conclusion that the "bound to fail" test should only be applied in a shareholder's petition and not in the case of a creditor's petition where the debt was disputed.

86 In our view, the "bound to fail" test is in principle the wrong test to apply in cross-claim cases, whether the debt is disputed or undisputed. As a matter of evidence, until the cross-claim is tried, it would be impossible to tell what the decision of the court would be, either on the merits of the cross-claim or whether its quantum would equal or exceed the undisputed debt. Applying such a stringent test at the hearing of any application to restrain a winding-up petition would effectively lead to the dismissal of the application. It would amount to applying a principle of law rather than a principle of evidence.

87 This standard of proof is also inconsistent with the standard that is applicable where the application is to stay the petition after it has been filed. The standard of proof in a stay application founded on a serious cross-claim on substantial grounds is that the petition is unlikely to succeed or that it is likely that the court will hold over the petition in order to allow the cross-claim to be determined first. There is no particular reason why the standard of proof should be higher in the first case than in the second case. Moreover, it is ironic that in the second case, irreparable damage might well have been done to the company by the filing of the petition, and yet the standard of proof in staying the petition is lower than the "bound to fail" standard. We therefore conclude that it is inappropriate to apply the "bound to fail" test in cross-claim cases.

88 For all these reasons, the New Zealand approach does not commend itself to us, and we respectfully decline to follow it.

Findings of this court

89 In summary, our findings on the issues raised on appeal are as follows:

(a) MA has a genuine cross-claim based on substantial grounds;

(b) until the cross-claim is decided by the arbitrator (whom the parties have agreed is the proper adjudicator of this issue), we affirm the judge's finding in the court below that it is not possible at this stage to conclude that the cross-claim is not equal to or in excess of the undisputed debt;

(c) the evidence does not show that HL's dominant purpose in threatening to wind up MA was to secure for itself and for the Sers the release of their covenants under the SPA;

(d) the filing of a winding-up petition against MA is likely to cause irreparable harm to MA's business and reputation; and

(e) HL has not shown the existence of any special circumstances why the court should not restrain HL from presenting a winding-up petition against MA.

90 Accordingly, we allow the appeal with costs below and on appeal to follow the event, and the usual consequential orders.