

# LEGAL NEWSLETTER

## BANKRUPT'S CAPACITY TO CONTRACT



# DISQUALIFICATIONS OF A BANKRUPT



Under section 36–38 of the Insolvency Act 1967 (“the Act”), a bankrupt is disqualified from doing or participating in an array of matters. For example, a bankrupt without the prior sanction of the Director General of Insolvency:

Cannot maintain any civil action other than for personal injuries (Section 38(1)(a) of the Act).

Cannot leave the country (Section 38(1)(c) of the Act).

Cannot carry on any business (Section 38(1)(d) of the Act).

Cannot participate or manage any business carried out by relatives as listed under the Act (Section 38(1)(e) of the Act).

In general, there is no blanket legal provision which disallows a bankrupt from entering into a contract. In the case of *Foo Fatt Chuen v. Jacobsen Cheong Weng Hin & Ors* [2012] 8 MLJ 522, the court stated the following:

“THE LAW ON CONTRACTS ENTERED INTO BY A BANKRUPT

[46] ... True enough in *Kwan Chew Shen v Citibank NA* [1987] 2 CLJ (Rep) 704, for instance, it was held that there appeared to be no blanket provision anywhere in the Bankruptcy Act to the effect that a bankrupt was incapable of entering into a contract. It is of significance to note the following passage by VC George J (as His Lordship then was) from the case to give the ruling its proper context:

Before concluding it is perhaps relevant to consider one other aspect of the matter based on the wide belief that once a person is adjudged bankrupt the right to enter into contracts ceases until such time as he is discharged.

This is an erroneous belief.

... while he may not enter into a contract that would amount to his carrying on a business, it is significant that there is no blanket prohibition, express or implied, for a bankrupt to enter into a contract (at p 708 of the report).”



# Can a bankrupt enter into contracts?

# A contract entered into by a bankrupt may be unenforceable if it meant contravening any disqualifications under the Insolvency Act 1967

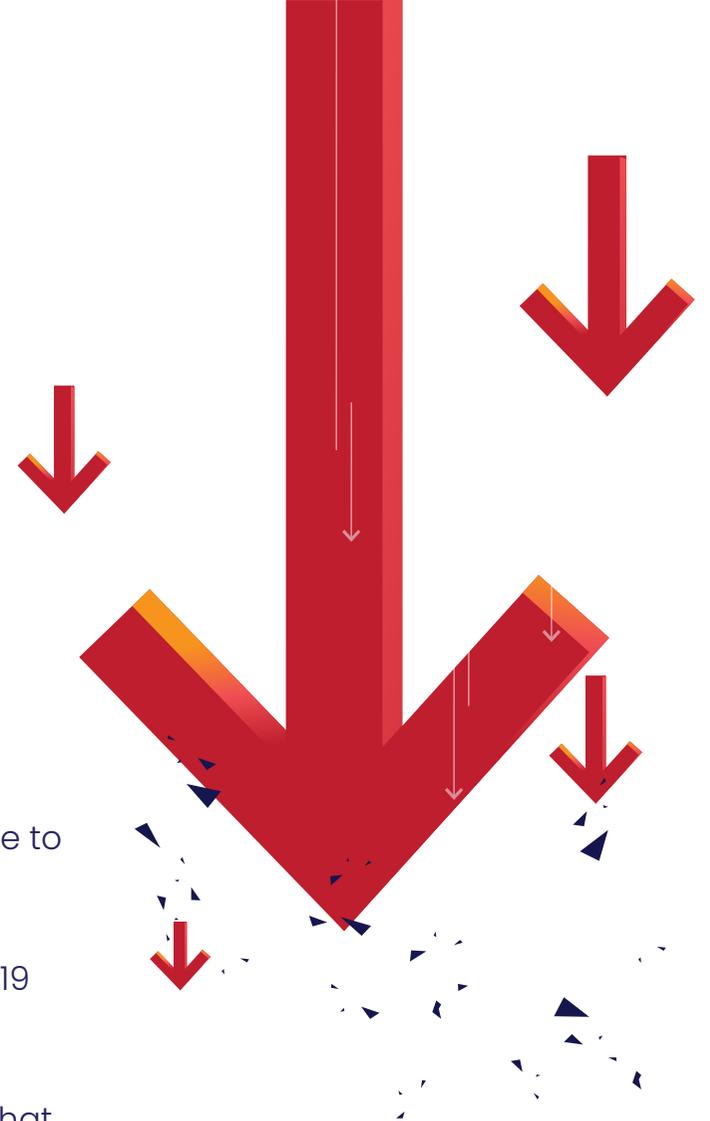
**Foo Fatt Chuen v. Jacobsen Cheong Weng Hin & Ors [2012] 8 MLJ 522**

## **Brief Facts:**

- The Plaintiff and the First Defendant (a bankrupt) had entered into a joint venture to develop pieces of land in Papua New Guinea into large housing development projects;
- Consequently, both parties had entered into a memorandum of agreement on 19 November 2009 and a supplemental agreement on 13 January 2010 ("the agreements");
- Subsequently, disputes arose between the parties and the Plaintiff contended that the First Defendant did not have any enforceable rights under the agreements as he was a bankrupt during the material time; and
- The First Defendant argued that a bankrupt is not prohibited per se from entering into agreements.

## **Issue:**

Whether the agreements were enforceable.



# DECISION:

The court illustrated that by entering into the agreements, there were elements of the bankrupt carrying on of a business and this was a violation under section section 38(1)(d) the Insolvency Act 1967. Therefore, the agreements were therefore unenforceable. The court held as follows:

“ (1) On the facts of this case, there was sufficient evidence to establish elements of an entering into, or carrying on of a business by the very terms of the relevant agreements. It was plain that the legislative intent of s 38(1)(d) of the Act was not to condone any act of the undischarged bankrupt in relation to the entry into or the carrying on of a business, or in relation to directly or indirectly taking part in the management of a company unless he had the prior permission of the DGI. A similar reasoning should apply in relation to the effects of the prohibition under s 38(1)(e) of the Act. Thus, although this court was not sitting as a bankruptcy court nevertheless it was held that since there had been a breach of s 38(1)(d) of the Act this court could not ignore the legal effects of illegality on the agreements (see paragraph 51).”



# Key Takeaways



- There is no legal provision stating that a bankrupt cannot enter into a contract.
- Nonetheless, a contract may be unenforceable should a bankrupt, by entering into a contract violates the Insolvency Act 1967.
- It is advisable to seek legal advice prior to entering into a contract with a bankrupt to ensure your rights are protected at all times.