

THE UPDATE



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We wish to bring the attention of our readers to the recently reported Court of Appeal decision in ***Lim Eng Chuan Sdn Bhd v United Malayan Banking Corporation & Anor*** [2011] 1 AMR 44, [2010] 9 CLJ 637. This decision joined the line of authorities starting from the landmark case of *Kimlin Housing Development Sdn Bhd v Bank Bumiputra (M) Sdn Bhd* [1997] 2 MLJ 805 which seeks to crystallize the law on disposition of landed assets charged by a company as security to a bank by way of registered charge under the National Land Code as well as pursuant to a debenture where the company is subsequently placed under receivership or in liquidation. The law is, in our respectful conclusion, not certain and remains to be settled by the Federal Court when it hears the appeal from *Lim Eng Chuan* which is pending at leave stage.

THE 'CHRONICLE' OF KIMLIN

1. Yes, the saga continues. The novelty of law as conceived in the decision of the Supreme Court (then the highest court in Malaysia which was subsequently renamed as Federal Court) in *Kimlin Housing Development Sdn Bhd v Bank Bumiputra (M) Sdn Bhd*ⁱ ("Kimlin") with regard to the disposition by financial institution, in the course of realizing its security, of a landed property belonging to its borrower company in receivership or liquidation was revisited recently by the Court of Appeal in *Lim Eng Chuan Sdn Bhd v United Malayan Banking Corporation & Anor*ⁱⁱ ("Lim Eng Chuan"). Indeed, in between these two cases over the span of 13 years, there was a couple of reported decisions coming from the Federal Court that sought to narrow down the seemingly 'perilous' effect of *Kimlin*. They were *Melantrans Sdn Bhd v Carah Enterprise Sdn Bhd & Anor*ⁱⁱⁱ ("Melantrans") and *K Balasubramaniam, Liquidator for Kosmopolitan Credit & Leasing Sdn Bhd v MBf Finance Bhd & Anor*^v ("K Balasubramaniam"). *Lim Eng Chuan* is the latest to join the line of authorities on this area of law albeit emanating from the Court of Appeal which is at a lower tier subservient to the Federal Court.

Kimlin

2. Firstly, let us recap the facts and decision in *Kimlin*. There, the borrower company (appellant) ("the Borrower"), the registered proprietor of certain lands ("the Lands"), created two legal charges ("the Charges") under the National Land Code 1965 ("NLC") over the Lands in favour of a bank (the 1st respondent) to secure the banking facilities granted to it. The Borrower/chargor also executed a debenture^v in favour of the bank/chargee as security ("the Debenture") by way of a fixed charge and a floating charge over, among others, all its plants, equipment, machinery, assets, properties and undertakings. The Debenture provided, *inter alia*, for the bank to appoint receivers and managers ("the R&M") and for such R&M to have certain powers. Subsequently, events occurred upon which the bank exercised its powers under the Debenture to appoint R2, R3 and R4 as the R&M. Unlike a usual debenture, however, there was no express provision in the Debenture appointing the R&M as attorneys of the Borrower. Being desirous of selling

the Lands without resorting to proceedings under the NLC to obtain an order for sale ("the judicial sale"), and having some doubt about their authority under the Debenture to effectuate such sale, the R&M applied to the High Court for leave to sell the Lands ("the leave application"). Five months later, the Borrower was wound up and a liquidator was appointed. The liquidator opposed the leave application.

3. The Federal Court held as follows:

(1) The provisions of the NLC as to the rights of a chargor were designed for its protection and could not be waived nor could the chargor contract itself out of the NLC. Therefore, no power of sale could be conferred by a chargor under the NLC on a chargee itself by way of a debenture or power of attorney or otherwise. Proceedings must be brought by the chargee to obtain a judicial sale in accordance with the procedure laid down in the NLC. Any power of sale which purported to be conferred by a debenture or power of attorney on a chargee itself, omitting all mention of notice and periods of default as prescribed by the NLC and the necessity for obtaining a judicial sale would be invalid and ineffective.

(2) The provisions of the NLC setting out the rights and remedies of parties under a statutory charge over the land comprised in Part XVI were *exhaustive* and *exclusive* and any attempt at contracting out of those rights --- unless expressly provided for in the NLC --- would be void as being contrary to public policy.

Therefore, **the R&M were not entitled to sell the lands by virtue of the powers conferred upon them by the Debenture without taking proceedings under the NLC to obtain a judicial sale.**

(3) The R&M could not resort to s.206(3) of the NLC which appeared to have reserved the contractual operation of any transaction relating to alienated land^{vi}. To invoke s.206(3), it is a condition precedent that there was in existence a transaction relating to alienated land which was valid and enforceable as a contract. Since, however, the relevant provisions of the Debenture relied upon by the bank as conferring upon it a power to sell the lands were void as stated in the preceding

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paragraph, the condition precedent for the application of s.206(3) was absent.

(4) As to the issue on the impact of the winding up of the Borrower on the powers of sale of the R&M, since a statutory charge under the NLC took effect as a security only as opposed to a common law mortgage which entailed a transfer of ownership of the mortgaged land to the mortgagee, with the advent of liquidation, any sale of the land of the wound-up company would be a purported sale of property belonging to the Borrower which required the approval of the court under s.223 of the Companies Act 1965 (“the Act”)^{vii}.

(5) Unlike the legal position in the United Kingdom where a liquidator was obliged to stand on the sidelines in the course of the receivership, the clear implication following from the provisions in the Act in Malaysia was that liquidation did not merely terminate the agency of a receiver and manager but also his powers on winding up, since there was no estate for the receiver and manager to administer by virtue of the definition of the word “officer” under s. 4(1)(b) of the Act [which includes a receiver and manager of the company appointed under a power contained in any instrument, *ie.* a privately-appointed receiver and manager] read with 300(1) of the Act^{viii}.

4. The principal effect of *Kimlin* appears to be that unlike previously held general understanding that a debenture confers on a debenture holder (*eg.* bank) a conventional power of sale exercisable independently of the provisions of the NLC which bypasses the machinery expressly provided by the NLC (*ie.* via judicial sale) without intervention of the court, the debenture holder can no longer enforce its security in the form of a statutory charge under the NLC over landed property other than complying with the explicit provisions under the NLC^{ix}.

Melantrans

5. It took about six years before the apex court had an opportunity to review *Kimlin*, but on a different fact pattern. In *Melantrans*, the 1st respondent (“the said borrower”) who was the registered proprietor of the lease of a piece of land (“the said lease”) executed a debenture in favour of the bank as security for banking facilities granted (“the said debenture”), which was followed by a first legal charge over the said lease under the NLC.

About 18 months later, the bank exercised its rights under the said debenture and appointed a receiver and manager (“the said R&M”) over all the assets and undertakings of the said borrower.

6. Unlike *Kimlin*, there are provisions in the said debenture which:

- (i) irrevocably appointed the said R&M the lawful attorney of the said borrower;
- (ii) empowered the said R&M to act as agent of the said borrower;
- (iii) further empowered the said R&M to effect the sale of the assets secured by the said debenture after taking possession of them.

7. The said R&M entered into an agreement to sell the said lease to the appellant but the appellant refused to proceed with the said purchase on the ground that the said R&M did not have the power to sell the said lease by private agreement in view of *Kimlin*. The said borrower applied to the court for a declaration that the said R&M was duly empowered by the said debenture to sell the said lease. Both the High Court and the Court of Appeal ruled in favour of the said borrower. The question of law posed to the Federal Court was : ‘Notwithstanding a valid power of attorney contained in a debenture, can the receivers and managers appointed under the said debenture proceed to sell the property charged under the NLC by private treaty?’

8. The Federal Court answered the question in the affirmative. In doing so, the highest court of the land drew important distinctions in the facts of the case before it and the facts in *Kimlin*. Firstly, the Debenture in *Kimlin* did not contain an express provision appointing the receivers and managers as attorney of the Borrower. Secondly, in *Kimlin*, the Borrower went into liquidation. The Federal Court pointed out that its predecessor, the Supreme Court did not in *Kimlin* consider the position of the receiver and manager as the agent of the borrower company which went into liquidation. While *Kimlin* correctly dealt with a prescribed method of sale to be undertaken under s.256 of the NLC by a chargee and not a chargor, the said R&M in *Melantrans* undertook the sale on behalf of the said borrower which was the chargor of the said lease. The provisions of the NLC specifying for judicial sale were therefore inapplicable to the factual scenario in

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Melantrans because the said R&M was acting as agent of the chargor.

9. It is submitted that in effect, *Melantrans* restored the generally understood position prior to *Kimlin*. It is this. **In a case where the debenture concerned contains an express provision appointing the receiver and manager as attorney of the borrower and as agent of the borrower and where the borrower is not under liquidation, the receiver and manager appointed by the debenture holder/bank pursuant to the debenture is entitled to exercise its power to sell the charged assets (including landed property in respect of which a fixed legal charge has been created and registered pursuant to the NLC) by private treaty without having to go through the mechanism of sale provided under the NLC.**

10. Query : What if, given similar fact pattern, the borrower is under liquidation? Will there be any difference to the power vested in the receiver and manager in dealing with the charged assets post-liquidation? This brings us to the next case, *K Balasubramaniam*.

K Balasubramaniam

11. In 1982, Koperasi Serbaguna Kosmopolitan Bhd (“the Koperasi”) --- subsequently purchased by the 1st respondent (“MBf”) --- made advances to Kosmopolitan Credit & Leasing Sdn Bhd (“KCL”) which were secured by fixed and floating charges on the assets of KCL under a debenture (“the KCL Debenture”). The charges were duly registered under s.108 of the Act. In February 1991, the Koperasi had appointed the 2nd respondent as receivers and managers over all the assets and liabilities of KCL under the powers contained in the KCL Debenture. In May 1991, KCL was wound-up and the appellant was appointed as the liquidator. In the course of carrying out his work, the appellant issued a notice in Form 33 under the Companies (Winding-Up) Rules 1972 (“the Rules”) and s.277(5)^x of the Act demanding the return of all the properties of KCL in the possession of the 2nd respondent who rejected such demand. The appellant filed an application for numerous reliefs (“the OS Application”) including declarations that the KCL Debenture and the appointment of the 2nd respondent as receivers and managers were null and void and seeking the return of the charged assets which were all movable assets. Whilst the OS

Application was pending, the appellant took out another application seeking a number of directions as to the future conduct of the winding-up. The five orders obtained *ex-parte* by the appellant in this other application were subsequently set aside on the application of the 2nd respondent. The appellant’s appeal to the Court of Appeal was dismissed. In final appeal to the Federal Court, six questions of law were framed which concerned the respective rights of the 2nd respondent as the receivers and managers of KCL appointed under the KCL Debenture and of the appellant as the court appointed liquidator.

12. At the outset, the Federal Court drew special attention to the type of the assets under consideration in the case, namely movable assets of KCL. Such assets were covered under the KCL Debenture as fixed charge which, on the authority of *Mahadevan & Anor v Manilal & Sons (M) Sdn Bhd^{xi}*, was an equitable one. The subject matter in the case thus involved the enforcement of an equitable charge over a movable property. On the other hand, *Kimlin* case concerned land (an immovable asset) which was charged under the NLC. The issue of law raised in *Kimlin* was whether a receiver and manager appointed under a debenture could proceed to sell the charged land by just obtaining the leave of the court (since the chargor was in liquidation) without taking any proceedings under the NLC. Such distinction propelled the apex court to remark that the principles in *Kimlin* should be restricted in scope and limited to powers of a receiver and manager to sell land charged under the NLC and that *Kimlin* should not apply to assets comprised in a fixed and floating charge contained in a debenture, such assets including immovable as well provided they are not charged under the NLC.

13. Following from such remark, it would appear to us that the Federal Court in *K Balasubramaniam* took the position that where an immovable asset fell under a charge in a debenture and if it was charged under the NLC, then it must be dealt with in accordance with the provisions in NLC *ie.* judicial sale. In this respect, it seems that *K Balasubramaniam* contradicts the principle propounded in *Melantrans*.

14. In other words, *K Balasubramaniam* seems to suggest that so long as an asset of a company/chargor is charged under the NLC, irrespective the chargor is under receivership or liquidation or not, such asset must be dealt with in

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accordance with the NLC. That such was the suggestion could be gleaned from the fact that the Federal Court made the remark based on the same rationale as expressed by Abdul Hamid Mohamad J (as he then was) in *Mastiara Sdn Bhd v Motorcycle Industries (M) Sdn Bhd*^{xii} that:

“...what is said in *Kimlin*'s case should be confined to charges registered under the Code. In other words, if a charge is registered under the Code, the remedy must be in accordance with the Code. If the charge in an equitable charge, outside the Code, the Code does not apply and the chargee may enforce the remedy provided in the debenture. Otherwise, there would be a lacuna. The law (courts) recognizes equitable charges but no remedy is available.”

15. We are thus faced with two divergent views from two different panels of the Federal Court in respect of a scenario where the chargor company is not in liquidation and the debenture concerned contains an express provision appointing the receiver and manager as attorney and agent of the chargor, one stating that the receiver and manager is entitled to exercise its power to sell the assets charged under the NLC by private treaty without having to go through the mechanism of sale provided under the NLC (“the Melantrans’ position”), and the other stating that no one is entitled to exercised any power of sale of the assets charged under the NLC without complying with the mechanism provided under the NLC (“the Balasubramaniam’s position”). Whilst the Melantrans’ position can be construed as *ratio decidendi* of the case, the Balasubramaniam’s position is merely an *obiter dicta*. That said, the law is that where two decisions of the Federal Court conflict on a point of law, the later decision prevails over the earlier decision --- *Dalip Bhagwan Singh v Public Prosecutor*^{xiii}. Does the recent decision of *Lim Eng Chuan* provide any clarity to this hazy scene ?

Lim Eng Chuan

16. This decision of the Court of Appeal in *Lim Eng Chuan* was made almost six years after *K Balasubramaniam*. The facts are not dissimilar to those in *Melantrans* except that the subject in *Lim*

Eng Chuan was a piece of land as opposed to a lease which difference does not matter insofar as core principle is concerned. In *Lim Eng Chuan*, the bank/1st respondent gave an overdraft facility to the borrower/appellant. As security, the borrower charged its land to the bank under the NLC and created a debenture which contained an irrevocable power of attorney in favour of the bank (“the PA”), *inter alia*, to sell the land. Upon the borrower’s default in July 1987, the bank demanded for repayment. In September 1994, the borrower was wound up at the instance of another creditor. Following that, utilizing the PA under the debenture, the bank entered into a sale and purchase agreement (“the SPA”) to sell the land to the purchaser/2nd respondent. The borrower brought an action for declaration that the sale of the land pursuant to the PA by the bank to the purchaser was null and void on numerous grounds, including that the sale of the land when the land had been charged to the bank under the NLC was contrary to the principles enunciated in *Kimlin*, that the sale having been entered without leave of the court was *ultra vires* s 223 of the Act and that the PA did not survive the winding-up of the borrower, hence the sale utilizing the PA was void. The High Court dismissed with costs the borrower’s application.

17. The Court of Appeal by majority of 2-1 affirmed the decision of the High Court and dismissed the borrower’s appeal. In doing so, the majority distinguished *Kimlin* on the facts and taking a cue from *K Balasubramaniam*, viewed that the *ratio* of *Kimlin* pertained only to the power of sale exercised by a receiver and manager appointed under a debenture which has no express provision to appoint attorneys for the borrower company. The majority went on to hold as follows:-

- (1) the PA survived the winding-up order and remained valid and effective even after the donor/borrower had been wound-up.
- (2) the bank as the attorney of the borrower was entitled to sell the land pursuant to the PA. In executing the SPA for the sale of the land to the purchaser utilizing the PA granted under the debenture, the bank/chargee was acting on behalf of and as agent for the borrower/chargor. The provisions of the NLC setting out the mechanism for judicial sale of land charged under the NLC did not apply when the sale of the charged land was by the chargor

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because those provisions were meant for situations where the sale was being undertaken by the chargee. The majority in essence based their decision on *Melantrans'* case.

- (3) s 223 of the Act was inapplicable. The bank was exercising its rights under a security when selling the land whereas s 223 was designed to protect unsecured creditors, leaving the rights of secured creditors intact by preserving the 'free' property of the wound-up company to await the distribution of such assets among unsecured creditors.

18. In summary, the answer to the core question for determination was that where the borrower (being a company) has created a legal charge under the NLC and also executed a debenture (containing a power of attorney given in favour of the bank for valuable consideration and expressed to be irrevocable) by way of security for a loan given by the bank to the borrower, and the borrower has defaulted and a winding-up order has been made against it, the exercise of the power pursuant to the power of attorney for the sale of the land by the bank to a purchaser [without complying with the mechanism of sale prescribed under the NLC]^{xiv} is NOT void.

19. From *Lim Eng Chuan*, the following conclusions can be arrived at:

- (1) *Melantrans'* position has been restored.
- (2) As long as the debenture in consideration contains a power of attorney (in favour of the bank or the receiver and manager to be appointed) to sell, by private treaty, the land which has been charged pursuant to the NLC, the attorney (be it the bank or the receiver and manager) is entitled to exercise the power to sell the land by private treaty WITHOUT HAVING TO COMPLY WITH THE MECHANISM OF SALE PRESCRIBED UNDER THE NLC.
- (3) The position mentioned in (2) above is true regardless whether the chargor is in liquidation or not.
- (4) Notwithstanding s 223 of the Act, no leave of the court is required to dispose of the assets

of the wound-up company which has been charged to the chargee.

20. The minority decision was that the sale contravened the statutory prohibition under s 223 of the Act because the chargor of the land had been wound up at the time of the sale and no leave of the court had been obtained. The learned minority judge cited and emphasized on the part of *Kimlin* which stated that:

“...with the advent of liquidation, any sale by the receivers and managers of the lands pursuant to the debenture would be a purported sale of property which belonged to the borrower company, and so would require the approval of the court under s 223 of the Act.”

It is our respectful submission that the minority decision on this point is preferable than that of the majority. Both the judgments of the majority judges were, with due respect, not convincing and were against the natural and ordinary meaning of the wordings of the relevant provision.

21. Alternatively, the learned minority judge held that the sale was in contravention of the provisions in Part Sixteen of the NLC. The learned judge held the view that the sale was actually, on the facts of the case and evidence given, undertaken or effected by the chargee/bank and not by the chargor/borrower. It was the chargee bank which was desirous of enforcing the security, which gave notice to exercise its power of sale and to take physical possession of the land and which took out the advertisement. The relationship is beyond that of a normal agency as between the donor of the power of attorney and the donee of the power of attorney. The donee/chargee as agent had used the authority under the PA not for the benefit of their principal, the donor/charger but for their own benefit to achieve the objective of the debenture arrangement. Therefore, such sale must be deemed to have been effected by the chargee rather than the charger. Legally, it ought to have been effected in accordance with the provisions of the NLC by judicial sale. Since the SPA was not a judicial sale, it was invalid.

22. It remains to be seen whether the Federal Court will agree *in toto* with the majority decision of the Court of Appeal, as we understand from the

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solicitors of the appellant in *Lim Eng Chuan* that the matter is now pending before the apex court.

ⁱ[1997] 2 MLJ 805

ⁱⁱ[2011] 1 AMR 44

ⁱⁱⁱ[2003] 2 MLJ 193

^{iv}[2005] 2 MLJ 201

^v The definition of 'debenture' by Chitty J in *Edmonds v Blaina Co (1887) 36 Ch.D 215* that 'the term itself imports a debt - an acknowledgment of a debt - and speaking of the numerous and various forms of instruments which have been called debentures without anyone being able to say the term is incorrectly used... (G)enerally, if not always, the instrument imports an obligation or covenant to pay. This obligation or covenant is in most cases at the present day accompanied by some charge or security.' has been applied in Malaysia, see *Bensa Sdn Bhd (in liquidation) v Malayan Banking Berhad & Anor* [1993] 1 MLJ 119.

^{vi}S.206(3) of the NLC provides that the provisions in the NLC requiring a dealing to be effected in the statutorily prescribed manner shall not affect the contractual operation of any transaction relating to alienated land or any interest thereon.

^{vii}S.223 of the Act provides that any disposition of the property of the company made after the commencement of the winding up by the Court shall unless the Court otherwise orders be void. S.219 of the Act provides that in a case other than one where a resolution has been passed by the company for voluntary winding up, the winding up shall be deemed to have commenced at the time of the presentation of the petition for the winding up.

^{viii}S.300(1) of the Act provides, among others, that all officers of a corporation are obliged to deliver up to the liquidator appointed by the Court all the moveable and immovable property of the corporation or all books and papers in his custody or under his control

^{ix}S.253 to s.269 of the NLC.

^xS.277(5) of the Act provides that the Court may require any...receiver,... agent or officer of the company to...deliver, convey, surrender or transfer to the liquidator...forthwith or within such time as the Court directs any money, property, books and papers in his hands to which the company is prima facie entitled.

^{xi}[1984] 1 MLJ 266

^{xii}[1998] 3 CLJ 874

^{xiii}[1998] 1 MLJ 1

^{xiv}The words in parenthesis are our addition. The said core question can be seen in paragraph [15] on page 53 of the judgment.

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