

## Client Alert

March 2020

### Survival of Companies Impacted by the COVID-19 Outbreak

Economies all around the world are experiencing an unprecedented economic slowdown amidst rising concerns of the Coronavirus ("**COVID-19**") pandemic and Malaysian companies including large conglomerates are not spared. As it stands, the Movement Control Order ("**MCO**") in Malaysia, which is in effect from 18 March to 31 March 2020, has severely impacted various industries such as tourism, travel, aviation, retail, and construction among others. With no immediate certainty in sight, companies will be deeper in debt with little or no revenue generated. This will accordingly cause defaults in debt obligations and significantly increase the risk of insolvency. As a result, significant number of corporations (if not all) will be impacted.

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Key questions concerning the survival of an organisation that will arise out of the economic crash would include among others:

- Whether your company is now or will be in financial distress?
- What are the rescue mechanisms to prevent liquidation of your company?
- What you should do if a debtor is undergoing restructuring efforts?

In the unfortunate event that your organisation is severely impacted by COVID-19 and the MCO, the first immediate thing to do is to assess your financial status and consider whether a temporary moratorium will assist the viability of the organisation as a going-concern in the longer run.

#### Corporate Rescue Mechanism under Companies Act 2016 ("**CA**")

There are several mechanisms under the CA which will provide temporary shelter while you seek to restructure your existing debt obligations, including refinancing or rescheduling of credit facilities and securities.

The CA provides for the following rescue mechanisms namely (i) Corporate Voluntary Arrangement (ii) Judicial Management, and an improved (iii) Scheme of Arrangement process whereby there are moratorium periods preventing legal proceedings or action to be taken against the financially distressed company ("**Moratorium**"). Such Moratorium will allow breathing space for the organisation to restructure its debt or obtain additional financing. Key highlights of the various rescue mechanisms are discussed below:

##### (I) Corporate Voluntary Arrangement

- A Corporate Voluntary Arrangement ("**CVA**") is a procedure initiated by directors or shareholders of a private limited company (with no pledged





security) to prepare a proposal for its creditors to enter into a voluntary arrangement to essentially accept a reduced payment ("**Proposal**").

- A company that opts for a CVA will be entitled for **Moratorium for 28 days, which is extendable to 60 days.**
- A key consideration in the Proposal is that it should aim to preserve viable but distressed companies, provide a real prospect of return and maximise creditors' interests, all of which would be a better option than winding up the distressed company.
- This process is mainly driven without the Court's supervision. Nonetheless, to safeguard the creditors' interest, the implementation of the Proposal will be supervised by an independent insolvency practitioner.
- Having the Moratorium in place also provide breathing space to distressed companies to work out alternative arrangements with its bank creditors which may include restructuring/rescheduling of existing facilities, granting of temporary cash line facilities to address immediate trade lines requirements or even providing additional assets to secure existing financing to maintain security cover ratio expected by bank creditors.

#### **(ii) Judicial Management**

- Judicial Management ("**JM**") is a process where the rehabilitation or restructuring efforts of an organisation is placed in the hands of a qualified insolvency practitioner i.e. the Judicial Manager. This process is initiated upon the application of a company director or a creditor of private companies (except those which are publicly listed) to the Court.
- The Court will consider whether placing the organisation under a JM if there is reasonable probability of preserving the business which would serve the interests of creditors better than a winding up.
- The Judicial Manager is then tasked with preparing a restructuring plan for the organisation and a temporary **Moratorium for 6 months** will be granted. A further **extension of another 6 months** could be obtained from the Court.
- Appointment of Judicial Manager can also be seen as a useful tool to give comfort to bank creditors to ensure financially distressed companies with sound fundamentals are being managed by professionals with relevant skillsets to assist the distressed companies out of this unprecedented perfect storm. It is safe to say not many companies (especially those in the SME category) would have experienced such unprecedented times and will likely need all the expert assistance that they can get. Business owners should appreciate appointment of Judicial Manager does not mean the business owners have lost their business. It is a temporary measure to assist their companies to regain their footing.

#### **(iii) Scheme of Arrangement under CA**

- A company under financial distress, through its director, shareholder, creditor or even Judicial Manager may also consider applying to Court to sanction a



scheme of arrangement ("**SA**") which essentially is a compromise or arrangement between the company, its members and creditors.

- A SA is a court driven restructuring process where the affected creditors, members as well as the company in question are expected to go back to the Court to fully ventilate and justify the genuineness of such scheme.
- While the process of the SA is being considered or taking place, the Court may grant a restraining order equivalent to a **Moratorium for 3 months**, which may be further extended up to a **maximum of 9 months** provided that certain statutory criterias are met.
- A scheme of arrangement does not just entail rescheduling of debts. It can also include issuance of straight debt financial instruments, issuance of quasi- equity financial instruments to creditors to mitigate repayment pressures and injection of additional equity by existing shareholders or by new potential investors.

### **Action for creditors - What you need to do.**

While a Moratorium may be in place pending the restructuring efforts, various applications may be file to challenge or set aside such Moratorium. It is important to fully review any scheme or proposal received to identify whether the organisation seeking refuge through the various corporate mechanisms are merely abusing the process to delay the inevitable. There has been instances where the Courts have found the applicants using Moratorium or restraining orders merely to delay the legal process when there is no actual restructuring or rehabilitation efforts being undertaken. In some instances, assets were further depleted during this period.

Nonetheless, in a genuine effort undertaken to restructure the company in financial distress, it may be worthwhile to support such scheme or proposal to recover the debt owed.

### **Financial Relief Scheme**

In February 2020, the Malaysian government issued an emergency **stimulus package** ("**Stimulus Package**") worth USD 4.8 billion to counter the economic impact of the COVID-19 outbreak.

In line with the Stimulus Package, the Malaysian banking sector is stepping up measures to provide financial relief to help its customers affected by COVID-19 by, amongst others, rescheduling or restructuring loans, offering payment moratoriums as well as short-term financing to help alleviate short-term cash flow problems. BNM has allocated a RM 2 billion special relief facility which will be specifically deployed in the form of working capital for small and medium enterprises.

There will be a 100% stamp duty exemption on agreements entered into arising from these rescheduling, restructuring, or moratoriums exercises. The exemption can be used for agreements entered into between 1 March 2020 until 31 December 2020. Subject to clearance from the stamp offices, examples of these



agreements could include new loan agreements that is connected to a restructuring scheme or new securities granted to secure previously unsecured credit facilities. The latter could provide temporary relief to companies and banks who may be dealing with previously unsecured trade lines.

### **Plans Moving Forward**

Companies should reassess their financial position and, amongst others, consider the impact of COVID-19 and/or MCO on business strategies and vulnerabilities. In the event that the company is unable to repay its debts, the company may wish to review any force majeure provisions, initiate conversations with creditors or financiers to avail itself to any corporate rescue mechanism or financial relief measures offered by the relevant financial institutions.

Similarly, creditors should assess the impact to credit profile and align contingency plans with key customers. With the uncertainty surrounding the duration of COVID-19 and/or MCO causing business disruptions, creditors should evaluate counterparty risk and take mitigation measures to preserve accounts receivables.

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