THE CHANGING TREND OF SCHEMES OF ARRANGEMENT AND APPROACHES TOWARDS ITS EFFICACY

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ABSTRACT

This article is an attempt to look into the distinct approach adopted by the Australian and English courts in light of the observations made by the Singapore Court of Appeal in the Oriental Insurance case on the issue of whether Scheme of arrangement derives its efficacy from statute or from an order of the court. It briefly outlines the latest developments in the use of Scheme and the reasons that added to growth of its use. The author compares the approaches using the case of extension of time and concludes by suggesting that the Australian approach can favour the growth in use of Scheme.

I. INTRODUCTION

A Scheme of Arrangement ('Scheme') is an arrangement between a company and either the holders of its securities or its creditors. This arrangement has to be approved by the court. Schemes of arrangement can achieve almost any required change and may be used when a re-organisation cannot be easily (or at all) achieved using other mechanisms;[2] an example being the acquisition of Corus Group by Tata Steel which was done by way of a scheme of arrangement in April, 2007.

Scheme of arrangement is of wide import and it can be used for restructuring a company when in debt or for restructuring a company's finance during solvency. But since the

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[2] G. EABORN, TAKEOVER LAW AND PRACTICE 474 (1ST EDN, 2005).

procedure requires Court approval and has to withstand the test of fairness and reasonableness in a Court of law, it has been regarded as 'unsafe' and 'tedious' in practice. Hence, despite being of wide import, in theory, the parties feared using it in commercial practice.

Traditionally, schemes have been viewed as inflexible, time-consuming and costly structures, relative to contractual offers, and on smaller deals the stamp duty saving may be outweighed by the extra cost associated with preparing the necessary documentation (which will be more extensive as compared to a contractual offer) and engaging counsel to assist with court procedures.[3] In recent years schemes of arrangement (as opposed to a more traditional takeover offer) have become the structure of choice for recommended bids.[4] Six of the last seven largest takeovers of UK targets, Scottish Power (11.6 billion), Alliance Boots (110.6 billion), Reuters Group (18.6 billion), Gallaher (17.5 billion), Corus (16.2 billion) and Hanson (16 billion)[5] have been carried out through Scheme.[6] The reason for this popularity depends in part on tax considerations, and also on the fact that a successful scheme assures the bidder of 100 per cent of the target's shares.[7]

The main impetus for use of Scheme has come from a shift in the attitude of the Courts. Courts have demonstrated a liberal view on many occasions having welcomed the market innovation in form of "hybrid" schemes. A hybrid scheme is one that contains both transfer, in respect of loan note elected shares, and reduction elements.[8] In the past, on a securities exchange offer, a scheme involving cash and non-cash consideration would be

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[3] P. Myners *"Smart Capital" European Edition Current Legal Issues for Investors in European Businesses*, No. 13, First Quarter (2008) at 2

[4] J. Payne, *Schemes of Arrangement, Takeovers and Minority Shareholder Protection,* LEGAL RESEARCH PAPER SERIES PAPER No 42/2010, May 2010.

[5] See *'London Scheming'* 26 INT'L FINANCE LAW REVIEW 46-49 (2007). For more details *available at* http://www.iflr.com/article/1977098/londons-scheming.html (accessed 15 August., 2009) [hereinafter 'London Scheming'].

[6] *Ibid.*

[7] P. Myners, *supra* note 4

[8] J. Payne, *supra* note 3

designed as a combination of a cancellation scheme and a transfer scheme.[9] This could be helpful to achieve a tax-neutral transaction for UK-tax paying target shareholders whilst structuring the acquisition of the remaining interest in the target as a cancellation scheme to benefit from the stamp duty saving.[10]

Another factor which has significantly contributed to this changing trend is the introduction of greater clarity within the UK legal regime relating to Schemes. In the UK, the development in the market practice was very informal until the Takeover Panel issued its consultation paper in the year 2007[11] further in year 2011, the Panel published "*Guidance Regarding the Publication and Implementation of Code Amendments*".[12] One of the purposes served by the Code is to bring a degree of certainty in the conduct of bids for the benefit of all shareholders.[13] In the spirit of this principle, the Panel has time and again made the provisions clearer and exhibited flexibility in interpreting provisions of the Code that are applicable to Scheme. In addition to the changes to the Takeover Code, new practice directions came into force on 1 October, 2007 and later in March 2011 with the aim of streamlining the court-based procedures applicable to Schemes.[14]

However, the tension between the Australian approach and the English approach and the recent observation by Singapore Court of Appeal in the case of *Oriental Insurance Co Ltd v Reliance National Asia Re Pte Ltd*[15] has spread a cloud of uncertainty on the future of Scheme. On the question whether Scheme derives its efficacy from statute or from an order of the court, both the countries have adopted a divergent approach. Australian

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[9] See http://www.cliffordchance.com/content/dam/cliffordchance/PDF/takeover_guide.pdf. (accessed 28 April, 2012).

[10] *Id.* However, it seems that the Hybrid Scheme is no longer used as it is now possible to use a cancellation scheme and obtain the related stamp duty saving, whilst still securing capital gains rollover relief for shareholders provided certain conditions are satisfied. For Further discussion, please see Takeover Guide, *supra* note 9.

[11] Please refer PCP2007/1

[12] Please refer PCP2011/1

[13] In Re Expro International Group plc, [2008] 11 EWHC (Ch) 1543 (Eng.), [hereinafter "In *Re Expro"*].

[14] *See* Practice Statement No.18, UK Takeover Code UK.

[15] Oriental Insurance Co Ltd v. Reliance National Asia Re Pte Ltd., [2008] 3 S.L.R. 121, [hereinafter "Oriental Insurance"].

courts favour the latter view. English courts, in contrast, take the position that a Scheme of arrangement which has been approved by the requisite majority of the company's creditors derives its efficacy from statute and therefore operates as a statutory contract.[16] This controversy as to whether a scheme of arrangement derives its efficacy from an order of court or from the statute has important ramifications for creditors. In particular, the issue is whether the court has the authority to grant a creditor an extension of time, after it has approved a scheme of arrangement, to file its proof of debt.[17] Hence, the distinction between the approaches adopted by the two legal systems becomes an important one as it hits the very premise of Schemes of arrangement which is to give flexibility to the creditors.

This article is an attempt to look into the distinct approach adopted by the Australian and English courts. Further, it will highlight the observation made by the Court of Appeal in *Oriental Insurance Co Ltd v Reliance National Asia Re Pte Ltd*.[18] The first part of this article will revisit the conventional view about the Scheme and list out reasons why it was not widely used until late. Further, it will briefly touch upon the latest developments in use of Scheme and the reasons that added to growth of its use. The second part of the article will focus on the distinct approach adopted by English and Australian Courts. It will also discuss briefly the approach adopted by Singapore Courts in the case of *Oriental Insurance* where the Singapore Court of Appeal favours the Australian approach. In the end, the article suggests why the Australian approach can favour growth in the use of Scheme. Commercial transactions require certainty and it will be in the interest of commerce that law bridges this gap to give efficacy to trans-border mergers and acquisitions that are happening using Schemes of arrangement.

II. CONVENTIONAL VIEW REGARDING SCHEME AND THE CHANGES THEREIN

[16] A. Hargovan, *The source of efficacy for creditors' schemes of arrangements in England, Australia and Singapore*, 31(7) COMPANY LAW 199-206 (2010).

[17] *Id.*

[18] Oriental Insurance, *supra* note 15

The development of Schemes of arrangements can be attributed to the "ingenuity of lawyers in adapting a procedure designed for a specific purpose to attain other purposes".[19] This observation, and the subsequent growth and adaptation of Schemes of arrangements to suit a multitude of purposes, is reinforced by Davies:[20]

> "The *scheme of arrangement is thus an immensely flexible instrument. However, because it is as much an instrument of insolvency law as of corporate law … the scheme of arrangement has a rather uncertain image. There can be almost as many types of schemes of arrangement as there are inventive corporate and insolvency lawyers, which indicates both the significance of the scheme procedure and the impossibility of identifying such a thing as a typical scheme of arrangement."*[21]

The Scheme in its traditional sense was characterised by a lack of familiarity and understanding which gave rise to certain negative perceptions such as it is more favourable to targets than to bidders because the target controls the process. In a merger where parties are equal, this provides a more favourable condition. This was perhaps the main reason that schemes of arrangement were not more widely used in corporate restructuring. Another concern about the Scheme was that irrevocable undertakings cannot be used on schemes[22] and hence Schemes were used only in highly leveraged deals. However, Scheme did not aid in cases there was a possibility of hostile takeover. In the case of a hostile bid, a bidder will opt for an offer rather than a scheme. In contrast to a takeover offer, there can therefore be no such thing as a hostile scheme of arrangement.[23] A scheme of arrangement requires a friendly target board in order to succeed.

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[19] R. AUSTIN & I. RAMSEY, FORD'S PRINCIPLES OF CORPORATIONS LAW 1207 (2005)
[20] P. DAVIES, GOWER AND DAVIES' PRINCIPLES OF MODERN COMPANY LAW 1082 (2008)
[21] *Id.*
[22] *Id.*
[23] P. Myners, *supra* note 4, at 5.

Despite the common origins for Schemes in the countries under discussion, UK, Australia and Singapore, the modern insolvency laws in each of these countries cast a different shadow on the commercial landscape.[24] Significant differences have emerged in law and practice which have led to a marked departure from the traditional view of the concept.

Companies in Singapore are reliant on Schemes of arrangements as a primary tool to rescue and rehabilitate financially distressed companies and favour this option over other alternatives, such as judicial management, for reasons discussed below.

In contrast to the current approach in Singapore and Hong Kong, creditors' schemes in Australia are generally less common since the introduction of voluntary administration as the primary corporate rescue vehicle a decade ago. Hence although Schemes of arrangement still exist in Australian corporate insolvency law, they are rarely used for corporate insolvencies[25] Notwithstanding the benefits[26] and successes of voluntary administration as a corporate rescue regime and the drawbacks of Schemes of arrangements,[27] Schemes still offer some advantages - the insolvency threshold is lower for schemes than for voluntary administration, they offer flexibility in design and a Scheme of arrangement is binding on all creditors once it is approved.[28]

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[24] Companies in Hong Kong, for example, use either schemes of arrangement or informal out-of-court corporate workout practices similar to the well-established "London Rules" pioneered by the Bank of England as an alternative to formal court-based corporate rescue.

[25] Schemes are still popular, though, for mergers and share capital reorganizations.

[26] CORPORATIONS AND MARKETS ADVISORY COMMITTEE, Report on Issues in External Administration 2008 at para.2.2.2, *available at http://www.camac.gov.au* (accessed 20 April, 2010). For a summary of some of the main differences between a creditors' Scheme of arrangement and a deed of a company arrangement under the voluntary administration provisions in Pt 5.3A of the Corporations Act 2001 (Cth), see *Re Pasminco Ltd*, [2002] 41 A.C.S.R. 511; City of Swan v. Lehman Brothers Australia Ltd., [2009] FCAFC 130. Also see AUSTRALIAN LAW REFORM COMMISSION, General insolvency Inquiry Report No. 45, 1988 [hereinafter "the Harmer Report"]. The Report stressed that voluntary administration should be a fast and efficient means to rescue a company or, alternatively, to maximise the value of the debtor company and thereby deliver greater benefits than an immediate liquidation. These goals are now reflected in the statute, section 435 A of the Corporations Act 2001 (Cth). For example, compared to schemes, voluntary administration has the advantage of not requiring court approval, which saves money and time.

[27] Schemes of arrangements are generally viewed as cumbersome, lengthy and expensive owing to statutory compliance obligations. *See* further, the Harmer Report, *supra* note 27 at 46.

[28] For a fuller discussion on a comparison between schemes and voluntary administration, *see* R. Langley, *The future role of creditors' schemes of arrangement in Australia after the rise of voluntary administrations* 27 COMPANY AND SECURITIES LAW JOURNAL 70 (2009).

In the UK, the City Code on Takeovers and Mergers has generally been lauded, by experts, as a system of self-regulation that offers the advantages of speed, flexibility and low cost administration.[29] It has answered the growing need of the commercial market with its flexibility towards interpreting provisions of the Code in case of Schemes. Andrew Watkins, a partner at the law firm Trowers & Hamlins, is of opinion that schemes had soared in popularity because their main disadvantage of having to wait for a court hearing had become less of a problem. He further opined that

> "*keen for the City of London to maintain its competitive advantage, the courts have become much better at fitting in scheme of arrangement hearings at short notice. Bidders, especially private equity buyers, may embrace schemes even more enthusiastically because the security of securing 100 per cent of the target should make banks more willing to lend.*"

It is seen that banks are reluctant to lend on a standard takeover offer if it risks acquiring only an 85 per cent holding. The certainty that Scheme offers in a corporate acquisition also allays a bank that otherwise may be hesitant to lend in case of takeover through contractual bid where exposure to risk is higher. In transactions where a colossal amount of money is involved, a takeover scheme helps in saving stamp duty which may be miniscule in terms of percentage but adds up to a huge amount in a large transaction.

Hence, the traditional opinion relating to Schemes of arrangement is, to a large extent, changing and it is gaining soaring popularity among the commercial parties across the aforementioned nations. The reasons for the same are, simply, that Scheme offers more certainty for effecting an acquisition, it also helps saving stamp duty which may be a colossal in cases of big transaction, and it grants lending banks, who are not very concerned about the process of control, the guarantee that the target security will be granted.[30]

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[29] For example, *see* B. HANNIGAN, COMPANY LAW 874 (2003)**;** P. DAVIES, GOWER AND DAVIES' COMPANY LAW 750 (2003)**.;** G. Morse, *Controlling Takeovers: The Self-Regulation Option in the United Kingdom*, JOURNAL OF BUSINESS LAW 58, 61 (1998); On the advantages offered by self-regulation in terms of expertise and cost, *see* A. Ogus, *Rethinking Self-Regulation*, 15(1) OXFORD JOURNAL OF LEGAL STUDIES 97, 97-8 (1995).

[30] *Supra* note 29.

In light of this renewed Scheme and the reasons for the same, the breadth of discretion enjoyed by the Court as to whether or not it should sanction a Scheme is important especially since, once the scheme has been sanctioned, it binds all parties, even the dissentients.[31] Drawing from this it is important to understand where Scheme derives its strength from. Is it the order of the Court or the Statute that gives the Scheme a binding effect? The question is pertinent as goes to the root of Scheme and determines whether a Scheme can be amended once court approves it.

III. THE ENGLISH APPROACH

In the case of *Kempe* v. *Ambassador and Co,*[32] the precise question before the court was whether the Scheme derives efficacy from the will of the Parliament or from order of the Court. The case involved a question of extension of time for filing a claim under a proposed scheme. The Privy Council rested its opinion in favour of the former view. This decision reversed the order of the Court of Appeal of Bermuda wherein the latter court had extended the time for filing the claim.[33]

The Privy Council adopted the position that a scheme of arrangement which has been approved by the requisite majority of the company's creditors derives its efficacy purely from statute and therefore operates as a statutory contract. Lord Hoffmann, on behalf of the Privy Council in *Kempe,* while assessing the nature of a scheme, reiterated that the requirement that the application should be "*in the manner provided by the Rules*" means only that the form of application should be in accordance with the Rules, it cannot mean that the application should be treated as if it was, for all purposes, an application to vary or reverse the decision of a liquidator."[34]

Disagreeing with the Australian approach, in the decision of the Supreme Court of

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[31] *Buckley* Vol 2 at para 425.53.
[32] [1998] 1 W.L.R. 27.
[33] *Id.*
[34] *Supra* note 29, at 276.

Western Australia in *Caratti* v. *Hillman*,[35] where the Court could extend any period prescribed by the Scheme under its power to extend periods fixed by its orders,[36] the English Court observed that though it is true that the sanction of the Court is necessary for the Scheme to become binding and that it takes effect when the order expressing that sanction is delivered, it is not enough to enable one to say that the Court has by its order made the Scheme. Further, the Court held that "*It is rather like saying that because royal assent is required for an Act of Parliament, a statute is an expression of the royal will*."[37]

As per the view of the court, it is the Statute which gives binding force to the Scheme, just as the rules of the Constitution give validity to Acts duly passed by the Queen in Parliament.[38]

This brings us to another important question on the role of the Court. Does the Court act as mere rubber stamp while sanctioning a scheme? The observation made by the English courts suggests that though the sanction of the Court is by no means a formality and that while giving its sanction, the Court has an inherent jurisdiction to correct any obvious mistakes in the document which sets out the scheme, it is beyond the powers of the Court to alter the substance of the Scheme and impose upon the creditors an arrangement to which they did not agree.[39]

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[35] [1974] W.A.R. 92. at 94 (Jackson C.J.). In this case, the scheme was " …*an integral part of the court's order*" and Burt J. said that " *the rights [under the scheme] are … in my opinion created by the order and the procedure whereby those rights are to be established or ascertained is a procedure whereby those rights are to be established or ascertained is a procedure which is also created by the order*."

[36] The case has since been followed at first instance in Australia and in Bond Corporation Holdings Ltd. v. State of Western Australia (No. 2), [1992] 7 W.A.R. 61, 68 at 95 (Anderson J.). The reasoning was said to be, that "*once the order is made, it is the order, ' speaking in terms of the scheme'*", *per* Caratti v. Hillman at 95 (Burt J.), "*that has effect, not the resolution of the creditors and not the statute*".

[37] *Supra* note 33.

[38] In Re Garner's Motors Ltd., [1937] Ch. 594, 598–599 and Devi v. People's Bank of Northern India Ltd. [1938] 4 All E.R. 337, 343.

[39] *Supra* note 38.

In *Kemp*, reliance was placed on the cases of *In re Garner's Motors, Limited*[40] ("*Re Garner's Motors*") and *Devi*[41] in support of the holding that a Scheme of arrangement derives its efficacy from Statute. In *Re Garner's Motors*, the question before the Court was whether a Scheme of arrangement entered into between a creditor and one of its joint and several debtors would discharge the liability of the other joint and several debtor. In answering the question in the negative, Crossman J considered "*that the effect of section 153 of the Companies Act, 1929 (c 23) (UK) is to give to a scheme when sanctioned by the Court under the section a statutory operation.*"[42] In the case of *Devi*,[43] the directors of an Indian bank ("the bank") purported to forfeit the appellants' shares in the bank by reason of the appellants' non-payment upon the bank's calls on these shares. The calls on the shares had been made via a resolution that was passed in complete ignorance of the terms of an amended Scheme of arrangement that had been approved by the court. The bank contended on appeal that the forfeitures had subsequently been ratified by the whole body of its creditors and shareholders. The Privy Council held that such forfeitures were *ultra vires* as a Court-approved scheme could not be amended or departed from by the mere acquiescence of the company's shareholders and creditors.

> "*Upon confirmation by the court of the amended scheme of arrangement, that scheme becomes binding upon the creditors, the shareholders and the bank alike and Its terms could thereafter only be varied by order of the court after the variation had been approved at meetings of the creditors and shareholders'.*" [44]

In contrast to Crossman J's judgment in *Re Garner's Motors* it would appear that the obiter in *Devi* does not quite support Lord Hoffmann's holding in *Kempe* that a Scheme of arrangement derives its efficacy from the Statute, although it emphasises the corollary that a court-approved Scheme is binding on all parties to the Scheme. However, English

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[40] [1937] Ch 594.

[41]. Devi v. People's Bank of Northern India Ltd. [1938] 4 All E.R. 337, 343.

[42] *Supra* note 27 at 598–599. Please note that it was subsequently cited by Lord Hoffmann in *Kempe* at 276.

[43] *Supra* note 28.

[44] As *per* Lord Romer at 343, in a passage which was subsequently relied upon by Lord Hoffmann in *Kempe* at 276.

work published before the decision of the Privy Council in *Kempe,*[45] cites the two cases of *Re Garner's Motors* and *Devi* as authority for the proposition that the effect of the Court's approval of a scheme of arrangement *founded originally in contract, becomes statutory* and thus cannot be altered by contractual agreement, other than by a supplementary Scheme sanctioned by the Court.

It is submitted that it appears that, to date, the question of the Court's jurisdiction to extend the time for filing proofs of debt in respect of a court-approved Scheme has not directly arisen for consideration in England either before or after the Privy Council's decision in *Kempe*. *Kempe* has been followed by the Hong Kong courts in two cases, *viz*, *Re Universal Dockyard Ltd* [46]and *Re UDL Holdings Ltd*[47] . In both the cases, the Hong Kong High Court simply unquestioningly accepted the holding in *Kempe* as correct, and no (or little) comments were made in relation to Lord Hoffmann's judgment.[48] *Kempe* is also cited by the learned authors of *Buckley*[49] to the effect that a scheme does not operate as an agreement between the parties affected but *it has binding force by virtue of statute* once an application to the court has been made and the consent of the relevant parties and the sanction of the court [have] been obtained.[50] It comes into effect as a result of the application to the court by the appropriate persons, approval by the court and the court order. It is *not* proper to say that it is *solely* the order that makes the scheme.

To conclude, in England, once a Scheme of arrangement has been approved and sanctioned by the court, it means that the court ordinarily has no jurisdiction to make any substantive alterations to the Scheme, save in limited circumstances and hence the Scheme is said to derive its legitimacy from Statute. The English position has far-reaching implications in commercial practice for creditors. The practical effect of the decision in *Kempe* is to preclude the court's jurisdiction to extend the time for creditors to

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[45] D. Brown, CORPORATE RESCUE: INSOLVENCY LAW IN PRACTICE (1996) at para 18.54.

[46] [2003] 3 HKEC 893.

[47] [2006] 3 HKLRD 84.

[48] See Re Universal Dockyard Ltd., *supra* note 46 at 20 and Re UDL Holdings Ltd., *supra* note 47 at 58.

[49] *Buckley* Vol 2, para 425.64

[50] Gore-Browne has reiterated a similar proposition in his treatise on company law. *See* GORE BROWNE ON COMPANIES VOLUME 2 (2005) at para 46.

file their proofs of debt pursuant to the Scheme. This will be discussed in later part of the article.

IV. THE AUSTRALIAN APPROACH

Contrary to the approach taken by the Privy Council in *Kempe*, the Australian Courts have consistently taken the position that once a Scheme of arrangement is approved by the Court, it becomes an order of Court, and thus, the statutory provisions on civil procedure (the Rules of Court, in our local context) permit the court to grant an extension of time for, *inter alia*, a creditor to file its proof of debt.

The judicial reasoning in *Kempe* was rejected in Australia, countered by Justice Santow of the Supreme Court of New South Wales in *Matine Ltd, Re*[51] where he vehemently held that the reasoning in *Kempe* would produce incongruous consequences. Drawing an analogy from the logical conclusions, he observed that the fact that the Court's jurisdiction being conferred by statute does not make the decisions of the court under the statutory jurisdiction any less 'orders of the court' that others as they deriving their efficacy from being made by court in the first place.[52] He observed that even if the statute is regarded as an indispensable prerequisite to determine the jurisdiction of court, it is, in causative terms, merely a 'background' fact behind that efficacy. He further went on to note that a contrary view will be

> *"like saying that the birth of Lee Harvey Oswald 'caused' the death of President Kennedy*."[53]

It is submitted that if a Court loses all jurisdiction in respect of a Scheme of arrangement once it has sanctioned the Scheme (subject to limited exceptions), it will raise doubts on the appellate jurisdiction exercised by the Court as suggested in *Kempe.* Justice Santow viewed the reasoning of the Privy Council in *Kempe* as "attackable" and, in his Honour's

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[51] Re Matine Ltd, (1998) 28 A.C.S.R. 268; this passage was cited with approval by Santow J. in Re AGL Gas Networks Ltd (2001) 37 A.C.S.R. 441 at 446.

[52] *Id*

[53] *Supra* note 51.

opinion, "vulnerable"[54] due to the reason that the Court in *Kempe* proceeded on the assumption that a Scheme does not derive its efficacy from the order of a Court and did not indicate where the Court obtains jurisdiction to exercise the function conferred.[55]

There is a line of Australian authorities that consistently establish that an approved Scheme derives its force from the Court order, not from the antecedent resolutions of members and creditors.[56] In *Re AGL Gas Networks Ltd*[57] (hereinafter "*Re AGL Gas Networks"*) Santow J[58] elaborated further on the Australian approach and carefully explained why the approach in *Kempe* should not be followed. He submitted that in *Australia, the authorities* such as *Hill v Anderson Meat Industries Ltd*,[59] *Caratti*[60] and *Bond Corp Holdings Ltd v Western Australia*[61] establish that an approved Scheme does indeed derive its force from the court order and not from the antecedent resolutions of members and creditors[62]. Further, Street J observed in relation to a creditor's Scheme that

> "*the approval by the court of the scheme amounts to a discharge of the debtor company's liability by operation of law which is effected by the court order and not by the events antecedent thereto though these antecedent events are indispensable statutory prerequisites of the court's jurisdiction to make an order approving a scheme and thus rendering it binding on the company and on the creditors*."[63]

The effect of the Australian authorities is that, once approved, there is no Scheme separate from the order of the Court. Rather, any Scheme in the sense of a proposal

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[54] *Supra* note 51.
[55] *Supra* note 49.
[56] Western Australia (No.2), [1992] 7 W.A.R. 61; AGL Gasworks, [2001] 37 A.C.S.R. 441; cf. dicta of Austin J. in Ray Brooks Pty Ltd. v. New South Wales Grain Board (No.2) [2002] 43 A.C.S.R. 657 where his Honour expressed preference for the English approach in *Kempe* but felt constrained by the weight of the Australian authorities to the contrary.
[57] [2001] 37 ACSR 441. *Caratti* was subsequently followed by the Supreme Court of New South Wales' decision in *Re AGL Gas Networks*.
58 See *Re AGL Gas Networks*, *ibid.* at 46–47.
[59] [1971] 1 NSWLR 868.
[60] *Supra* note 56.
[61] [1992] 7 ACSR 472.
[62] *Supra* note 50.
[63] *Hill*, *supra* note 59 at 877.

decided at the relevant meeting is subsumed into and by the order of the Court.[64]fn44 It follows therefore that a Scheme, and its consequential steps, can be saved in Australia from the consequences of an accidental non-fulfilment of a condition precedent with the aid of the Rules of Court.

V. APPROACH FOLLOWED BY THE SINGAPORE COURTS- ORIENTAL INSURANCE CASE

In *Oriental Insurance*,[65] the central issue that fell for determination was whether a company that failed to file its proof of debt in time under a Scheme of arrangement could be granted an extension of time for filing. In this part, the focus will be upon approach taken by the Singapore Court of Appeal on the question of whether scheme derives efficacy from the crown or the court. In resolving this issue, it was imperative for the Court of Appeal to examine the nature of Schemes of arrangement and, more relevantly, its source of efficacy. The Singapore High Court considered the legal controversy in Australia and England as to the nature of Schemes of arrangement and, upon evaluation of the conflicting legal principles in this area as discussed earlier, relied upon the English approach in *Kempe* and dismissed the application by Oriental Insurance.

The Court of Appeal in *Oriental Insurance* reversed the decision of the High Court and favoured the Australian position that views Schemes as essentially orders of Court and held:

> "*We are of the view that the Australian approach is also consistent with these established principles [relating to the purpose of schemes of arrangement and legal principles surrounding their operation*."[66]

Further, the Court of Appeal held that adopting the Australian approach does not necessarily mean that clarity, certainty and finality would be sacrificed at the altar of expediency or that the objectives of section 210 can no longer be properly achieved.

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64 *AGL Gas Networks*, *supra* note 57 at 46.
65 *Oriental Insurance*, *supra* note 15.
66 *Oriental Insurance*, *supra* note 15 at 61.

Between the English and Australian approaches, the former approach appeared to be unnecessarily strict and mechanical, leading perhaps to potentially unjust consequences in some instances.

The Court placed reliance on the critique of the judicial reasoning in *Kempe* expressed by Justice Santow in *Matine Ltd, Re*,[67] and reinforced in *AGL Gas Networks, Re*,[68] that it would produce "*incongruous consequences*" should the precedent in *Kempe* be followed. Delivering a judgment on behalf of the Court of Appeal while drawing support from the judicial criticism directed to *Kempe* in the Australian authorities,[69] Justice Rajah held that the analogy of royal assent given by the Privy Council in *Kempe* (to support its holding that a scheme derived its efficacy from statute) was unmeritorious for the reasons[70] that such analogy is apt only if the Court's sanction of a Scheme is regarded as a *mere formality* like the royal assent required for UK Acts.

It is submitted that both English cases as well as precedent in Singapore have established that the court's sanction is not just a formality and that the court, in fact, has a crucial role to play in deciding whether a scheme is to be approved. It is worth noting that even in the UK, the Courts have increasingly sought to facilitate changes to Schemes where they reflect or assist offers clearly in the interests of shareholders.[71]

VI. COMPARING APPROACHES - THE CASE OF EXTENSION OF TIME

In light of the above, we will examine the issue of whether extension of time is permissible once the Scheme is approved. Considering the character of Scheme as a flexible tool of corporate restructuring, and its recent growth as discussed, it will be logical as well as in interest of commerce that the flexibility of Scheme must be maintained and Courts should not adopt a hyper technical approach.

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[67] (1998) 28 A.C.S.R. 268.

[68] *AGL Gas Networks*, supra note 15 at 46.

[69] *See Hill*, *supra* note 59; *Caratti*, *supra* note 60; *Bond*, *supra* note 61; *Re AGL Gas Networks*, *supra* note 57; *Ray Brooks*, *supra* note 56.

[70] *Oriental Insurance*, *supra* note 15 at 63

[71] *Re Allied Domecq*, [2000] 1 BCLC 134.

It is submitted that if we adopt the English approach that Scheme derives efficacy from Statute, any such extension will not be permissible. The Australian approach which purports that Scheme derives efficacy from the Court order can allow extension of time where the facts of the case so warrant.

On the precise question of whether the time limits in the Scheme are fixed or flexible, the English Court opined that it is one of substance. The argument was that if the Court has the jurisdiction to enlarge the period for filing an appeal against the rejection of a claim, it must also have the jurisdiction to extend the final filing deadline for the original claims. Having held that a Scheme of arrangement derived its efficacy from the Statute and not from the Court order sanctioning the Scheme, Lord Hoffmann went on to hold[72] that it was not open to a Court to extend the time limits laid down in a Scheme as this would be a *material alteration* that would detract from certainty and expedition, which were the chief objects of any scheme:[73]

> *"It is of course true that the sanction of the court is by no means a formality. Furthermore, in giving its sanction, the court has an inherent jurisdiction to correct any obvious mistakes in the document which sets out the scheme. But it cannot alter the substance of the scheme and impose upon the creditors an arrangement to which they did not agree. The question of whether the time limits in the scheme are fixed or flexible is in their Lordship's opinion one of substance".*

However, in *Caratti v Hillman*,[74] the Full Court of the Supreme Court of Western Australia took the view that the procedure leading to the extinguishment of rights of creditors through a Scheme under companies' legislation was a procedure created by an order of the Court. The Court order approving the Scheme fixed the period within which a creditor was authorised to lodge a claim. Consequently, the Court held that the Rule of

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[72] *Kempe*, *supra* note 32 at 296.
[73] *Kempe*, *supra* note 32 at 297.
[74] *See Caratti*, *supra* note 60.

Court was available to allow the Court to extend the period for lodgement of claims by creditors.

The Trial Judge[75] in the case of *Oriental Insurance*, in Singapore, held that there would be serious repercussions if creditors' were allowed the extension of time. According to him, such an approach would be detrimental for future Schemes of arrangement as certainty, efficacy and finality of Schemes would be severely compromised. However the Singapore Court of Appeal[76] rejected the view that an extension of time in respect of a Court approved Scheme is a matter of substance or materiality of the commercial decision of the Scheme.[77] Having determined the threshold question, it followed that the Court was empowered by the relevant Rule of Court to grant an extension to a creditor to file its proof of debt.

On the question of whether judicial discretion should be exercised in favour of the creditor,[78] the Singapore Court of Appeal was satisfied that the extended timeline would not cause prejudice to Reliance, the defendants, or the other creditors. The fact that it was a solvent Scheme aided this conclusion. On the contrary, it was held that failure to grant Oriental Insurance an extended deadline would severely prejudice the creditor.[79] Turning attention to the reason for the application, the court was satisfied that the present case was not one of patent oversight. Rather, the delay was viewed to have been "*a slip between the cup and the lip*"[80] on Oriental's part which was viewed with a degree of leniency. Accordingly, Oriental Insurance was granted an extension of time.[81]

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[75] *Oriental Insurance*, *supra* note 15 at 25.

[76] *Oriental Insurance*, *supra* note 15 at 25.

[77] *Oriental Insurance*, *supra* note 15 at 65.

[78] Determination of this question was dependent on two main factors identified by the court--namely, whether any prejudice would be caused to other parties to the scheme; and the reason behind the party seeking an extension of time.

[79] *Oriental Insurance*, *supra* note 15 at 84.

[80] *Oriental Insurance*, *supra* note 15 at 91.

[81] The Court of Appeal also held that section 392(4)(d) of the Companies Act (Cap 50, 2006, Singapore) was available to extend the time to submit a proof of debt if it could be shown that there was no "*substantial injustice*" to the parties.

Thus it can be safely submitted that the Singapore Court of Appeal had reasoned that the English approach will invariably mean that once the Court has approved a Scheme of arrangement, it no longer has jurisdiction to grant an extension of time for a creditor to file its proof of debts in respect of that Scheme *regardless* of the circumstances, save in cases of "*obvious mistakes in the document which sets out the scheme*"[82] or where consent to the Scheme was obtained by fraud.[83]

It is submitted that the English approach is intuitively restrictive as even in a situation where the failure to file a claim in time is not in any way attributable to the fault of the creditor and where allowing the creditor an extension of time to file its claim does not prejudice any of the parties, an extension of time cannot be granted unless there is an obvious mistake in the documents setting out the scheme or no fraud.

In my submission, the facts of *Kemp* warranted the application of a strict approach as the Privy Council had found, as a *fact*, that it was a "*principal feature"* of the Scheme in question to impose a strict deadline for filing claims, after which creditors would be altogether barred from participating in the liquidation. However, the same cannot be said for all other Schemes of arrangement without such a feature. Hence a blanket method of adopting the English approach as a general principle will lead to incongruous results. Further, courts should not be reluctant to abdicate the powers given to them by Statute (Companies Act) *vis-à-vis* Schemes of arrangement, especially when doing so would allow an injustice to stand.

The court in *Oriental* in its obiter noted that the Privy Council in *Kempe* did not consider this point carefully, but merely accepted it as a valid assumption. In contrast to cases like *Devi , British and Commonwealth Holdings plc , Eltraco* and *Chew Eu Hock,* all of which support the English approach, where the creditors in question (or, on the facts of *Devi*, the directors of the debtor company) sought to amend or object to the substantive terms of a Court-approved Scheme such that they were, in fact, trying to *resile* from the original

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[82] *Kempe, supra* note 32 at 276.

[83] *Fletcher* v. *Royal Automobile Club Ltd.*, [2000] 1 BCLC 331 (CA)

scheme which had been agreed to by the requisite majority of supporting creditors and sanctioned by the court, the applicant in an extension of time case is usually not trying to substantially amend or resile from the scheme that it has entered into. It must be noted that the purpose of seeking extension of time laid down in the scheme is in tune with the purpose of participating in the Scheme. It appears that the significance of this distinction was also, at least partially, appreciated by the High Court Judge in the *Oriental* case, where she noted that:

> "*While the applicant in the Oriental did not seek to amend the scheme, in my view, the principles governing this issue are important as they form another part of the framework in which the issue should be analysed*." [84]

A better view, perhaps, is to treat an extension of time in respect of a Court-approved Scheme simply as a matter of *procedure*, rather than as a matter going to the substance or materiality of the commercial dimension of the Scheme (an amendment of the latter nature would entail seeking the views of all the parties bound by the scheme).[85] If the view that an extension of time is usually a matter of procedure is accepted, then the grant of an extension of time will not be seen as detracting from the established principle that a Court-approved Scheme should not be altered in substance.

Thus we see that The Rules of Court in Australia[86] and Singapore[87] enable the Court, by order, to extend any time fixed by any judgment or order. The Rules of Court impact the operation of a Scheme of arrangement in the following way - if a Scheme of arrangement is said to derive its efficacy from the order of the Court approving the Scheme, then it stands to reason that a court has inherent jurisdiction to vary its own orders.

Viewed in this light, the Australian approach is in no way inconsistent with the established principles relating to Schemes of arrangement, and also gives due consideration to the overarching need for clarity, certainty and finality in this area of

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[84] *Re Reliance National Asia Re Pte Ltd,* [2008] 1 SLR 569.
[85] *Oriental Insurance*, *supra* note 15.
[86] Pt. 2 r.3, Supreme Court Rules
[87] Ord.3 r.4, Rules of Court (Cap 322, R 5, 2006 Rev Ed).

law.[88] Further, a Court order is in no way less binding than a statutory contract on the parties to a Scheme of arrangement, and it is trite law as well as common sense that a Court order cannot be altered at will by the parties who are subject to it.[89]

VI. CONCLUSION

Considering the increased use of Scheme in corporate restructuring and growth of financial markets, it is submitted that a hypertechnical approach should not be adopted. Such an approach will be prejudicial to the interest of commerce as well as contrary to the essence of Schemes of arrangement. Scheme has been considered as an immensely flexible tool and the word 'arrangement' is of wide import.

On the question whether Scheme derives its efficacy from Stature or Court order it may be noted that, if a Scheme of arrangement is said to derive its efficacy purely from Statute, then it stands to reason that it operates as a statutory contract and this effectively restricts the court's ability to order rectification to a very limited set of circumstances which precludes an extension of time for a creditor to file a proof of debt after the court has approved a scheme of arrangement. Thus answer to this question has given rise to judicial tension in England and Australia and lacks a uniform approach.

The English approach in *Kempe,* wherein Lord Hoffmann referred to *Caratti* and expressly disagreed with it, is clearly at odds with the Australian approach. The competing points of view on the nature of Schemes of arrangement was addressed by the Court of Appeal in Singapore recently in *Oriental Insurance* and resolved in favour of the Australian view. It is submitted that the Singapore Court of Appeal did not take the view that the English approach was wrong; rather, decided that "*the Australian position was more persuasive*."

The question of whether the court has jurisdiction to extend time in respect of a Court-

[88] *Oriental Insurance*, *supra* note 15 at para 66.
[89] *Oriental Insurance*, *supra* note 15 at para 66.

approved Scheme is essentially a question of discretion, and invariably requires a judge to take a considered view on what best accords commercial certainty and fairness in this area of the law. There are real practical conundrums with the strict English approach, and the reasoning in *Kempe* poses a perennial threat.

Adopting the Australian approach does not necessarily entail sacrificing clarity, certainty and finality. In fact, the Australian approach mitigates some of the injustice that may potentially result under the English approach. It also gives due consideration to the established principles relating to Schemes of arrangement while meeting, at the same time, the objectives of the legislative framework governing such Schemes. The Australian approach meets the underlying legislative intent and the policy and the objectives of section 210 of the Companies Act. If the Australian approach is adopted, the question of commercial uncertainty is ruled out as any Court order, once finalised, can only be amended in very limited circumstances, and any application to amend a court order would be subject to due process. It follows from the binding nature of a Court order that the Australian approach can also achieve the legislative intent that Schemes of arrangement should function as machinery to overcome the impossibility of attaining absolute consensus from all the company's creditors or members on a proposed scheme and to bind minority dissentients to the scheme.

Further, the Australian approach will have the added advantages of avoiding a strained construction of the plain wording of section 210(3) of the Companies Act, which, suggests that a scheme of arrangement is made binding only upon its approval by the Court.[90] It will also avoid the unfairness or injustice which may potentially be caused to an innocent creditor who is not to be blamed for its failure to file its proof of debt in time.

There is also no reason why the Australian approach cannot embrace the legal concept that a Scheme of arrangement which is approved by *all* the creditors of a company "*is wholly a contractual scheme*".[91] The Court order sanctioning such a scheme can be seen,

[90] *Oriental Insurance*, *supra* note 15 at para 68.
[91] *Oriental Insurance*, *supra* note 15 at para 77.

in essence, as a *consensual order*. The sanctity of contract which lies at the heart of a Scheme that has been duly approved by the company's creditors or members is preserved if the Australian approach is followed.

The increase in use of Scheme is a reflection of the market's acceptance that the advantages now outweigh the disadvantages due to Court practice in recent years. However, it remains uncertain whether the distinction in approach stated above will jeopardise the future of Scheme of arrangement or whether this can be resolved without much ado. It remains to be seen if Scheme is here to stay.