Liquidator of Leong Seng Hin Piling Pte Ltd v Chan Ah Lek and Others
[2007] SGHC 9

Case Number : Suit 680/2005

Decision Date : 19 January 2007

Tribunal/Court : High Court

Coram : Belinda Ang Saw Ean J

Counsel Name(s) : Gan Kam Yuin (Bih Li & Lee) for the plaintiff; Spencer Gwee and Lee Kwok Weng (Lee Kwok Weng & Co) for the defendants

Parties : Liquidator of Leong Seng Hin Piling Pte Ltd — Chan Ah Lek; Chan Soon Chew Tony; Chan Ah Lay

Companies – Winding up – Fraudulent trading – Whether defendants knowingly parties to carrying on of business of company with intent to defraud creditors – Whether defendants continuing to receive supplies knowing that company could not pay for them – Section 340(1) Companies Act (Cap 50, 1994 Rev Ed)

Insolvency Law – Avoidance of transactions – Undue preferences – Whether cash payments made by company in favour of second defendant amounting to undue preferences – Whether second defendant may set off such cash payments from debt owed to him by company – Section 329(1) Companies Act (Cap 50, 1994 Rev Ed)

19 January 2007

Belinda Ang Saw Ean J:

1 The plaintiff is the liquidator of Leong Seng Hin Piling Pte Ltd ("LSH"), a company which was wound up on 29 April 2005 pursuant to a winding up petition presented by Group Industries Pte Ltd ("GIPL") on the ground that LSH was insolvent as it was unable to pay a judgment debt. In this action, the plaintiff as liquidator of LSH sought a declaration under s 340(1) of the Companies Act (Cap 50, 1994 Rev Ed) that the three defendants, who were former directors of LSH, were knowingly a party to the carrying on of the business of LSH with intent to defraud creditors. As such, the defendants were liable to make such contributions to the assets of the company as the court thought proper. The second claim was against the second defendant and it was to recover the sum of $430,066.34, being the amount of money paid out in preference of the second defendant. For this second claim, the plaintiff relied on s 329(1) of the Companies Act read with ss 98 to 100 of the Bankruptcy Act (Cap 20, 2000 Rev Ed).

2 On 4 December 2006, I delivered a relatively lengthy oral judgment covering the main grounds of my decision for dismissing the plaintiff's claim against the defendants under s 340(1) of the Companies Act, but allowing the claim against the second defendant for undue preference in respect of a lesser sum of $190,835.21. On the question of costs, the plaintiff was ordered to pay costs of the action to the first and third defendants. As against the second defendant, the plaintiff was awarded 50% of the costs of the action. The plaintiff has appealed against my decision. I now set out in full the reasons for my decision.

3 The founding two directors of the company were Chan Ah Lay ("the third defendant") and his son, Tony Chan Soon Chew ("the second defendant"). Madam Lim, the sole proprietor of Soon Guan Piling and Engineering Construction ("Soon Guan") was once a director of LSH; but she had no management responsibilities and eventually left the company. The third defendant was appointed the

managing director of the company soon after LSH's incorporation and, due to his ill health, relinquished this position around 27 July 2004. The second defendant thereupon immediately succeeded the third defendant as the managing director of LSH. Chan Ah Lek ("the first defendant") was also named as director at around the same time (*ie* 26/27 July 2004).

4 The business relationship between GIPL and LSH went as far back as 2000 when GIPL agreed to the manufacture and supply of pre-cast reinforced concrete piles ("RC piles") to LSH. LSH did not pay GIPL for any of the RC piles supplied between April and July 2004 even though it had paid a total of $909,492.61 to its other creditors during the period spanning 21 April 2004 to April 2005. No payment was made even after judgment was obtained against LSH on 28 February 2005. The last payment, which was to settle GIPL's March 2004 invoice, was on 25 June 2004. It was this failure to make good the judgment that eventually resulted in the winding up of LSH by GIPL.

Fraudulent trading under s 340(1) of the Companies Act

5 The plaintiff's pleaded case was that the defendants were knowingly a party to the carrying on of the business of the company with intent to defraud creditors of the company or for fraudulent purposes. Despite the generalisation, the only creditor in relation to whom the defendants could be said to have had an intention to defraud was GIPL and the only relevant intention in relation to GIPL was the supplies collected between 3 April and 10 July 2004. It was argued that the defendants had caused LSH to continue to order RC piles from GIPL even though they were aware that the company was indisputably insolvent and there was no reasonable prospect that the company would be able to pay for them when payment was due. It was averred in paragraph 8 of the Statement of Claim that:

> For upwards of a year before the winding up of [LSH], the defendants regularly caused the Company to purchase goods on credit without any reasonable prospect of being able to pay for them. Very many of these goods were not paid for at the date of the winding up. In particular, at this time, the Liquidator has identified a Judgment entered against the Company for $330,614.70, interest thereon at 6% per annum from 1 September 2004 to 28 February 2005,amounting to $9,836.92 and costs of $12,000 in Suit No 784 of 2004/Q by [GIPL] on 28 February 2005 arising from the sale and supply of goods by [GIPL] to the Company over the period 2004.

6 According to the liquidator, Mr Don Ho Mun-Tuke, based on the balance sheet test of insolvency, LSH was already insolvent since 2001 and the company continued to be insolvent until it was wound up. This balance sheet insolvency was evident from (a) the audited accounts for the financial year ended 31 December 2002 and financial year ended 31 December 2003 respectively; (b) the company's management accounts, balance sheet and profit and loss account as at 31 December 2004 and (c) a comparison table of the company's audited accounts for the period from 31 December 2001 to 31 December 2004. It was apparent from these accounts that by 31 December 2003, the capital of the company was depleted. As at the same date, the total trade creditors amounted to $392,825.00 and the trade debtors was only $38,512.51. It was argued that any reasonable person looking at the accounts for the financial year ended 31 December 2003 ("the 2003 accounts") would have no doubt that the company was not a going concern. The auditor's report to shareholders dated 15 June 2004 on the 2003 accounts was issued with a negative qualification in the following terms:

> ... the company's current liabilities exceeded its current assets by $664,249 and its total liabilities exceeded its total assets by $255,946. These factors raised doubt that the company will be able to continue as a going concern.

A similar negative qualification was given by the auditors in their report for the accounts for the

financial year ended 31 December 2002 ("the 2002 accounts").

7 Counsel for the plaintiff, Ms Gan Kam Yuin, submitted that the defendants' conduct in relation to the unpaid supplies, which went beyond the bounds of ordinary decency, was objectively speaking plainly dishonest. She urged that common decency dictated that the defendants either stop collecting supplies from GIPL between April 2004 and July 2004 or pay GIPL for the undisputed portion of the invoices. Elaborating she explained that even though the price increase of the relevant supplies was being disputed by LSH who claimed that there was an agreement to hold prices at current level, the defendants could have but did not pay the undisputed portion of the invoices. Alternatively, they ought to have returned the unused RC piles to GIPL. The defendants' behaviour deviated from the standard of an ordinary decent person thereby giving rise to an inference of dishonesty on the part of the defendants. Ms Gan relied on *Rahj Kamal bin Abdullah v PP* [1998] 1 SLR 447 ("*Rahj Kamal*") at [30] for the proposition that positive evidence of a dishonest intention was not needed. Dishonesty could be inferred from the surrounding circumstances and from the subsequent conduct of the defendants.

8 The defendants refuted the serious claim of fraudulent trading brought under s 340(1) of the Companies Act. Their counter argument was that it had a dispute with GIPL over the price of the RC piles supplied between April and July 2004. It was not a case of the company's inability to pay GIPL. In support, the defendants pointed out that, save for the disputed GIPL invoices, all third party creditors were paid. Moreover, LSH stopped ordering RC piles from GIPL after the dispute arose and had since 9 July 2004 obtained supplies from other sources such as Power Precast Concrete Pte Ltd, Eastern Union Trading and Sawmill and ECI Corporation Pte Ltd. The third defendant explained that at the end of the day, the company, having lost the case on the disputed invoices to GIPL (*ie* Suit No 784 of 2004/Q), was faced with a sizeable judgment with which the company and its owners did not have the wherewithal to discharge. The failure to satisfy the judgment sum led to the winding up of the company.

9 Furthermore, it was denied that the company was insolvent at the time the RC piles were supplied and collected by the defendants. The auditors of the company did not qualify the accounts as such. The accounts were drawn up on a going concern basis on the assumption of continued financial support of the directors. In other words, the company was able to continue trading legitimately with continued financial support from the source indicated. The continual financial support from the directors was borne out by the evidence. If anything, LSH was insolvent on 28 February 2005, being the date GIPL entered judgment against the company in Suit No 784 of 2004/Q. The rationale was that the debt to GIPL in respect of the RC piles would have only crystallised on 28 February 2005. Yin Kum Choi ("Yin"), an accountant who testified as the defendants' expert, accepted that based on the balance sheet insolvency test the company was insolvent on paper from 2001, but he opined that, having regard to the circumstances of this case, balance sheet insolvency as a test was inappropriate. Yin was of the opinion that the company had the ability to pay its debts as and when they fell due given its resources to pay debts from the company's bank overdraft facility and from directors' financial support in the form of loans. By this, Yin meant that there was no risk of cash flow insolvency (*ie* inability to pay debts as they fall due) until 28 February 2005.

10 In any case, counsel for the defendants, Mr Spencer Gwee, argued that even if it was accepted that the company was insolvent, the non-payment of GIPL's invoices and subsequently the judgment sum did not constitute a breach of s 340(1) of the Companies Act, relying on *Re Sarflax Ltd* [1979] 1 Ch 592 in support of his contention. In that case, the directors ceased trading, collected and distributed the assets to creditors without regard to pending litigation. By the time judgment was entered against the company it had distributed all assets to creditors having failed to make provision for *pari passu* payment to the judgment creditor. The mere preference of one creditor over another

did not amount to an "intention to defraud" even where a director knew or had ground to suspect that his company would not have sufficient assets to pay all the creditors in full. In the present case, between April 2004 and April 2005, the company paid its other creditors a total sum of $909,492.61. What happened here, so the argument developed, was no different from the facts of *Re Sarflax Ltd* in that there was no provision for *pari passu* payment to GIPL of the judgment sum. On the authority of *Re Sarflax Ltd*, there could be no suggestion that the defendants were dishonest and hence caught by s 340(1) of the Companies Act.

11 Section 340(1) of the Companies Act is these terms:

> If, in the course of the winding up of a company or in any proceedings against a company, it appears that any business of the company has been carried on with intent to defraud creditors of the company or creditors of any other person or for any fraudulent purpose, the Court, on the application of the liquidator or any creditor or contributory of the company, may, if it thinks proper to do so, declare that any person who was knowingly a party to the carrying on of the business in that manner shall be personally responsible, without any limitation of liability, for all or any of the debts or other liabilities of the company as the Court directs.

12 It is important to keep in mind that the pre-requisite for the exercise of the court's power under s 340(1) of the Companies Act to declare persons personally liable for the debt, is that it should appear to the court "that any business of the company has been carried on with intent to defraud creditors of the company or … for any fraudulent purpose." Furthermore, there are in s 340(1) references to "intent to defraud", "for any fraudulent purpose" and "knowingly". Plainly, these words connote dishonesty which is an essential ingredient to liability. Thus, there must be a finding of dishonesty on the part of the defendants for a case of s 340(1) to be made out (see *Tang Yoke Kheng (trading as Niklex Supply Co) v Lek Benedict and others* [2005] 3 SLR 263 ("*Tang Yoke Kheng"*) at [10]).

13 The question of whether a person carrying on the business was dishonest was subjective, not objective, in the sense that he personally must have been dishonest. The question of dishonesty is one of fact to be determined by the court based upon an assessment of all the facts and circumstances of the case. The burden of proving fraud lay with the plaintiff as the party alleging it. On the standard of proof, the Court of Appeal in *Tang Yoke Kheng* reiterated that the strength of the evidence required before a court will come to the conclusion that fraud has been perpetrated even in a civil trial will usually be higher than in run-of-the-mill civil claims, notwithstanding that the standard of proof is nominally (and theoretically) the same in all cases. Choo J at [14] stated that "because of the severity and potentially serious implications attaching to a fraud, even in a civil trial, judges are not normally satisfied by that little bit more evidence such as to tilt the 'balance'. They normally require more." In conclusion, he said:

> Therefore, we would reiterate that the standard of proof in a civil case, including cases where fraud is alleged, is that based on a balance of probabilities; but the more serious the allegation, the more the party, on whose shoulders the burden of proof falls, may have to do if he hopes to establish his case.

14 A related matter is the standard of what constitutes honest conduct. Whilst honesty is not measured according to some private standard of a defendant, neither is the objective standard of the reasonable man a proper test. However, that objective standard might serve as a guide in the assessment of whether the defendant was dishonest (see *Tang Yoke Kheng (supra)* at [9]). Commenting on the objective standard, Lord Hoffmann in *Aktieselskabet Dansk Skibsfinansiering v Brothers & Ors* [2001] 2 BCLC 324 ("*ADS v Brothers*")at 334 observed:

> While I quite accept that a defendant cannot be allowed to shelter behind some private standard of honesty not shared by the community, I think that there is a danger in expressing that proposition by invoking the concept of the hypothetical decent honest man. The danger is that because decent honest people also tend to behave reasonably, considerately and so forth, there may be a temptation to treat shortcomings in these respects as a failure to comply with the necessary objective standard. It seems to me much safer, at least in the context of an allegation of fraud, to concentrate upon the actual defendants and simply ask whether they have been dishonest. Judges or juries seldom have any conceptual difficulty in knowing what is meant by dishonesty.

15 The quoted passage from Lord Hoffmann's judgment was approved by the Court of Appeal in *Tang Yoke Kheng* at [9]. Choo J noted that "[t]o rely on the objective standard as a sole test would be exceptional because it would require the court to be convinced that the negative answer given in the factual circumstances was sufficiently indicative of fraud to warrant a finding of fraud." So the subjective intention of the defendant that he has acted in good faith (and a court may draw inferences from the surrounding circumstances of the case as to the defendant's state of mind and his honest intent: see *Tang Yoke Kheng* at [8]) constitutes evidence which the court evaluates and test against the weight of other objective facts available including, if required, the objective standard of what an honest person would have done in the circumstances in assessing the conduct of the defendant which is alleged to be dishonest.

16 With these principles in mind, I now turn to the facts of the present case. The main plank of the plaintiff's case was that LSH was insolvent from as far back as 2001 and that, at least, from 2003 the defendants must have known that the company was insolvent. An insolvent company was definitely not in a position to pay for the supplies ordered between April and July 2004. The plaintiff dismissed as a red herring the defendants' claim that the company had financial resources to draw on, namely, either the bank overdraft or directors' loans. After December 2003, the third defendant did not inject fresh money into the company. From January 2004, salary in the total sum of $51,846.94 which was due to the second defendant but not paid over was treated as his loan to the company. Money from Madam Lim was repaid once Tan Beng Guan ("Tan") paid for the used machines he bought from LSH. The alleged financial support was not real and there was cash flow insolvency. Ms Gan referred me to the case of *Buildspeed Construction Pte Ltd (in liquidation) v Theme Corp Pte Ltd & another* [2000] 4 SLR 776. In that case, there was on the facts balance sheet insolvency; the company had ceased business and there was no continuing financial support from bankers or creditors. The court held that the company in those circumstances was unable to pay its debts as they fall due. In that case, cash flow insolvency was established. Besides, the situation here, so it was argued, was of a company very different from the case before the Hong Kong appellant court in *ADS v Brothers*. Whilst, the Hong Kong appellate court observed that there was no dishonesty and a key point was that the director believed that the holding company would continue financial support for the company and there was no indication from the holding company that it would not continue support. In contrast, Ms Gan pointed out that LSH had no new projects in 2004. There were no revenue streams from new work. The signs all pointed to the company winding down its business. It was a clear case of the defendants obtaining supplies from GIPL without any reasonable prospect of being able to pay or provide payment for the supplies.

17 In my judgment, the case for breach of s 340(1) of the Companies Act was so flimsy that it should never have been advanced. The emphasis is on the need for convincing evidence in a case such as this (see [13] above). The question was not whether there was a reasonable prospect of payment but whether the defendants were personally dishonest. At the risk of repetition, s 340(1) is invoked only where the business of the company had been carried on with intent to defraud. It is not engaged in every case where an individual creditor has been defrauded in the course of the carrying

on of the business of the company. Equally, a company which has borrowed or bought goods on credit while insolvent does not *per se* offend s 340(1). It is necessary to show that the creditor was deceived or misled and the director intended to gain an advantage. Neither would closing down a company by methods which disadvantaged creditors *per se* offend against s 340(1). I quote from and adopt the helpful observations of Lord Hoffmann's in *ADS v Brothers (supra)* at 332:

> In cases in which fraud is inferred, there is almost always … 'something else': a misrepresentation to creditors of the company's position or their prospects of payment or a dishonest intent to gain some personal advantage.

18 In this case, the background facts and particularly, the financial support provided by directors over the years were important and decidedly material in determining whether the business of the company was carried on with intent to defraud GIPL within the meaning of s 340(1) of the Companies Act. As stated, the only creditor in relation to whom the defendants could be said to have had an intention to defraud was GIPL and the only relevant intention in relation to GIPL was the supplies between from 3 April and 10 July 2004. So did the defendants continue to receive supplies knowing that it could not pay for them so much so that the defendants had been knowingly a party to the carrying on of the business of the company with intent to defraud GIPL within the meaning of s 340(1)? In my judgment, it was impossible to reach the conclusion, on the evidence before me, that the business of the company was carried throughout the relevant period with intent to defraud GIPL.

19 LSH was a family company. The directors were all related to each other. The third defendant was father to the second defendant, husband to Madam Lim and brother to the first defendant. The company was also run to a great extent, with a degree of informality that is typical of such family enterprise. In many, if not all, respects, the second and third defendants identified the company's interests with their own, and vice versa. For instance, loans by the second defendant's parents to the company were in the perception of the second defendant, lenders' money rather than the company's. A feature of this case was the so-called second defendant's current account with the company. This account was referred to as a "running account". The terminology "running account" was, in my view, a misnomer given how it was operated. Monies would be withdrawn by the second defendant in advance to meet the expenses of the company such as wages and to pay suppliers. I would characterise (and I so find) the monies withdrawn from the company as a cash float to meet the expenses of the company.

20 The company was in the business of piling and general contractors. The third defendant started the business and in 1998 incorporated the company to take over the business of the sole proprietorship. After a couple of years of business, LSH's business began to run into difficulties sometime in 2001. Both the second and third defendants had, in my view, an honest belief that they could turn the company around and were working hard to do so. The third defendant said that the company suffered losses in 2001, but with cost saving measures and control over finances, it managed to recover from the 2001 losses to register some profits, albeit negligible profits in 2002 and 2003. However, the company's audited accounts for the year ended 31 December 2003 showed, *inter alia*, accumulated losses exceeding the paid up capital by $255,946.00 and cash on hand of only $656.00. LSH's only assets were trade debts and small sums of deposits and prepayments. A year later, LSH's financial problems only worsened. Its own internal balance sheet reflected liabilities exceeding assets by $510,457.38, accumulated losses to the tune of $810,457.38 and a net loss for the financial year ended 31 December 2004 of $254,512.30.

21 The history of this company as Yin noted was one where financial support from directors, who were also shareholders, was evident right from early days well before the dispute over the price of the subject supplies. Over the years, the directors were financing the operations of the company.

When examined in the actual setting in which the RC piles were purchased between April and July 2004, the fact that the company was in the red and its assets outstripped its liabilities was not determinative and could hardly constitute evidence of dishonest intention on the part of the defendants to carry on the business of the company to defraud the creditors or GIPL. This was because the insolvency appeared on the face of the balance sheet and did not, and I so find, reside in an inability to pay debts as they fall due. It could not be said that there was no reasonable prospect of meeting the GIPL invoices for the supplies from April to July 2004.

22 It is a convenient to pause here for a moment to mention that the first defendant was not a director at the time of the subject supplies. He was made a director around 26/27 July 2004 and prior to his appointment, he had never participated in the management of the company. In the circumstances, it was difficult to imagine how he could have been a person who was knowingly a party to the carrying on of the business with intent to defraud creditors or a single creditor, namely GIPL, within the terms of s 340(1). There was no evidence that the first defendant was a participant or had concurred in the activity which constituted the dishonest act to cheat GIPL. I had no hesitation dismissing the plaintiff's claim against the first defendant.

23 Reverting to the position of the second and third defendants, the company continued to pay its expenses and creditors (except GIPL) up to the time of winding up. Between April 2004 and April 2005, the company paid its other creditors a total sum of $909,492.61. During the period when the company was insolvent by the plaintiff's reckoning, the company had business dealings with GIPL and it paid GIPL $1,797,469.32 from 2001 up to June 2004 for all invoices except for the supplies between April and July 2004. The fact that the overdraft facility was not used to settle the subject supplies or that it was terminated in October 2004 was as I said not determinative nor did it changed my analysis of the evidence.

24 The last payment in June 2004 for the March 2004 invoice was routine and no different from the way LSH and the second and third defendants had acted in the past and in their dealings with GIPL. Payment term under the GIPL statement of account was 30 days but the company commonly paid on or after 90 days. The non-payment of the RC piles supplied between April and July 2004 was on account of an ongoing dispute with GIPL. The plaintiff argued that the alleged dispute was a sham. GIPL succeeded in obtaining summary judgment against the company thereby demonstrating convincingly that the dispute was not genuine. LSH's defence and counterclaim was a sham. I have already commented on the claim against the first defendant in [22] above. As for the other two defendants, were the second and third defendants out to cheat GIPL, one might have expected them to continue to place orders with GIPL and to string GIPL along with promises to pay in the near future. The evidence before the court was the complete opposite (see [8] above). There was unchallenged evidence that the third defendant tried, but was unsuccessful in his attempts, to reach an amicable settlement with GIPL. GIPL insisted on full payment, albeit, payment by instalments was acceptable. Evidence of attempts at settlement militated against the plaintiff's claim that the second and third defendants were out to cheat GIPL. The fact that legal advice was sought after the action was started by GIPL did not mean that the second and third defendants could not have come to the conclusion that GIPL had gone back on its promise not to increase prices until after completion of the Benoi and Tanglin Hill projects. The fact that the company lost the litigation and also discontinued the counterclaim one month thereafter was not compelling support for the plaintiff's allegations of fraudulent intent. Even though LSH's defence was weak, it did not translate into evidence of the defendants' dishonesty. On the face of it, on legal advice, LSH's counterclaim was apparently more than the plaintiff's claim. The third defendant's testimony was that the company defended the claim and put forward a counterclaim on legal advice. The plaintiff won and the counterclaim was discontinued. The overall evidence, on a balance of probabilities, pointed to the third defendant's perception that GIPL had reneged on its promise and I found that the decision not to pay for the

supplies was on account of this dispute with GIPL. Thus the plaintiff's contention that the second and third defendants had been carrying on business with an intention to defraud GIPL was plainly unfounded.

25 The fact that the defendants chose to pay other creditors did not take the matter any further. If anything those payments showed an intention to give preference to the some creditors (*eg* Madam Lim) and would not suffice to establish an intention to defraud others like GIPL. Andrew Ang JC (as he then was) in *TangYoke Kheng (trading as Niklex Supply Co) v Lek Benedict & Others (No 2)* [2004] 4 SLR 788 cited the decision of *In re Lloyd's Furniture Palace Ltd* [1925] Ch 853, where it was held that the preference of a creditor who was himself a director shareholder and the promoter of the company could not amount to fraudulent trading without more. This position was also made clear in *Re Sarflax Ltd* (*supra* at [10]).

26 For all these reasons, the plaintiff's claim that there was fraudulent trading within s 340(1) of the Companies Act failed as it was not made out in the present case.

Undue preference under section 329 of Companies Act

27 The claim here concerned a sum totalling $430,066.34. The plaintiff alleged that the transfer to the second defendant of a debt owed by LSH to the third defendant totalling $376,176.48 on 27 July 2004 which was followed by two payments made by LSH in favour of the second defendant in August 2004 and September 2004 ("hereafter collectively referred to as "the cash payments") amounting to $430,066.34 were undue preferences within the meaning of s 329(1) of the Companies Act read with ss 98 to 100 of the Bankruptcy Act. The cash payments were undue preferences as there was plainly a desire to prefer. The plaintiff contended that the company was already insolvent when the cash payments were made to the second defendant or the company was made insolvent by those cash payments. Alternatively, since the cash payments took place more than six months, but less than two years prior to the onset of the company's insolvency, this entailed the proposition that the second defendant as recipient of the benefit of the cash payments was "an associate" of the company so that the period for invalidating the cash payments under s 100(1)(b) of the Bankruptcy Act should be extended to two years (see ss 99, 100 and 101 of the Bankruptcy Act read together with Companies (Application of Bankruptcy Act Provisions) Regulations (Cap 50, Rg 3, 1996 Rev Ed) ("Companies Regulations"). Regulation 4 provides that an "associate" refers to "a person connected with a company" which is defined, *inter alia*, to mean a person who is a director of the company.

28 It is a convenient juncture to mention that according to Yin, the company was insolvent on 28 February 2005. If anything, the company would have failed the liquidity test, at the earliest, in October 2004. By then the used machines were sold and the overdraft facility terminated. However, I did not find it necessary to make a finding on when exactly the company was insolvent. The company was wound up in April 2005 as it was unable to pay its debt. The petition to wind up the company was filed on 4 April 2005. The cash payments took place less than two years prior to the presentation of the petition or the commencement of winding up and the second defendant as a director of LSH was "an associate" of the company within the meaning of the relevant provisions. It was not disputed that s 99(5) read with s 101(4) of the Bankruptcy Act applied such that it fell on the second defendant to rebut the statutory presumption that the cash payments to the second defendants were influenced by a desire to prefer the second defendant.

29 In support of his claim, the plaintiff relied on several interdependent facts. First, he argued that, contextually, the defendants were well aware of the company's precarious financial situation since 2001 when its balance sheet showed significant deficits. The accumulated losses over assets grew over time. Second, as at July 2004, the second defendant was owed only $51,846.94 by LSH.

On the other hand, the third defendant was owed $376,176.48 by LSH. However, following the third defendant's assignment of the debt to the second defendant, the company's indebtedness to the second defendant increased by $376,176.48. Consequently, the total debt owing to the second defendant after the assignment was $428,023.42. At the date of the winding up, LSH purportedly was indebted to the second defendant in the sum of $237,188.21. By assigning his debt on 27 July 2004, the end result was that a sum of $237,188.21 was owed by LSH to the second defendant thereby putting him in a better position than he would otherwise have been in when the company is placed in liquidation. Had there been no assignment, the second defendant would have instead owed LSH a sum of $138,988.27 and the second defendant would have to make good this indebtedness. Third, the total sum of $430,066.34 withdrawn by the second defendant in August and September 2004 came from funds provided by Madam Lim (through Guan Soon), which represented the only substantial inflow of funds which LSH possessed in the entire year. In October 2004, the company repaid Madam Lim's loan and in the same month the overdraft bank facility was cancelled and the used machines sold earlier was also delivered to Tan in October 2004.

30 The second defendant denied that there was any undue preference. The cash payments were intended for the purchase of new piling equipment from China.[note: 1] The purchase did not materialise. The second defendant thence utilised the cash payments to pay LSH's expenses and trade creditors. He also returned some money to the company. As for the payments retained by the second defendant, it was said that there was a running account between the second defendant and LSH and that those payments were made pursuant to that running account.[note: 2] Mr Gwee submitted that the second and third defendants had mutual dealings with the company and they were therefore entitled to set off the debts due to them. Counsel maintained that to rebut the statutory presumption, the second defendant's conduct before, during and after receipt of the cash payments had to be considered.

31 The third defendant averred that the assignment of the debt was, *inter alia*, to incentivise the second defendant. The third defendant was suffering from ill health and his intention was to continue the business under the second defendant who could bring new ideas into the business. Madam Lim's loan was to assist the company to buy new equipment from China. That was said to be consistent with the third defendant's intention to continue with the business under his son as opposed to ceasing business, a claim made by the plaintiff. In July 2004, the company had an unutilized bank overdraft of $800,000.00 which was cancelled in October 2004. As for his decision to cancel the overdraft facility, he claimed that he needed money for his medical expenses.

32 In the recent decision of *Amrae Benchuan Trading Pte Ltd (in liquidation) v Gregory Tan Te Teck* [2006] 4 SLR 969 at [51], Sundaresh Menon JC helpfully distilled the relevant principles applicable in deciding whether a transaction may be successfully challenged as an undue preference:

(a) A person is taken to intend the natural consequences of his action. As every payment or grant of security potentially has the effect of preferring the payee or the grantee in the event of the paying company's subsequent insolvency, something more has to be shown. Otherwise, the question of preference would be determined in every case simply by undertaking an objective inquiry into whether in effect there had been a preference.

(b) The legislation in its previous form provided that what had to be shown was that the achievement of the preference was the predominant intention. That is no longer the case. What needs to be shown under the law as it now stands is that the payment was influenced by the desire to improve the creditor's position in the event of an insolvent liquidation.

(c) The analysis is to be undertaken by reference to the time of the impugned transaction.

(d) Where the challenged transaction involves an associate, there is a rebuttable presumption that the company entered into that transaction under the influence of the relevant desire. In such a case, the court will examine all the facts, and determine whether on a balance of probabilities the presumption had been rebutted.

33 Although the cash payments totalled $481,640.34, only the sum of $430,066.34 was claimed as a preference. This was because the liquidator had accepted some payments thereby limiting the complaint to $430,066.34. I found his approach questionable and it showed that the liquidator had cherry-picked the evidence by allowing some deductions for expenses but not others. I shall elaborate on this observation shortly. Suffice it to say, even if it was accepted, for the sake of argument, that the various payments made by the second defendant were to be disregarded as was argued for by the liquidator, I did not think that the circumstances in context reflect the purpose of the voidable preference provisions.

34 I begin with an examination of the cash payments. Notably, the cash payments and the subsequent utilisation of the cash payments must be examined in the actual setting in which they took place. By way of background facts, Ms Gan in her closing submissions accepted as "true that the company maintained some sort of running account(s) and there were instances where the defendants or some of them helped support the company financially." This so called "running account" comprised a mixture of monies drawn by the second defendant from the company's bank account and monies collected by him for the company and monies paid out by him for the company's expenses and monies due to him as salary from the company. As I have explained earlier, this so called "running account" was a misnomer. The bulk of the money was money belonging to the company and held by the second defendant as an intermediary (a term used by Mr Gwee) to disburse payments for and on behalf of the company. Hence, on an analysis of the evidence, money taken by the second defendant from the company's account was a cash float to meet the company's expenses and pay trade creditors (see [19] above).

35 Ms Gan also rightly agreed that the cash payments in August and September 2004 were very similar in pattern to previous withdrawals or payments to meet the expenses and liabilities of the company. That the cash payments were simply a repetition of past patterns of behaviour made it more difficult, in my judgment, for the liquidator to argue that the cash payments represented an unfair preference.

36 Equally, an examination of the various payments of expenses and trade creditors in the actual setting in which they took place and with reference to the cash payments showed that they were similar to transactions undertaken in the past in the ordinary course of business. Yin in his expert report stated:

> 4.11 ... for the period August 2004 to April 2005, the cash withdrawal by Mr Tony Chan totals $553,629.94 and in turn [the amount] paid out on behalf of the company as expenses [totalled] $197,794.73 and [the second defendant] returned $165,000 to the company. The net amount withdrawn by Tony Chan for this period is $190,835.21.

Separately, the plaintiff's statement marked "Annex A" tendered in answer to the further and better particulars sought by the defendants in respect of paragraph 5 of the plaintiff's Reply showed a total sum of $482,281.65 paid to creditors in the period from August 2004 up to March 2005. The liquidator realising the situation, allowed only some payments which explained his claim of $430,066.34 and not the full sum of $481,640.34 withdrawn in August and September 2004. But as I have earlier indicated, the liquidator's approach was questionable for the reasons stated in [35] and [36] above.

37 I accepted Yin's evidence that the liquidator did not consider the entire list of cash payments referred to in paragraph 4.1 of his expert report as well as some of the monies returned by the second defendant to the company. As for the return of monies, Yin said in cross-examination that the amount returned to the company was $70,000.00 but that sum was not taken into consideration by the liquidator. Ms Gan in her closing submissions clarified that $50,000.00 was not taken into account because it was paid into the company on 18 August 2004 before the withdrawal of $351,401.28. A further sum of $20,000.00 was returned on 28 September 2004 which was before the 30 September 2004 withdrawal in the sum of $130,239.06. I should imagine that at least the $20,000.00 should have to be taken into account by the liquidator.

38 In my judgment, the second defendant was obliged to rebut the statutory presumption in respect of the net balance of $190,835.21. He appeared to have kept this sum of money as he was himself a creditor. This was also the amount recorded in the company's books as paid as at the date of winding up of the company. Did the second defendant use this sum to prefer himself? Was this the sum the second defendant should pay back as preference?

3 9 As for this sum of $190,835.21, the second defendant argued that he was entitled to offset this amount against the total debt owed to him by the company *ie* $428,023.42. The accounts showed that by end December 2004, the balance of the debt owed by the company to the second defendant was reduced to $141,493.56. If we stop there, the undue preference arguable was $286,529.86 (*ie* $428,023.42 minus $141,439.56). However, in the following year, the second defendant had returned to the company some more money, namely, $95,694.65 so much so that from $141,493.56, the balance of the second defendant's account with the company changed to $237,188.21. This was possible because the cash payments were more that the sums disbursed and given back to the company collectively. In my view, the second defendant preferred to himself the balance of the cash float being as he saw it he was entitled to a set-off.

40 I disagreed with Mr Gwee's contention that the second defendant could offset what was owed to him from the cash payments. In my judgment, there was no such right of set-off. This is because and I agreed with Ms Gan that there was no real mutuality of debts. The money that the second defendant used to prefer himself came from the cash float which was the company's money. It was not a debt that the second defendant owed to the company which he could offset against the debt the company owed to him. The amount of the preference represented money that was refundable to the company. It was contrary to the statute to prefer one creditor over another and not because the creditor truly owed any money to the company.

41 For completeness, I now turn to the liquidator's assertion that the assignment was bad as it constituted an undue preference. The liquidator's contention that the assignment was an undue preference was untenable. First, the assignment itself could not have amounted to a "preference" as there was no net reduction in the company's assets as a result of the assignment. The assignment simply substituted one creditor for another. Notable, all of the debts to directors were unsecured. The second defendant was not put in a better position than the third defendant. Second, if there was no assignment, money from the cash float would probably have been used to pay the third defendant. As it transpired, the second defendant utilised the balance of the cash float to pay in part the debt owed to him by the company.

42 In my judgment, the second defendant had not rebutted the statutory presumption in respect of the sum of $190,835.21. Consequently, he was ordered to pay back this sum of money. For avoidance of doubt, the second defendant remained an unsecured creditor of the company in the sum of $428,023.42.

Result

43 For the reasons stated, the plaintiffs failed in his claim against the defendants under s 340(1) of the Companies Act but succeeded against the second defendant on a claim for undue preference in respect of the sum of $190,835.21. The plaintiff was ordered to pay costs of the action to the first and third defendant. As against the second defendant, the plaintiff was awarded 50% of the costs of the action.

[note: 1] Second defendant's affidavit at [12]

[note: 2] Second defendant's affidavit at [8]