



**D** DREW & NAPIER

# CLIENT UPDATE

LENDERS,  
LIQUIDATORS  
AND CAVEATS

17 April 2020

# LEGAL UPDATE

# In this Update

This update discusses the recent High Court case of *Aavanti Offshore Pte Ltd (in creditors' voluntary liquidation) v Bab Al Khail General Trading and another* [2020] SGHC 50 which highlighted the importance for lenders in secured financing transactions to follow through with the documentation and steps required to perfect the securities and of adherence to the relevant requirements when seeking a declaration from the Court. The Court also provided guidance for liquidators when seeking directions from the Court.

**03**  
OVERVIEW

**03**  
BACKGROUND

**05**  
THE LIQUIDATOR'S APPLICATION

**05**  
LENDERS BEWARE?

**06**  
A TIMELY REMINDER FOR PARTIES SEEKING DECLARATIONS

**07**  
LIQUIDATORS SHOULD ONLY SEEK DIRECTIONS WHEN IN REAL LEGAL DOUBT

## OVERVIEW

In the recent decision of *Aavanti Offshore Pte Ltd (in creditors' voluntary liquidation) v Bab Al Khail General Trading and another* [2020] SGHC 50, the Singapore High Court denied various declarations and orders sought by the liquidators of the applicant (“**AOPL**”).

From a credit and security perspective, this case illustrates the importance for lenders to follow through with the necessary documentation in secured financing transactions and to register any relevant security interests, including agreements to execute the same.

This case is also a timely reminder that, when seeking a declaration from the Court, the applicant should ensure that all interested parties are joined to the action. Parties should not take the requirements when seeking declarations lightly.

The Court also provided guidance to liquidators when seeking directions from the Court. Liquidators should only seek directions from the Court if in real legal doubt.

## BACKGROUND

### KEYPOINT

*The key takeaways from this case are:*

- (1) Lenders in secured financing transactions should ensure that all necessary documents and steps conferring a security interest are executed and require the borrower to comply with such steps as conditions precedent for the drawdown of the financing.*
- (2) Parties should not compromise on the legal requirements when asking the Court for a declaration just because the same may be practically difficult.*
- (3) Liquidators should determine whether the issues they need to resolve raise real legal doubt before seeking directions from the Court.*

### 1. Parties

The applicants were the liquidators (“**Liquidators**”) of AOPL, a Singapore company currently in liquidation. The respondents were 2 creditors of AOPL, Aavanti Industries Pte Ltd (“**AIPL**”), a Singapore company in liquidation which was also the sole shareholder of AOPL, and Bab Al Khail General Trading (“**BAB**”), a United Arab Emirates entity.

## 2. Convertible loan agreement

In June 2012, AOPL entered into a convertible loan agreement (“**CLA**”) with Sawit Plantations Pte Ltd (“**Sawit**”). Under the CLA, Sawit made a loan facility of up to US\$10,000,000 available to AOPL. AOPL subsequently drew down on the CLA. Clause 7.6 and clause 9.1 of the CLA set out putative arrangements for AOPL to grant security in favour of Sawit. Specifically, clause 7.6 provided that the lender was to have “*an exclusive lien on all assets purchased and/or sold by the borrower*” and clause 9.1 provided that for “*the clarity in addition to clause 7*”:

- (a) the lender shall require the borrower to encumber all assets of the borrower for the benefit of the lender (clause 9.1(i));
- (b) the borrower shall encumber the bank account registered under the name of the borrower for the benefit of the lender (clause 9.1(ii));
- (c) the borrower shall procure and ensure that all its shareholders grant pledge over all issued shares held by them in the borrower and the investments of the borrower for the benefit of the lender (clause 9.1(iii)); and
- (d) the borrower and shareholder shall execute and deliver to the lender the security set out in clauses 9.1(i) to 9.1(iii) and any related documents in the form satisfactory to the lender.

AOPL’s key asset was its 95% shareholding in PT Palm Lestari Makmur (“**PT Palm**”), which in turn owned a plantation in Indonesia. Ultimately, no security documents were ever executed.

About four and a half years later, the CLA was unconditionally assigned to BAB. AOPL was subsequently placed into liquidation. Thereafter, BAB demanded that the liquidators execute the necessary security documents to perfect BAB’s entitlement to security over AOPL’s assets. The liquidators sought AIPL’s consent to give effect to BAB’s purported entitlement to security under the CLA. AIPL disagreed that BAB was entitled to any security under the CLA.

In addition, from August 2017 to March 2018, AIPL was under judicial management. While under judicial management, AIPL issued two debit notes (“**Debit Notes**”) to PT Palm for management fees for the period December 2010 to July 2017 and January 2018. The liquidators of AOPL rejected the validity of the Debit Notes. PT Palm also wrote to AIPL rejecting the validity of the Debit Notes.

## THE LIQUIDATOR'S APPLICATION

AOPL's liquidators applied to the Court under Section 310 of the Companies Act seeking, among others, the following:

- (a) a declaration that AOPL was obliged to encumber all its assets, including the shares in PT Palm owned by AOPL, for the benefit of BAB;
- (b) an order that the liquidators execute all security documents as appropriate to comply with the CLA; and
- (c) a declaration that the Debit Notes are void and/or invalid, or in the alternative, a direction that the liquidators proceed with the liquidation of AOPL on such a basis.

In their application, the liquidators did not include PT Palm as a party to the application. PT Palm also did not apply to be joined as a party to the application.

The Court declined to make any of the orders, declarations and directions sought above. The Court found that:

- (a) clause 9.1(iii) did not create any security in favour of Sawit;
- (b) clauses 9.1(i) and 9.1(ii) had to be read together with clause 7.6. On a plain reading of the CLA, clauses 9.1(i) and 9.1(ii) read with clause 7.6 were agreements to execute a floating charge which were void for want of registration under Section 131 of the Companies Act;
- (c) in respect of the Debit Notes, the liquidators had not established the legal requirements to grant a declaration as established by the Court of Appeal in *Karaha Bodas Co LLC v Pertamina Energy Trading Ltd and another appeal* [2006] 1 SLR(R) 112. In particular, PT Palm had not been joined as a party, even though it was a party to the Debit Notes and PT Palm's evidence was crucial to the dispute on the validity of the Debit Notes; and
- (d) directions would not be given to the liquidators to proceed with the liquidation on the basis that the Debit Notes were void and/or invalid as that was a decision of commercial discretion for the liquidators.

## LENDERS BEWARE?

The Court adopted an objective interpretation of the CLA and found that clauses 9.1(i) and (ii) read with clause 7.6 of the CLA was an agreement to create a floating charge.

The Court then held that since clauses 9.1(i) and 9.1(ii) had not been registered within 30 days of their creation (i.e. 1 June 2012, the date of the CLA), they were void against the liquidator and the creditors of AOPL under Section 131 read with Section 4 of the Companies Act in force at the applicable time.

The Court's ruling highlights the importance placed on lenders to ensure that the necessary documentation is executed by the relevant parties and/or registered in time in order to perfect the relevant security interest granted in favour of the lenders.

The onus is on lenders in secured financing transactions to take the necessary steps to perfect the security interest granted or to be granted in their favour by (among other things) executing the necessary documents conferring the relevant security interest and taking other applicable perfection steps such as stamping and registration of such documents. It is not enough for a lender to merely require a borrower to encumber all its assets (as was the case in clauses 9.1(i) and 9.1(ii)), and thereafter assume that the borrower would thereafter take all the steps necessary to do so. Failure to do so may result in a lender losing the security they may have bargained for under the original agreement, especially when the borrower subsequently enters liquidation proceedings.

Indeed, lenders should ensure that all steps required for the creation, validity and perfection of any security interest, as well as legal opinions confirming the same where required, should be included as conditions precedent to the drawdown of the financing by the borrower i.e. all such items should have been fulfilled to the lenders' satisfaction before the borrower is permitted to utilise the financing.

## **A TIMELY REMINDER FOR PARTIES SEEKING DECLARATIONS**

The Court also declined to make the declarations sought by the liquidators regarding the Debit Notes. The Court took guidance from the seminal case of *Karaha Bodas Co LLC* and found that the requirements for a declaration had not been met because a party whose interest might have been affected was not before the Court.

The liquidators sought a declaration that the Debit Notes were void and/or invalid. However, even though the Debit Notes had been issued by the judicial manager of AIPL to PT Palm, PT Palm had not been joined as a party to the proceedings.

In *Karaha Bodas Co LLC*, it was held that in order for a declaration to be made, "all parties with affected interest should be before the court". In the present case, the Court found that since PT Palm had not been joined and was not before the Court, it was not satisfied a declaration should be granted.

In reaching its holding, the Court made the following observations:

- (a) The rationale for the requirement that all parties with affected interest should be before the Court was so that such parties were given the opportunity to raise objections. This also ensured that the Court takes into account all considerations.

- (b) A letter from the absent affected party stating that it consented to submit to the findings of the Court was insufficient to establish that it would be bound by a declaration of the Court.
- (c) The evidence from the absent affected party which was before the Court in this case only consisted of emails tendered by an interested party (i.e. BAB). Such evidence, being many steps removed from the primary source, was undesirable. The affected party should have been joined as a party to the proceedings, and the relevant individual in question should have given witness evidence by way of affidavit.
- (d) The Court also rejected BAB's argument that PT Palm was not joined as a party to the proceedings because of "*practical concerns*".

The above highlights the importance of joining the proper parties to the proceedings when seeking declarations from the Court. In particular, parties will not be permitted to take shortcuts and sidestep the requirements laid down by the Court in respect of seeking declarations just because fulfilling the same may be practically difficult.

## **LIQUIDATORS SHOULD ONLY SEEK DIRECTIONS WHEN IN REAL LEGAL DOUBT**

This case offers particular guidance to liquidators seeking to rely on Section 310 of the Act. In this regard, even though Section 310 of the Act is widely framed so that liquidators may apply to Court to "*determine any question arising from the winding up of a company*", a liquidator seeking the Court's assistance must still consider the appropriateness of such an application and the proper parties to be included.

The Court noted that liquidators should only seek directions "if in real legal doubt [and] it was not for liquidators to throw questions of commercial discretion to the court". The Court warned that "*[i]n appropriate cases, in addition to the refusal of the court to substitute its directions for the commercial decision of the liquidator, the court may also disallow the liquidator the costs incurred both by him directly as well as in instructing counsel, leaving it to him to bear such costs personally*".

*The content of this article does not constitute legal advice and should not be relied on as such. Specific advice should be sought about your specific circumstances. Copyright in this publication is owned by Drew & Napier LLC. This publication may not be reproduced or transmitted in any form or by any means, in whole or in part, without prior written approval.*

If you have any questions or comments on this article, please contact:



**Rakesh Kirpalani**

Director, Dispute Resolution & Information Technology  
Chief Technology Officer  
T: + 65 6531 2521  
E: [rakesh.kirpalani@drewnapier.com](mailto:rakesh.kirpalani@drewnapier.com)



**Pauline Chong**

Head, Banking & Finance  
Director, Corporate & Finance  
T: + 65 6531 2796  
E: [pauline.chong@drewnapier.com](mailto:pauline.chong@drewnapier.com)



**Renu Menon**

Deputy Head, Banking & Finance  
Director, Corporate & Finance  
T: + 65 6531 2253  
E: [renu.menon@drewnapier.com](mailto:renu.menon@drewnapier.com)



**Teri Cheng**

Associate Director, Corporate & Finance  
T: + 65 6531 2268  
E: [teri.cheng@drewnapier.com](mailto:teri.cheng@drewnapier.com)

**Chua Yong Quan**

Senior Associate, Corporate & Finance  
T: + 65 6531 2411  
E: [yongquan.chua@drewnapier.com](mailto:yongquan.chua@drewnapier.com)

**Timothy Oen**

Associate, Dispute Resolution & Information Technology  
T: + 65 6531 2598  
E: [timothy.oen@drewnapier.com](mailto:timothy.oen@drewnapier.com)

**Valerie Tan**

Associate, Corporate & Finance  
T: +65 6531 2413  
E: [valerie.tan@drewnapier.com](mailto:valerie.tan@drewnapier.com)

**Drew & Napier LLC**  
10 Collyer Quay  
#10-01 Ocean Financial Centre  
Singapore 049315

[www.drewnapier.com](http://www.drewnapier.com)

T: +65 6535 0733  
T: +65 9726 0573 (After Hours)  
F: +65 6535 4906

 **DREW & NAPIER**