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Restructuring & Insolvency

# Ratification of Agreements by the Court in Bankruptcy

## Introduction

In order to preserve a bankrupt's assets for distribution to creditors, any disposition of the bankrupt's property from the date of the bankruptcy application is considered void. However, this position is not absolute – the Court may consent to or ratify the disposition. In *Sutherland, Hugh David Brodie v Official Assignee* [2021] SGHC 65, the Singapore High Court set out the applicable principles that it would take into account when considering whether to ratify such disposition.

The arrangement in this case was for the applicant to make payments on behalf of the debtors to stave off a mortgagee sale of the debtors' property so as to obtain a better price than in a mortgagee sale, and that the applicant would be repaid from the surplus sale proceeds ahead of unsecured creditors. The arrangement was recorded in an assignment agreement. However, the debtors were soon made bankrupt, and the Official Assignee considered the agreement to be void.

On an assessment of the facts, the Court ratified the agreement. The Court found that the agreement was made in good faith, that it would benefit the interests of the creditors, and that it would be fair and just to ratify the agreement.

This Update provides a summary of the case and the key points of the Court's decision.

## Brief Facts

The Debtors had been facing claims from creditors and sought to propose a joint voluntary arrangement. As part of this, the Debtors intended to sell their Property. However, the Property was mortgaged to a bank.

The Debtors sought the help of their friend, the Applicant, in making payments totalling \$414,000 to the bank to repay the mortgage instalments so that the Debtors could sell the Property on the open market and obtain a better price than in a mortgagee sale. The arrangement was that the Applicant would be repaid from the surplus sales proceeds after the bank was paid, but ahead of the Debtors' unsecured creditors. The Applicant did not seek any interest on the payments. This arrangement was recorded in an Assignment Agreement.

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The Debtors were made bankrupt before they could sell the Property. There was then a mortgagee sale which generated a surplus of about \$1 million over what was owed to the bank. However, the Official Assignee took the position that the Assignment Agreement was void under section 77(1) of the Bankruptcy Act ("**BA**") because it was entered into only after the bankruptcy application against the Debtors had been filed. The Applicant was thus only an unsecured creditor and would only receive a small fraction of what he paid to the bank.

The Applicant thus brought proceedings seeking ratification of the Assignment Agreement under section 77(1) of the BA.

## Holding of the High Court

The Court ratified the Assignment Agreement, allowing the Applicant to be repaid for his payments to the bank ahead of the unsecured creditors.

### Ratification under the BA

Section 77(1) of the BA provides that, where a person is adjudged bankrupt, any disposition of property made by him from the making of the bankruptcy application until the making of the bankruptcy order shall be void, unless the disposition has been made with the consent of, or been subsequently ratified by, the Court.

The purpose of this provision, which has been retained as section 328(1) of the Insolvency, Restructuring and Dissolution Act, is to preserve the bankrupt's assets for orderly and rateable distribution to the general body of creditors.

The Court set out the applicable principles in the test for determining whether to ratify an agreement under section 77(1) of the BA.

- (a) The first consideration is whether ratification promotes the objective of this provision (preserving the bankrupt's assets for orderly and rateable distribution) or undermines it.
- (b) A disposition that was in the interests of the general pool of creditors fits with the objective of the provision, and may be ratified if it is otherwise fair and just.
- (c) In determining what was in the interests of the general pool of creditors, the Court should ask whether, at the time the disposition was made, it was likely to benefit the general pool of creditors.
- (d) Good faith, notice, and value will be relevant when considering ratification, but how important or necessary they are will have to be considered as part of the overall exercise of discretion.

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**Application**

On the facts, the Court found that the arrangement in the Assignment Agreement resulted in benefit to the creditors. The unsecured creditors benefited from not having to deduct from the sale proceeds the amount of interest payable to the bank on the \$414,000 advanced by the Applicant. The Court stated that it would not be fair or just for the unsecured creditors to take the benefit of this saving – and in addition share rateably in the \$414,000 advanced by the Applicant – if the Assignment Agreement were to be void.

The Court further found that the intention of the parties was for the Applicant to be paid ahead of the unsecured creditors, and that the Applicant had acted in good faith throughout. Therefore, the Court considered that this was an appropriate case for ratification of the Assignment Agreement.

**Concluding Words**

The Court's decision provides a guide as to how it will approach applications for the ratification of dispositions of property by a bankrupt from the day of the making of a bankruptcy application till the making of the bankruptcy order, which are otherwise void. The Court is likely to ratify a disposition when it furthers the objective of preserving the bankrupt's assets for orderly and rateable distribution, and is otherwise fair and just.

For further queries, please feel free to contact our team below.

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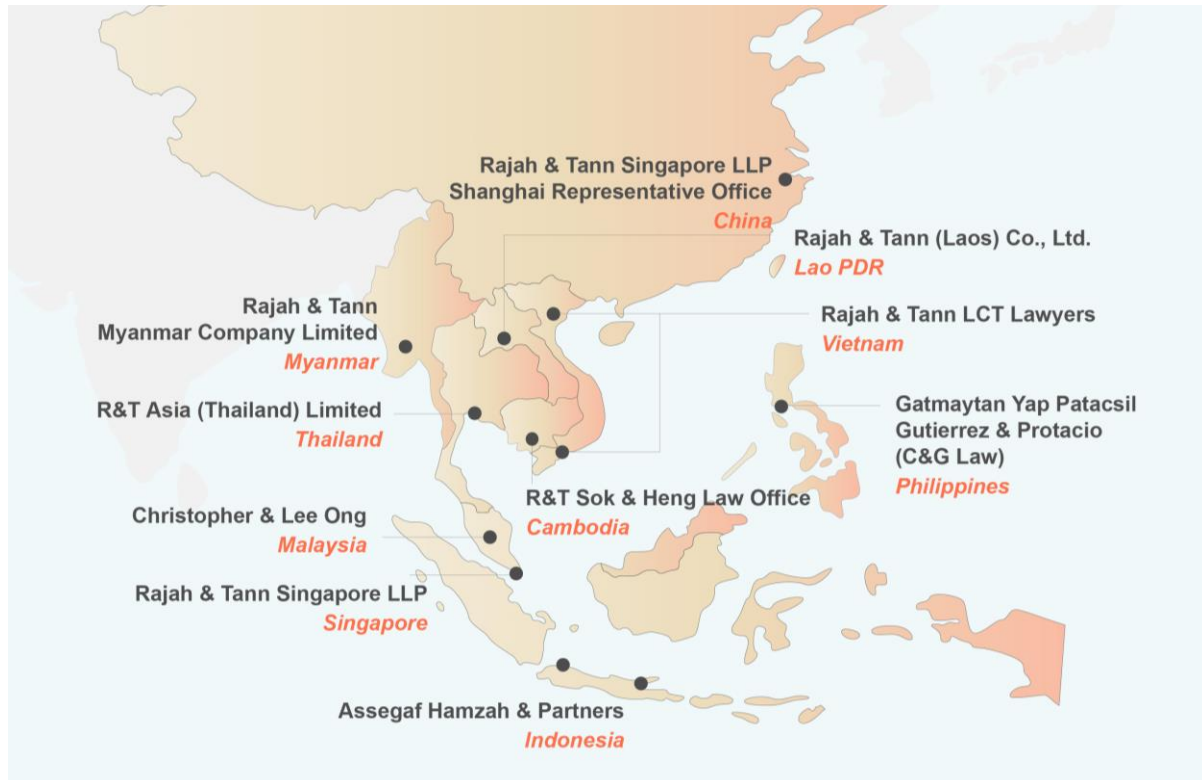
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