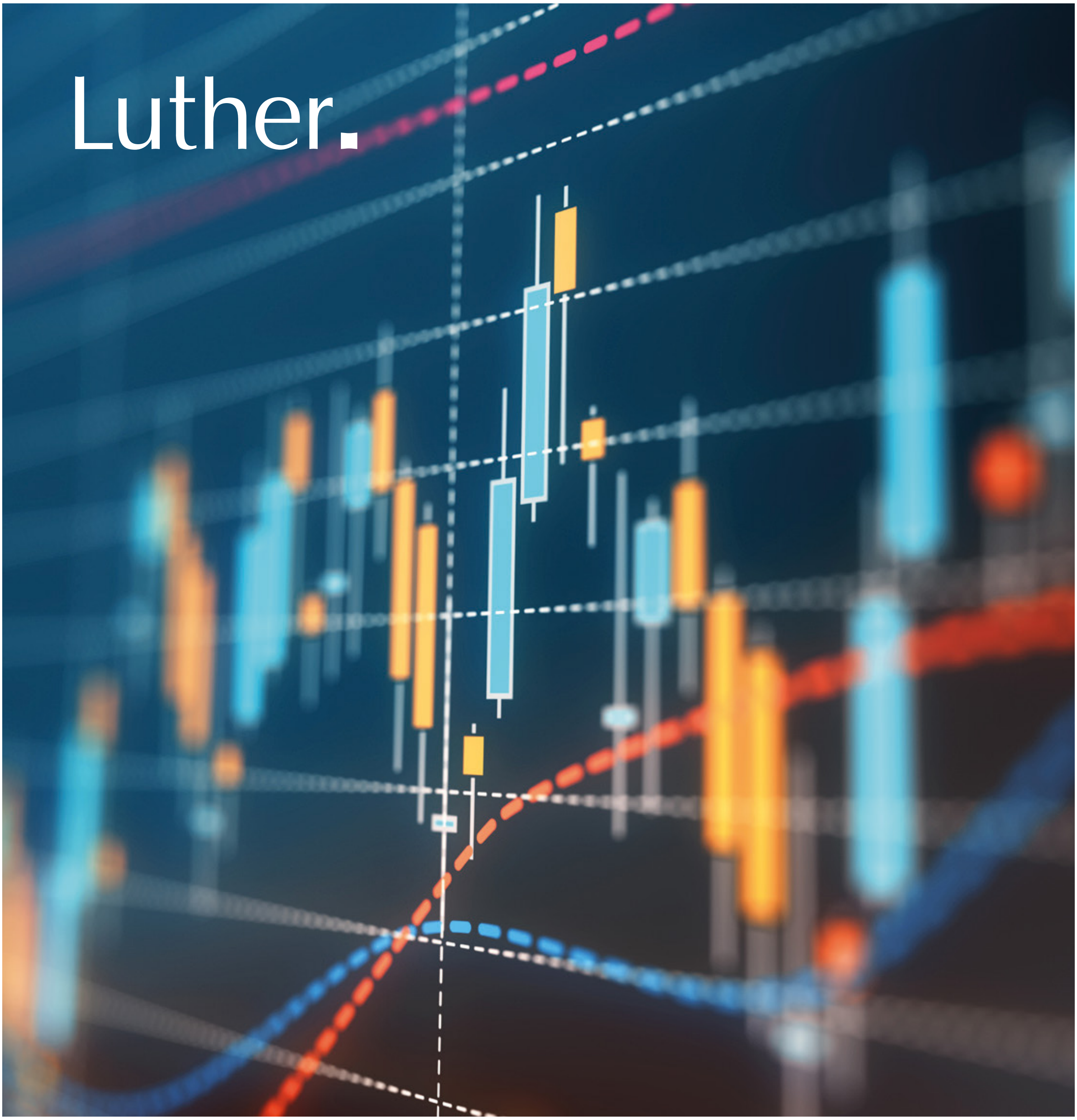

Special Situations and Distressed M&A – Southeast Asia

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Introduction

Challenging times come with great uncertainty – but also great opportunity. After the abrupt end of the recent bull market caused by the COVID-19 pandemic, a new wave of business consolidations and acquisitions may follow at valuations the market has not seen for a decade. Applications are myriad: Financially resilient strategic investors looking to secure their supply chains and distribution channels, a buy-out of cash-strapped joint venture partners or a step-up of venture capital and private equity investments getting "dry powder" to work – all of them potentially involving distressed target companies.

Investing in such special situations poses complex challenges and hurdles. Both can be overcome with proper transaction structuring and adequate mitigation measures. A fast reaction time is of paramount importance since distressed transactions are driven by considerable timing constraints.

The aim of this client briefing is to bring its reader up-to-speed on the major points that are to be expected in special situations and distressed M&A. We will start with a general section covering topics that emerge in every such scenario. The general section is followed by different country-parts for Indonesia, Malaysia, Myanmar, Singapore and Thailand covering legal obstacles and potential pitfalls that need to be addressed accordingly.

Who we are

Combining international outlook with local expertise, we are not your average legal advisor. We rather think of ourselves as your partner, sharing your passion and vision.

We are constantly engaged in complex and challenging transactions, helping to shape the legal standards in the region. Our lawyers have decades of experience in the relevant markets. Our advice is commercially minded, taking into account the strategic background and other economic parameters of an M&A deal. Never losing sight of the important points and without getting caught up in formalities and "lawyer-talk".

Lawyers and tax advisors

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Locations

20

Long-standing connections to commercial law firms worldwide

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General transactional matters

Level of distress

As a first step, purchasers should verify and analyse the level of distress of the target company: Did formal insolvency proceedings commence or were related petitions handed in? Were receivers, administrators or judicial managers appointed? If so, there is obviously a change in control over the process of sale from the board of directors to the relevant appointee. Consequently, purchasers need to make sure that they are dealing with the right representatives and stakeholders and modify their strategy as and if required. Buying-out of formal insolvency proceedings may have greater deal-certainty: The risks of challenges of a distressed transaction are more remote given formalised sale procedures and, if applicable, court and creditors' sanctioning.

NB: In the vast majority of jurisdictions we are active in, mitigating measures were introduced as a response to the COVID-19 pandemic also covering insolvency-related topics. These measures range from interim moratoria for the filing of insolvency-related petitions, the increase of monetary thresholds for such petitions, additional protection for directors of distressed companies etc.

Transaction structuring

As in every M&A deal, a decision needs to be taken at the outset whether the distressed transaction should be implemented as a share deal or an asset deal: Asset deals provide a purchaser with the possibility of "cherry-picking" assets and shielding-against certain liabilities of a seller. Share deals are easier to execute as there is less complexity in the transaction documentation and few or no third party consents. Obviously, in distressed transactions, asset deals are more common and usually the preferred option; share deals have limited applicability.

NB: In certain jurisdictions specific liabilities are transferred *ex lege* to a purchaser in an asset sale in case such asset sale qualifies as a transfer of business on a going concern basis. This needs to be closely analysed and monitored to avoid any unpleasant surprises post-closing.

What has gained more momentum in recent years are "loan-to-own" transactions: As the term suggests, it is a strategy to convert debt of the target company into equity of the target company. There are various ways to implement this, such as purchasing existing (secured) debt below par or advancing new debt to the target company linked with an equity issuance. Loan-to-own transactions can be handled both consensually or non-consensually, the latter involving formal restructuring procedures.

Due diligence and deal management

Distressed transactions are conducted under significant time pressure and usually signed and closed within a matter of weeks rather than a matter of months. Access to information and documents may be limited. Deal parties need to strike a clear balance between the level of due diligence they are comfortable with in order to go ahead with the deal and the kinds of information which can be considered as non-essential. Purchasers should not underestimate the possibility of a seller not being willingly selling, but being instead compelled to sell because of financial constraints and pressure from lenders. This impacts the level of collaboration on seller's side in procuring the required due diligence information.

As outlined above, mitigating factors for lack of due diligence work can be put in place if the distressed transaction is adequately structured. However, contractual protection in form of indemnities or representation and warranties in a distressed transaction is limited, in particular when buying out insolvency proceedings. The official insolvency administrator will propose the contractual terms with limited room for manoeuvre. The target company or its assets are usually purchased on an "as-is" basis with no escrow or other holdback rights. Associated risks will need to be captured mostly in pricing.

A purchaser should be mindful that the interests of various stakeholders need to be aligned and managed. Senior lenders, junior lenders and secured lenders may all have different views as to asset realisations.

W&I insurance as potential mitigating factor?

In our experience, the willingness of a W&I (warranty & indemnity) insurance provider to underwrite a transactions hinges on the quality and quantity of the due diligence conducted by a purchaser. In case there is not sufficient time for a market-standard due diligence, hardly any W&I insurance provider will be willing to shoulder the risk. Deal parties should expect difficulties in obtaining cover under a W&I policy since the available deal time in distressed transactions is massively shortened and processes significantly accelerated.

<u>NB:</u> Any liability for voidance of transactions due to specific insolvency claw-back rules (such as transactions at an undervalue, unfair preference etc) is a standard carve-out in W&I policies. For the sake of completeness, deal parties should also expect that any COVID-19 related losses will be carved-out from W&I policies.

One of the latest developments in the W&I insurance market are “synthetic” W&I policies: The seller does not give, or gives only very limited, representations and warranties to the purchaser in the transaction documents. Rather, the purchaser agrees to a set of representations and warranties with the W&I insurer in the W&I policy. To our knowledge, synthetic W&I policies have so far not been explored in Southeast Asia. It will be interesting to see on how this concept develops and whether it will be applied in distressed transactions in the future.

Other considerations

In most jurisdictions there are no general exemption for distressed transactions in terms of regulatory approvals, such as merger control or restrictions on foreign ownership. Deal parties need to take this into account when planning for the viability of a distressed transaction and timelines.

Indonesia

Indonesia is a civil law country by tradition, with its legal system being based on Dutch colonial laws. Its corporate legal system as well as the respective registries are basic and do not recognise many modern corporate legal instruments. While these circumstances can make M&A deals challenging in Indonesia, its vast market and high growth rates make it one of the most attractive target markets. Prioritising and timing of the right aspects from the start is paramount.

Considerations for distressed transactions

For distressed transactions, the following points are noteworthy in our view:

Clean sales

Creditors as well as receivers in insolvency proceedings have the right to challenge prior transactions entered into by a company by way of an *actio pauliana*. The claim must be based on the presumption that the transaction was carried out to the disadvantage of creditors without immediate contractual obligations and with the actual or perceived knowledge by the company of the disadvantage it causes to its creditors. Deal parties should anticipate such actions by creditors in relation to transactions which are perceived as detrimental to their position. This needs to be kept in mind in order to achieve a clean sale.

Directors of a distressed company

Under Indonesian law, members of the board of directors may be held personally liable for debts and other liabilities of an insolvent company if the insolvency is caused by their fault or negligence. Additional safeguards and precautions should be taken in order to shield the directors from any such liability.

Corporate restructuring mechanisms

Alternatively to a mere receivership, in which a receiver appointed by the commercial court carries out the liquidation of the respective company, the commercial court can grant a suspension of debt payment obligations (*Penundaan Kewajiban Pembayaran Utang*, “PKPU”). A PKPU is a court supervised debt restructuring process involving a court appointed administrator with the aim of avoiding insolvency proceedings. The composition plan made by the administrator is subject to creditors’ approval and may include an option of third party investment. It is therefore advisable to maintain close contact with potential target companies in order to have the option to influence potential composition plans.

Declaration of insolvency

Companies in Indonesia are generally unlikely to declare insolvency in time. It is therefore vital to evaluate the situation of a target company at the outset of a distressed transaction in order to avoid situations in which a mandatory involvement of authorities and creditors is overlooked.

Valuation topics

The valuation of a target company in a distressed transaction typically leads to discrepancies in the purchase price and the nominal share value. Tax authorities have an option to apply their own valuation where they suspect wrongful undervaluation. The assistance of independent appraisers as well as documentary evidence of the parameters leading to the agreed consideration are essential for discussions in this context.

Country-specific deal points

Shareholding requirements

Indonesian corporate law requires a minimum of two share-holders in a limited liability company in order to maintain its liability limitation. Since shareholders have a statutory pre-emptive right regarding share transfers and increases in share capital, the involvement of all parties in the pre-negotiation phase is essential. A unilateral "squeezing out" of shareholders is not feasible under Indonesian law.

NB: The level of protection of shareholder's rights, especially those of minority shareholders, is comparatively high.

Foreign ownership restrictions

Foreign ownership in Indonesian companies is often capped due to investment restrictions. The maximum ownership ratio a foreigner is entitled to depends on the activity of the target company and the sector it is active in. This needs to be taken into account in structuring of the M&A deal.

Notification requirements

A change of control by way of a transfer of shares or a capital increase requires pre-notification to the employees of the target company (by direct communication) as well as its potential creditors (by publication in a national newspaper) at least 30 days prior to closing. Where the transaction structure makes these notifications necessary, it is crucial to arrive at an agreement on the points that need to be communicated early on in order to avoid spending additional time awaiting the expiry of notification periods.

Due diligence

Expired business as well as technical licenses and inconsistencies in corporate documentation often lead to considerable timing issues if not identified at an early stage. Pending legal proceedings, clarifications on real property as well as collateralised moveable property can only be independently verified by manual searches at the respective courts and registers.

Also the quality of financial information provided by a target company might not meet international standards: Indonesia has not adopted IFRS for reporting by domestic companies and only partially converged its national standards towards IFRS. There is no general audit requirement. Further, it is not uncommon that companies falsely report to tax authorities not least due to irrational approaches by the latter in terms of expected profits. Findings in this regard together with tax liabilities (see below) are the most common reason that may make an asset deal the more suitable option for transactions as specific liabilities can be carved-out.

Tax liabilities

Tax liabilities pose the most common reason for deferred consideration payments in Indonesia. A thorough look into the tax history of a target company is essential in order to assess this risk. The fact that many companies made use of the so-called "Tax Amnesty" in the past does not necessarily simplify these matters. The effect of the amnesty is bound to a high amount of accuracy during its declaration, as well as strict reporting requirements in the years following it.

Luther in Indonesia

We collaborate with Maqdir Ismail & Partners in Jakarta, Indonesia since many years. Our foreign lawyers in Indonesia speak Bahasa Indonesia and have constantly been seconded to Maqdir Ismail & Partners to consult clients in Indonesia while relying on the local expertise of our colleagues.

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Malaysia

Malaysia continues to go from strength to strength as an economic powerhouse in Southeast Asia. Ranked 12th in the World Bank's Ease of Doing Business Ranking of 2020, offering political stability, competitive taxation, modern infrastructure and low labour costs, Malaysia has in recent times enjoyed an influx of investments from multinational corporations and overseas SMEs.

Considerations for distressed transactions

Clean sales

If a target company is already trading insolvent or is in danger of insolvency, caution is necessary to avoid falling foul of provisions rendering certain antecedent transactions being vulnerable to challenge.

Counting backwards from the date a creditor files a petition for winding up a company, there is a window of time in which transactions of particular kinds may be void, as follows:

Transactions at overvalue: In essence, if a company acquired any property, business or undertaking for cash consideration at an *overvalue* within two years prior to the presentation of a petition for a compulsory wind up, the liquidator may recover the excess value from the transferor.

Transaction at an undervalue: If a company instead sold any property, business or undertaking at an *undervalue* within two years prior to the presentation of petition, the liquidator may recover the difference in value from purchaser.

Undue preference: Acts which are deemed to confer an undue preference on a creditor are both void and deemed fraudulent. The following are the key elements of a transaction constituting undue preference: (i) There was an act in relation to property made by or against a company. Such acts include, for example, a transfer of property, mortgage, delivery of goods and payment, (ii) the act was done when the company was already unable to pay its debts as they fall due, (iii) the act was in favour of any creditor or a person in trust for any creditor, and (iv) the act was done within six months of the presentation of a petition for compulsory wind up.

Void dispositions: Once a wind-up petition has been filed, any disposition of the property of a company not done by the liquidator will be void unless permitted by a court. Such dispositions include any transfer of shares or alteration in the status of the members of the insolvent company.

Void floating charges: Finally, in general terms, a floating charge on the undertakings or properties of a company created within six months of the presentation of a wind up petition is invalid, save to the extent of any cash consideration given for the creation of the charge, or where it is proven that the company is still solvent immediately after its creation.

Directors of a distressed company

In normal circumstances, directors need to act in the best interests of a company. For a distressed company where formal insolvency proceedings have become likely, however, directors must also take into account the interests of creditors. In addition, directors would need to avoid triggering personal liability, in particular through the following: (i) wrongful trading, meaning, in essence, at the time a debt was contracted, a director had no reasonable ground of expectation that the company would be able to pay that debt, (ii) fraudulent trading, which involves the carrying on of business with intent to defraud the creditors of the company and (iii) failing to disclose or deliver to the liquidator all property of the company.

Corporate rescue mechanisms

In terms of Malaysia's statutory corporate rescue mechanisms, the main ones are as follows: (i) A court sanctioned scheme of arrangement, (ii) a company voluntary arrangement, where court approval of the compromise made between a company and its creditors is not necessary, and (iii) judicial management, where a distressed company is placed under the management of a qualified insolvency practitioner.

Country-specific deal points

Foreign equity ownership

The equity ownership of foreigners is restricted in certain industry sectors. This needs to be taken into account in structuring a transaction.

Foreign ownership of land

In Malaysia, foreign ownership of land usually requires the consent of the relevant State authority, and the conditions for consent may vary from one State to another. As examples, different States set different minimum values of land eligible for foreign purchase and may have different types of reserved lands not available for foreign ownership. It is therefore crucial for a purchaser to identify at the very start of a planned transaction whether there are any barriers at the State level against their ownership of the target land.

Labour law

Malaysia does not have a regime equivalent to those implemented under the European Union Transfer of Undertakings Directive – commonly known as "TUPE" following the United Kingdom term – for the protection of employees when businesses are transferred. Where there is a change in the ownership of a business for the purposes of employment law, employees will not be automatically transferred from the buyer to the purchaser of a business. The purchaser has the freedom to choose whether to offer new engagement to an employee; should an offer not be made, the employee would be terminated, and it is the seller who will bear the responsibilities of termination.

Luther in Malaysia

Luther's core team in Malaysia consists of counsels trained in Germany, France, Poland, England and Wales and Malaysia, supported by a network of local partner firms. This unique combination of European insight, international corporate expertise and deep knowledge of the Malaysian legal environment is the basis of Luther's trademark tailored and practical solutions for our client's every business need.

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Myanmar

Myanmar's legal system is governed by both old and new laws and regulations, as well as internal policies and practices of the Myanmar authorities. Many laws dating back to the colonial period and post-independence period are, with certain changes, still in force. Since its political and economic opening in 2011, Myanmar has embarked on a comprehensive reform process and is currently overhauling its legal framework. Existing laws were revised or replaced, and new laws enacted.

Considerations for distressed transactions

Myanmar recently passed a new insolvency law on 14 February 2020 ("New Insolvency Law"). The New Insolvency Law consolidated the scattered and partly outdated insolvency regulations and introduced an up-to-date regime benchmarked against international standards. The New Insolvency Law (but for the provisions on cross-border insolvency which are based on the UNCITRAL Model Law on Cross Border Insolvency) became effective after the notification was issued by the President of Myanmar on 25 March 2020. Given its recent introduction, there is little practical experience with the new legislation; in particular its application and implementation in practice remains yet to be seen.

Based on the New Insolvency Law, the following points are in our view noteworthy for distressed transactions:

Clean sales

Transaction at an undervalue: A transaction at an undervalue materialises when a company (i) makes a gift to a person or otherwise enters into a transaction with that person where no consideration is received, or (ii) enters into a transaction with a person for a consideration the value of which is significantly less than the current value of the consideration provided by the company. A Court must make an order restoring the (insolvent) company's position to what it would have been had the transaction not been entered into if, *inter alia*, the court is satisfied that the company was insolvent at the time of the transaction or became insolvent as a consequence of the transaction. The "relevant time" is generally two years prior to the date on which the petition for winding-up was filed. Such period may be prolonged to four years for connected persons or five years in case the intent of the company to enter into the transaction was to defeat, hinder or delay creditors from being paid their respective claims.

There is a specific "good faith" defence available: The court must basically uphold the transaction and refrain from making any orders to the contrary in case a company entered into the transaction in good faith and at the time it did so there were reasonable grounds for believing that the transaction would benefit the company,

Unfair preference: An "unfair preference" materialises in case a company enters into a transaction with a creditor during the relevant time that results in the creditor receiving from the company, in respect of an unsecured debt that is owed to the creditor, more than the creditor would receive from the company in respect of the debt if the transaction were set aside and the creditor were to prove for the debt. A court must make an order restoring the (insolvent) company's position to what it would have been had the transaction not been entered into if, *inter alia*, the court is satisfied that the company was insolvent at the time of the transaction or became insolvent as a consequence of the transaction. The "relevant time" is generally six months prior to the date on which the petition for winding-up was filed. It may be prolonged to four years for connected persons.

There is again a specific "good faith" defence available: A court must basically uphold the transaction and refrain from making any orders to the contrary if (i) the person received the benefit in good faith and at that time, (ii) the person had no reasonable grounds for suspecting that the company was insolvent and a reasonable person in the person's circumstances would have had no such grounds for so suspecting.

For both cases, the New Insolvency Law stipulates specific orders – "without contradiction" to the general order for restoring the position to what it would have been if the company had not entered into the transaction – a court may make. Such specific orders encompass *inter alia* (i) an order for the property transferred by or as part of the transaction to be vested in the company, or (ii) an order to release or discharge in whole or in part any security given by the company.

Corporate rescue mechanisms

Besides the option for liquidation the New Insolvency Law introduced, a corporate rescue and rehabilitation regime. The aim is to rescue the company as a going concern. There is also a separate rescue regime for micro, small and medium-scale enterprises.

Extortionate credit transactions

Lastly, the New Insolvency Law also introduced the possibility to set aside extortionate credit transactions.

Country-specific deal points

Approval by the Myanmar Investment Commission

Transactions with companies registered under the Myanmar Investment Law 2016 may require prior approval of the Myanmar Investment Commission. This is particularly the case for overseas loans and transactions resulting in the transfer of a majority of the company's shares or more than 50% of its assets to a party who is not a related body corporate of the investor (the investor usually being the controlling shareholder of the company who initially committed to the investment).

Foreign ownership restrictions

The Myanmar Companies Law 2017 distinguishes between Myanmar and foreign (owned) companies. The categorisation may not only affect the eligibility of the company to carry out certain restricted business activities set out in Notification No. 15/2017 of the Myanmar Investment Commission, but also the leasing, use and acquisition of land within Myanmar under the legal confines of the Transfer of Immovable Property Restriction Law 1987. A company is considered foreign (owned), if more than 35% of the ownership interest is directly or indirectly controlled by foreign persons.

Restricted investment activities are categorised as follows: (i) Investments that may be carried out only by the Union of Myanmar, (ii) investments that may not be carried out by foreign companies, (iii) investments that may be carried out in the form of a joint venture with a Myanmar citizen or Myanmar company (subject to any express exception in the relevant notification, the minimum direct shareholding or interest of a Myanmar citizen or Myanmar company in the joint venture must be at least 20%); and (iv) investments permitted only with the recommendation of the relevant Ministry.

Prior to any M&A deal, it is therefore vital to explore whether the activities of the target company may be carried out by a foreign investor (as a joint venture or 100% foreign owned), and whether such investment would require the approval of the relevant Ministry.

Licensed business activities

In addition to the aforementioned restricted businesses, certain activities may be subject to specific registrations and licenses with the relevant authorities. It is not uncommon that such licenses are subject to different conditions for foreign and Myanmar companies. Prior to any investment into a company carrying out a licensed business activity, it should thus be verified whether the company may have to apply for a new or amended license or permit to continue carrying out its business.

Corporate compliance and due diligence

It should be noted that due diligences in Myanmar are often of limited value due to a lack of public registers. Combined with the still common non-compliance of Myanmar companies, it may in many cases be prudent to consider an asset transactions to minimise particularly the risk of tax and labour compliance liabilities. Exemptions may apply if the company holds specific licenses or contracts which cannot be easily transferred, or if the company owns land rights, the transfer of which may attract high stamp duties and taxes.

Asset sales – Transfer of employees

Due to the difficult assessment of a company's potential liabilities and past compliance, most transactions are carried out by way of an asset deal, which may further allow for the application of benefits under the Myanmar Investment Law 2016 for the new company.

While Myanmar labour law is silent on the transfer of employees (and related tax and social security liabilities) in the event of a transfer of a business as going concern, it is common practice to novate employment contracts to the new company. A novation of existing employment contracts will usually not only result in a transfer of tax and social security obligations in respect of the employees, but also affect severance payments in the event of a later termination, which are determined based on the duration of continued employment.

Asset sales – Post-closing

One of the main concerns of any asset transaction in Myanmar is the post-closing integration phase, requiring not only the compliance with statutory obligations such as employee registration with the labour authorities, the registration of the transfer of assets (e.g. vehicles) and the re-application of licenses (e.g. with the relevant City Development Committee or industry-specific administrative authorities), but also the implementation of proper policies in accordance with group-internal requirements and international standards.

Offshore-financing solutions

In restricted sectors it is customary to choose a more flexible approach for structuring investments such as via offshore-financing solutions, in particular in the form of convertible loans and mezzanine (hybrid) financing instruments.

The legal framework for offshore-financing in Myanmar is primarily stipulated in the Myanmar Investment Law 2016, the Foreign Exchange Management Law 2012 and their implementing regulations. Any offshore-financing must obtain prior approval from and be registered with the Central Bank of Myanmar as stipulated in the Foreign Exchange Management Law 2012 and the Foreign Exchange Management Regulations 2014. For borrowers registered under the Myanmar Investment Law 2016, the application needs to be submitted through the Myanmar Investment Commission. There are various criteria for the approval of offshore-financings.

In case of secured offshore-financing, while the registration of securities such as fixed and floating charges with the Companies Register has become much easier since the enactment of the new Myanmar Companies Law 2017, the granting of securities over immovable property rights to the benefit of a foreign lender remains difficult.

Any financing provided with a conversion option should take into account the risks highlighted above for equity investments.

Luther in Myanmar

Active in Myanmar since 2013, we operate in Myanmar as Luther Law Firm Limited. We are one of the largest law firms and corporate services providers in Yangon with a team of multinational and local lawyers. We have the competence and expertise necessary to comprehensively assist and advise our clients on all aspects of corporate and commercial law as well as regulatory compliance.

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Singapore

The Singapore legal system is historically based on English law, with an ever increasing local jurisprudence. A strict application of the rule of law, up-to-date regulations and legal instruments and fast-reacting legal institutions make Singapore a popular legal hub for the region.

Considerations for distressed transactions

Clean sales

If a company is already trading insolvent or is on the brink of insolvency, certain provisions may jeopardise a "clean sale", such as:

Transaction at an undervalue: A sale by a company might qualify as a transaction at an undervalue if (i) it is an out-right gift or the value of the consideration received by the company is significantly less than the value of the consideration provided in return by the company, (ii) the transaction occurred within five years prior to the commencement of winding-up proceedings and (iii) the company was or became insolvent as a result of such a transaction. If a sale is qualified as a transaction at an undervalue, then the court is entitled to make any orders it deems to be fit to restore the situation prior to such sale. These orders might encompass unwinding the sale and a claw-back of the relevant assets.

Unfair preference: A sale by a company might qualify as an unfair preference if (i) a preference is given by the company to its creditor or guarantor of the company's debt, (ii) the company is induced by a desire to prefer such preferred party, (iii) the preference occurred within six months (or two years if the preferred party is an affiliate of the company) prior to the commencement of winding-up proceedings and (iv) the company was insolvent at the time the preference was given or became insolvent as a result of such preference. Similarly as in case of the transactions at an undervalue, if a transaction is qualified as an unfair preference, the court may make any orders it deems to be fit to restore the situation prior to the unfair preference.

Void dispositions: Following the commencement of winding-up proceedings, any disposition of assets of the insolvent company and any transfer of shares or alteration in the status of the members of the insolvent company shall be void unless the court orders otherwise.

In all such scenarios there is a risk looming that a sale might be set aside at a later point in time if not certain precautions are taken. The above considerations also apply *mutatis mutandis* in a share deal scenario if a seller itself is close to or already trading insolvent.

Floating charges for past value: A floating charge on the undertakings or properties of a company created within six months of the commencement of a winding-up proceedings is invalid, unless it is proved that the company was solvent immediately after creation of the charge, and except to the extent of any cash paid to the company in connection with the creation of the charge.

In all such instances, a compulsory winding-up proceeding is deemed to commence from the date where the relevant application was filed and therefore relates back to such date.

Directors of a distressed company

Directors of a distressed company need to be aware that additional safeguards and precautions should be taken in discharging their duties:

Interest of creditors: The interest of creditors are to be taken into account whilst discharging their duties as directors. Failure to do so might result in a breach of directors' duties triggering a criminal offence by and a personal liability of the director.

Wrongful trading and fraudulent trading: Wrongful trading encompass situations where the distressed company takes on an additional debt and the director involved in contracting of such debt had no reasonable or probable grounds, at the time the debt was contracted, of expectation that the company will be able to repay such a debt. The COVID-19 (Temporary Measures) Act recently modified these provisions by introducing a "defence" for directors: A director is not to be treated as having no reasonable or probable ground of expectation if the debt is incurred in the ordinary course of the company's business during the prescribed period (20 April 2020 to 19 October 2020) and before the appointment of a judicial manager or liquidator of the company.

Fraudulent trading encompasses situations where the business of the company has been carried on with the intent to defraud its creditors or for any other fraudulent purpose.

Directors breaching these provisions might commit a criminal offence and triggering a personal liability of the director. Further directors involved in a transaction at an undervalue or unfair preference or void disposition might find themselves in breach of directors' duties, inter alia triggering a personal liability of the director.

That said, it is vital to always stay on top of the financial situation of the company and clearly identify whether there is a risk that the company is insolvent or trading close to insolvency. Insolvency is usually established via the cash flow test (inability to serve debts when they are due) and, alternatively, the balance sheet test (liabilities of a company are greater than the assets of the company). "Nelsonian blindness" is not a proper defence and contingent liabilities need to be taken into account, where relevant. A reasonable paper trail should be kept in order to demonstrate the compliance by the directors with their duties.

Lastly, once the company entered into formal insolvency proceedings additional obligations apply, such as submission of a statement of company's affair to the liquidator detailing *inter alia* the assets, debts and liabilities of the insolvent company.

Corporate rescue mechanisms

Statutory rescue mechanisms are available at Singapore law, with schemes of arrangement being the most prominent one. Such schemes of arrangement can also be applied as a mean to implement an acquisition of a target company via a debt-to-equity swap (such as "loan-to-own" transactions). "Pre-packaged" options are available without the requirement for a formal creditors' meeting. Besides schemes of arrangement, another corporate rescue mechanism – although with limited practical relevance – is judicial management. In judicial management proceedings, an independent judicial manager is appointed to restructure the liabilities and to reorganise the operations of the distressed company.

Singapore recently passed the Insolvency, Restructuring and Dissolution Bill 2018 which is yet to come into force. The Bill will consolidate the currently applicable insolvency regime which is spread out over different legislations. *Inter alia*, provisions governing "*ipso facto*" clauses and new wrongful trading provisions will be introduced.

Country-specific deal points

Workforce in a "transfer of undertaking" scenario

In case an asset sale qualifies as a "transfer of undertaking" scenario, employees covered by the relevant provisions of the Employment Act are automatically transferred from the seller to the purchaser. Such a "transfer of undertaking" is generally realised if there is a transfer of business on a going concern basis. The employment relationship is then to be treated as if it was originally concluded by the purchaser instead of the seller. Further, notification, information and consultation obligations might apply.

Foreign ownership restrictions

There are generally no restrictions as to foreign ownership in Singapore. However, certain subsidy and government support schemes can only be applied for when there is at least 30% local ownership.

Luther in Singapore

We operate in Singapore via Luther LLP, a registered Foreign Law Practice. We are supported by, and cooperate with, I.N.C. Law LLC, a local law firm in Singapore, where advice on Singapore law is necessary.

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Thailand

The legal system of the Kingdom of Thailand is based on the civil law legal system. In addition, it is strongly influenced by common law principles. Primary sources of law include the Thai constitution, which is the supreme law, legislation such as codes and acts, decrees and customary principles. Under the current legal system, judicial decisions are not binding; in practice, however, decisions of the Supreme Court are persuasive, have some precedential value and are often used as a guideline for interpretation of the law.

Considerations for distressed transactions

Clean sales

When acquiring a company in receivership or bankruptcy, the provisions of the Thai Bankruptcy Act B.E. 2483 (1940) must be taken into account. For example, in the case of any sales of the assets of the entity in bankruptcy, without the creditors' approval, the transactions must be made in the form of an auction. However, this may involve certain difficulties in practice, as sales of a bankrupt company's assets by an auction process may not be supported by internal regulations of the official receiver. Further, the following potential legal obstacles and hurdles should be kept in mind in achieving a clean sale:

Cancellation of fraudulent acts: The purchasers should be careful in acquiring asset in a company which is insolvent. The acquisition of assets may be considered as a 'fraudulent act' if a company transfers its assets or performs any juristic act with the knowledge that it would prejudice its creditors. As a result, a court could unwind the transaction. Such unwinding of fraudulent acts can be requested either (i) before or (ii) during the bankruptcy process.

Before the bankruptcy process, the creditor can submit a petition to the court to revoke an acquisition or any juristic act over property rights. An acquisition can be revoked if the creditor can prove that (i) such acquisition prejudices him, (ii) the asset transferor (debtor) knows of such prejudice of the creditor, and (iii) the person enriched by such act knows that the act prejudices the creditor (except in case of gratuitous act, in which the knowledge of the transferor (debtor) alone shall be sufficient).

Further, during the bankruptcy process, the official receiver (if bankruptcy proceedings against the company commenced) or the plan preparer/plan administrator (if the company is

under business reorganisation) can request from the court to revoke a fraudulent act.

Unfair preference: Transfer of asset in a company may also be revoked by the court if (i) the transferee is a creditor of the company, (ii) the asset transfer is done by the company or done with the company's consent, (iii) the asset transfer is done within a period of three months before the date of bankruptcy filing, or business reorganisation application (this period is extended if the transferee is for example a director of the company), and (vi) such transfer gives the transferee an advantage over other creditors. The official receiver, the plan preparer, or the plan administrator can submit a petition to the court to revoke such transfer.

Cancellation of improper registration: If the company transfers an immovable property to the purchaser, such transfer – albeit duly registered – can be revoked if it prejudices a person who was previously in a lawful position to have its immovable property rights registered (for example, a person who lawfully obtained the property through a public auction, court order, or previous possession). Such a person may claim cancellation of the improper registration (unless the transferee acted in good faith).

Corporate rescue mechanisms

The Thai Bankruptcy Act B.E. 2483 (1940) does not contain any provisions for workout mechanisms or pre-court options (such as settlement of debt).

In case of a corporate insolvency, the following types of procedures are available for corporate debtors: (i) a creditor-initiated bankruptcy leading to a court order of absolute receivership under judicial supervision, (ii) a debtor-initiated bankruptcy through voluntary liquidation and (iii) a business reorganisation procedure with the objective of rescuing the business. The latter procedure will be operated by a reorganisation planner or a plan administrator under judicial supervision. An application for a reorganisation may be submitted by a debtor, a creditor or a governmental authority. Upon submission to and acceptance of the petition by a court, an automatic stay will come into effect and parties will be prohibited from taking certain actions regarding the debtor (e.g. requesting that the debtor is to be wound-up or commencing any bankruptcy action against the debtor).

Country-specific deal points

Cross-border transactions

There is currently no specific law governing cross-border transactions in Thailand. However, Thai law makes a difference between Thai and foreign-owned companies, which may affect the possibility for a foreign investor to get involved in a transaction. Under the Foreign Business Act B.E. 2542 (1999), the term "foreigner" means: (i) a natural person who is not of Thai nationality, (ii) a body corporate not registered in Thailand (e.g. a branch office of an overseas corporation), (iii) a body corporate registered in Thailand, matching one of the following descriptions: (a) being a body corporate of which at least half of its capital shares are held by persons indicated under points (i) or (ii) above, or a body corporate in which investment has been placed by the persons indicated under points (i) or (ii) above in the amount at least equivalent to half of the total capital thereof, (b) being a limited partnership or a registered ordinary partnership, in which, the managing partner or the manager is the person indicated under point (i); or (iv) a body corporate registered in Thailand of which at least half of the capital shares are held by persons indicated under points (i), (ii) or (iii) above, or a body corporate in which investment has been placed by the persons indicated under points (i), (ii) or (iii) above in the amount at least equivalent to half of the total capital thereof. For the purpose of this definition, shares of a limited company represented by share certificates issued to bearers are deemed as shares held by foreigners, unless otherwise provided by the Ministerial Regulation.

Some business activities are either completely prohibited or restricted (which means that they usually require a prior approval of the competent Thai authority) for foreigners. Unless prior approval is granted by the Ministry of Commerce, an enterprise engaging in these restricted business activities may not be held by a foreigner.

Land

The assets of a company can comprise of lands, buildings, factories, machineries, claims, accounts receivable and other rights and entitlements. In case of land, the acquirer should obtain official copies of the land title deed evidencing land ownership as well as any other supporting documents (e.g. certificates of land utilization and notices of possession). If the acquirer is a "foreigner" as defined by the Foreign Business Act B.E. 2542 (1999) (as outlined above), the acquirer is prohibited from holding land ownership. Thus, a foreign acquirer of lands must ensure that it or its acquiring vehicle registered in Thailand has not more than foreigner ownership.

Few exceptions apply, most notably investment promotions granted by the Board of Investment and the acquisition of land located in an industrial estate zone.

Business licenses and permits

Depending on the business activities and shareholding structure, companies may be required to hold several kinds of licenses and permits. For example, to own and operate a factory, a company must have obtained all necessary licenses and permits (e.g. construction license, building certificate, factory license, or operating license and land use license for land located within an industrial estate). If a company leases a factory, a factory lease agreement and documents showing ownership of the machinery used in the factory should be obtained and reviewed.

Workforce in a "transfer of undertaking" scenario

In case of an asset sale which effects employment transfers to the purchaser, the employees are not automatically transferred by operation of law. In addition to complying with the terms and conditions of the employment contracts, a consent from the relevant employees has to be obtained in order to complete the employment transfer. The transferee shall procure all rights and duties of the employees as under the previous employment contracts. However, if the employees do not consent to the employment transfer, the employment relation between the seller and its employees shall continue. This may force the seller to terminate the employment relation (any termination remains on the account of the seller).

Luther in Thailand

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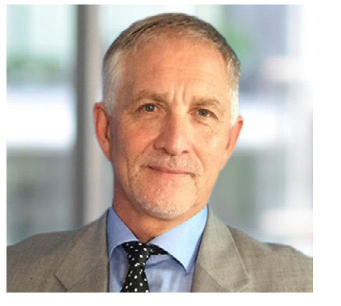

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