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When the Sun sets on a Company

Important developments in insolvency law from Sun Electric Power Pte Limited v RCMA Asia Pte Ltd (formerly known as Tong Teik Pte Ltd) [2021] SGCA 60

Recently, in ***Sun Electric Power Pte Limited v RCMA Asia Pte Ltd (formerly known as Tong Teik Pte Ltd) [2021] SGCA 60***, the Singapore Court of Appeal made several important clarifications about the law of insolvency in Singapore. In particular, the Court of Appeal clarified that:

- a company has an inherent right to appeal against a winding up order made against it, and its director or shareholder was entitled to have conduct of that appeal; and
- the relevant test for whether a company is insolvent is the cash flow test, and the test involved taking into account a list of relevant factors pertaining to the company.

This case is important because it appears to be a major departure from the rigid cashflow / balance sheet tests which were previously applied.

Brief Facts of the Case

The pertinent facts of this case are fairly straightforward.

Sun Electric Power Pte Limited ("**SEPPL**") was in the business of transmitting, distributing and selling electricity. SEPPL's sole director – and ultimate majority shareholder – was Mr Matthew Peloso ("**Mr Peloso**").

SEPPL was involved in a dispute with RCMA Asia Pte Ltd ("**RCMA**"). After failing to obtain a judicial management order and an interim judicial management order, SEPPL was ordered to pay costs amounting to S$11,500 to RCMA for both applications.

RCMA then issued a statutory demand to SEPPL for these costs and interest. SEPPL replied through its solicitors to admit the debt, and proposed to pay in instalments. Although this instalment proposal was rejected by RCMA, SEPPL proceeded to pay the first instalment into RCMA's solicitors' account. This was the only payment made by SEPPL.

RCMA proceeded to file a winding up application against SEPPL on 18 December 2019. On 7 September 2020, a winding up order was made against SEPPL. In making the winding up order, the judge found that the following three grounds were made out:

- SEPPL was deemed to be unable to pay its debts pursuant to section 254(2)(a) of the Companies Act as it had not repaid the costs claimed under the statutory demand;
- SEPPL was insolvent for the purposes of section 254(2)(c) of the Companies Act as it was both cashflow and balance sheet insolvent; and
- it was just and equitable to wind up SEPPL.

Mr Peloso then appealed against the winding up order in SEPPL's name. The key substantive issues before the Court of Appeal were:

- whether Mr Peloso (as director of a company under a winding up order) had the standing to bring the appeal;
- whether SEPPL was actually insolvent; and
- whether SEPPL should be deemed to be insolvent under section 254(2)(a) of the Companies Act.

The Court of Appeal's Decision

The Court of Appeal dismissed the appeal, and upheld the winding up order. In reaching this decision, the Court of Appeal also made various important clarifications and observations which have significant implications on insolvency law and practice in Singapore.

A director or shareholder of a company in liquidation has standing to bring an appeal against a winding up order

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The Court of Appeal clarified that Mr Peloso could bring the appeal. A company that is the subject of a winding up order has an inherent right to appeal against the winding up order, and the company's directors or shareholders have the right to control the conduct of that appeal.

It is not necessary for the directors or shareholders to first apply to stay the winding up order before appealing against it.

The costs of prosecuting the appeal will be borne by the directors or shareholders at first instance. If the appeal succeeds, the directors or shareholders can reclaim such costs from the company. However, they should also expect to be personally responsible for the payment of any party and party costs awarded in favour of the respondent in an unsuccessful appeal.

The cashflow test is the sole applicable test under section 254(2)(c) of the Companies Act

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The Court of Appeal found that SEPPL was insolvent on the evidence.

Perhaps more importantly, the Court of Appeal made it clear that the **sole and determinative test for insolvency** under section 254(2)(c) of the Companies Act is the **cashflow test**.

The cash flow test assesses whether the company's current assets exceed its current liabilities such that it is able to meet all debts as and when they fall due. "Current assets" and "current liabilities" refer to assets which will be realisable, and debts which will fall due within a 12-month timeframe.

The Court of Appeal also set out a non-exhaustive list of factors to consider under the cashflow test, such as:

- the quantum of all debts which are due or will be due in the reasonably near future;
- whether payment is being demanded or is likely to be demanded for those debts;
- whether the company has failed to pay any of its debts, the quantum of such debt, and for how long the company has failed to pay it;
- the length of time which has passed since the commencement of the winding up proceedings;
- the value of the company's current assets and assets which will be realisable in the reasonably near future;
- the state of the company's business, in order to determine its expected net cash flow from the business by deducting from projected future sales the cash expenses which would be necessary to generate those sales;
- any other income or payment which the company may receive in the reasonably near future; and
- arrangements between the company and prospective lenders, such as its bankers and shareholders, in order to determine whether any shortfall in liquid and realisable assets and cash flow could be made up by borrowings which would be repayable at a time later than the debts.

Other observations by the Court of Appeal

In obiter, the Court of Appeal also observed that a company that pays the debt demanded in a statutory demand **in part within the prescribed period** such that the remaining amount payable falls below the statutory threshold should not be deemed to be unable to pay its debts.

However the Court of Appeal reserved its judgment on whether **part-payment after the prescribed period** can defeat a winding up application premised on a statutory demand.

CONCLUSION AND COMMENTS

- The Court of Appeal's decision is useful in confirming that a director or shareholder of a company in liquidation can bring an appeal against the winding up order, without needing to stay the winding up application first. While there is already some support for this position from Malaysian authorities, this case has helpfully clarified that this is also the position under Singapore law.
- In our view, this decision also represents a significant departure from the previous application of the cashflow and balance sheet tests – such that the cashflow test is now a clear reference point for a company's insolvency (with parameters to establish this insolvency). It also indicates a willingness by the Singapore courts to take into account practical realities of a company when assessing whether it is truly insolvent.
- Given that the provision under section 254(2) of the Companies Act discussed in this case have been re-enacted under the Insolvency Restructuring & Dissolution Act, this case will be essential for practitioners and business owners in insolvency matters going forward.

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