Mergers & Acquisitions | Restructuring & Insolvency

Challenges to the One-Proxy Rule in a Recent Trust Scheme of Arrangement

Introduction

Since 2017, there has been a wave of consolidation and privatisation of real estate investment trusts ("**REITs**"), business trusts, and stapled trusts which have been effected through trust schemes of arrangement ("**Trust Schemes**") in accordance with the provisions of the Singapore Code on Take-overs and Mergers (the "**Code**") and the applicable trust deed(s).

For a Trust Scheme to be implemented, approvals required include:

(1) Approval of unitholders for amendments to the trust deed: the approval of the unitholders holding in the aggregate not less than three-fourths of the total number of votes held by the unitholders present and voting either in person or by proxy at an extraordinary general meeting to approve amendments to the applicable trust deed(s) to include provisions that will allow for a Trust Scheme to be effected;

(2) Approval of unitholders for the Trust Scheme: the approval of a majority in number of unitholders ("**headcount test**") representing at least three-fourths in value ("**value test**") of the units held by the unitholders present and voting either in person or by proxy at a meeting convened to approve the Trust Scheme;[1] and

(3) Approval of the Court: the grant of the approval for the Trust Scheme from the High Court of the Republic of Singapore ("**Court**") under Order 80 of the Rules of Court ("**Order 80**").[2]

Unlike for companies in Singapore where the Companies Act (Chapter 50) of Singapore ("**Companies Act**") prescribes a statutory framework and process for schemes of arrangement involving companies ("**Company Schemes**")[3], there is no prescribed statutory framework for Trust Schemes, although the Courts has taken jurisdiction over Trust Schemes pursuant to Order 80.

Contribution Note: *This Legal Update was written with contributions from Charmaine Saw, Associate, Capital Markets / Mergers & Acquisitions.*

[1] Paragraph 12(e) of the "Definitions" section of the Code.
[2] Chapter 322, R 5 of Singapore.
[3] The Insolvency, Restructuring and Dissolution Act 2018 (No. 40 of 2018) also sets out provisions in relation to a scheme of arrangement between a company and its creditors.

The market practice to date has therefore been to follow closely the established practice and process for Company Schemes for similar M&A transactions. To that effect and for the purpose of implementing the Trust Scheme in accordance with the provisions of the Code, the proposed amendments to the trust deed usually include a provision that each unitholder (i) shall be entitled to appoint only one proxy to vote at the Trust Scheme meeting, and (ii) may only cast all the votes it uses at the Trust Scheme meeting in one way ("**one-proxy rule**"). The one-proxy rule approach is consistent with the practice for Company Schemes, where the proxy rules are provided for under Section 181 of the Companies Act.

Although the one-proxy rule is consistent with industry practice (for Company Schemes as well as Trust Schemes), an issue which may arise is whether its application distorts the voting results, in particular, where investors hold units indirectly through a custodian or nominee ("**Relevant Intermediary**"[4]).

How then can commercial parties mitigate the risk of challenge to a Company Scheme/Trust Scheme on the basis that the one-proxy rule should not have been applied?

Background Facts

On 14 December 2020, the manager of Soilbuild Business Space REIT ("**SB REIT**" and the manager of SB REIT, "**SB Manager**") and Clay Holdings III Limited jointly announced the proposed acquisition of all the issued units in SB REIT by Clay Holdings III Limited, to be effected by way of a Trust Scheme in accordance with the Code.

On 8 February 2021, the SB Manager and the trustee of SB REIT (collectively, "**Applicants**") sought and obtained leave of Court to convene a Trust Scheme meeting in the manner set out in the application including, but not limited to, a direction for the adoption of the one-proxy rule for the purpose of voting at the Trust Scheme meeting.

The Trust Scheme was approved by 427 out of 755 unitholders (i.e. 56.56% in number) holding an aggregate of 234,299,582 out of 262,324,727 units (representing 89.32% in value) of the unitholders present and voting, by proxy, at the Trust Scheme meeting held by electronic means on 11 March 2021. Each unitholder who was a Relevant Intermediary, and who voted, cast one vote in accordance with the one-proxy rule.

The Applicants accordingly filed an *ex parte* application for Court approval of the Trust Scheme, and approval of the Trust Scheme was fixed for hearing on 25 March 2021.

At the hearing, counsels representing a unitholder opposed the application on the ground that the one-proxy rule should not have been used in respect of the Trust Scheme meeting as it forced all unitholders, including the Relevant Intermediaries, to submit only one vote "for" or "against" the Trust Scheme. The arguments raised in Court in objection included that it may not be representative of the votes of indirect unitholders which hold the units of SB REIT through the care of Relevant Intermediaries such as

[4] "Relevant intermediaries" are those which fall within the definition under Section 181(6) of the Companies Act.

nominee and custodian banks both in respect of the headcount test and the value test, as the Relevant Intermediaries are required to vote only one way, in accordance with the interests of the majority of the unitholders under its charge and potentially disregarding the votes of the minority unitholders under its charge.

At the hearing on 25 March 2021, in view of the concerns raised by the dissenting unitholder, the Court directed the Applicants to obtain the voting instructions, in aggregated form, received by each Relevant Intermediary in respect of the Trust Scheme resolution tabled for approval at the Trust Scheme meeting held on 11 March 2021. The hearing was accordingly adjourned to 30 March 2021.

The relevant information was tendered to the Court at the hearing on 30 March 2021. Based on the information obtained from the Relevant Intermediaries who voted, assuming the clients of the Relevant Intermediaries had submitted their votes directly as unitholders on the Trust Scheme resolution (instead of applying the one-proxy rule), the Trust Scheme resolution would still have carried.

After considering the material before it, the Court held that the procedure that the Applicants had followed in respect of the Trust Scheme was in accordance with the relevant legislation and the trust deed of SB REIT (before and after amendment), and consistent with industry standards, as with past cases of Trust Schemes. Further, the Court was satisfied that the Applicants had discharged their duty to make full and frank disclosure, and that the Court was not able to make any finding on the material presented that the voting outcome would have been different if the one-proxy rule had not been adopted. The Court accordingly granted the application for approval of the Trust Scheme.

One-Proxy Rule

The one-proxy rule is generally applied in the context of Company Schemes/Trust Schemes for clarity in determining whether the headcount test is satisfied. This is unlike voting on extraordinary or ordinary resolutions at general meetings of a company/trust where there is no headcount test requirement and shareholders/unitholders may vote in more than one way on different blocks of shares/units.

To illustrate in the context of a Trust Scheme, if a unitholder were allowed to vote in more than one way for a Trust Scheme and is counted as having voted both "for" and "against" the Trust Scheme resolution, his votes would effectively cancel each other out for the purposes of the headcount test. This would neither be an accurate or fair representation of unitholders' sentiment in respect of the Trust Scheme.

Further, where a unitholder who holds units through Relevant Intermediaries wishes to have his vote count, both in terms of the units he holds, and in terms of headcount, he is at liberty to take steps to have the units registered in his own name, save in certain circumstances.

It should also be noted that the question of allowing for multiple proxies for Relevant Intermediaries was considered by Parliament in the context of Company Scheme meetings.

Section 181 of the Companies Act, which provides the framework for appointing proxies of members of companies at general meetings, was amended pursuant to the Companies (Amendment) Act 2014 to include Sections 181(1B) and (1C) of the Companies Act.

While Section 181(1C) of the Companies Act allows Relevant Intermediaries to appoint more than two proxies to vote at a meeting of members ("**multiple proxy rule**"), Section 181(1B) of the Companies Act expressly provides for an exception to Section 181(1C), which states for the purposes of a meeting held for a Company Scheme, a member is, unless the Court orders otherwise, "*entitled to appoint only one proxy to attend and vote at the same meeting* [emphasis added]".

Section 181(1B) of the Companies Act was enacted to give effect to the modified recommendation of the Steering Committee for Review of the Companies Act, which originally provided that "*[f]or the purposes of section 210, if a majority in number of proxies and a majority in value of proxies representing the nominee member voted in favour of the scheme, it would count as the nominee member having voted in favour of the scheme*"[5].

The introduction of Section 181(1B) of the Companies Act makes it clear that Parliament was alive to the issue of voting by nominee members for the purposes of Company Schemes, yet decided not to apply the multiple proxy rule for Company Scheme meetings, unless otherwise directed by the Court.

Given the reasons above, practitioners in Singapore have generally adopted the one-proxy rule for the purposes of voting at Company Scheme meetings (and, by analogy, Trust Scheme meetings).

Duty to Give Full and Frank Disclosure

Given that an application for Court approval of a Trust Scheme is usually filed on an *ex parte* basis, the applicant has an obligation to make full and frank disclosure to the Court and to provide the Court with all relevant information necessary for it to make its decision. Even though the one-proxy rule is established industry practice, where it is to be applied, an applicant for a Trust Scheme may need to consider taking steps to satisfy the Court that its application of the proxy regime did not disenfranchise minority unitholders. This may include ascertaining and providing the Court with the instructions received by a Relevant Intermediary in respect of the Trust Scheme resolution.

Possible Impact for Future Company Schemes and Trust Schemes

Although the Court accepted that no prejudice had been caused in SB REIT adopting the one-proxy rule for the Trust Scheme meeting, it observed that the one-proxy rule may have the potential to cause prejudice in certain cases.

[5] Explanatory Statement to Clause 97 of the Companies (Amendment) Bill No. 25/2014. See also the Report of the Steering Committee for Review of the Companies Act (June 2011), Recommendation 3.41.

Given the Court's observations and in the light of increasing concerns raised by shareholders/unitholders in respect of the use of the one-proxy rule for Relevant Intermediaries, an applicant for a Company Scheme/Trust Scheme may wish to consider taking additional steps to satisfy the Court that the outcome of a Company Scheme/Trust Scheme meeting would not be different had a different proxy regime been utilised.

An applicant may also need to consider whether to apply for the Court to direct a different regime of proxy voting for the Company Scheme/Trust Scheme meeting. An example would be the multiple proxy rule, which would allow for the votes at the Company Scheme/Trust Scheme meeting to be counted on a "see-through" basis, to allow for clients of the Relevant Intermediaries to each submit their votes directly as if they were direct unitholders. In the context of Company Schemes, the application of a different proxy regime from the one-proxy rule will require leave of Court pursuant to Section 181(1B) of the Companies Act. There are however potential complications and issues with such a multiple proxy regime, which will need to be further discussed and resolved with relevant advisers.

In any case, irrespective of whichever proxy regime is adopted for future Company Schemes/Trust Schemes, proper disclosures ought to be put in place to ensure that persons who hold shares/units through Relevant Intermediaries are well aware of the implications of holding such shares/units through Relevant Intermediaries.

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