AMENDMENT OF INSOLVENCY ACT 1967: IMPACT TO THE GUARANTORS

BY NOR ADILAH BINTI MOHAMAD PUZI, EZRILAW FIRM

In Malaysia, any matters pertaining to bankruptcy or insolvency are governed by the Insolvency Act 1967 (Amendment to Bankruptcy Act 2016-Act A1534), which came into force on the 6th November 2017 replacing the previous Bankruptcy Act 1967 (Act 360). Following the amendment of such Act, there are a few related rules accompanying the Act such as Insolvency Rules 2017, Insolvency (Voluntary Arrangement) Rules 2017, Insolvency (Fees) (Amendment) Rules 2017 and Insolvency (Cost) (Amendment) Rules 2017.These laws ensure fair and efficient distribution of debtors' assets to the creditors and able to assist the debtors to manage his assets and liabilities if he fails to manage his property well.[1]

Insolvency Act 1967 had made a significant reform towards a more debtor-friendly approach to bankruptcy by providing immunity for social guarantors and additional protection for other guarantors by virtue of Section 5(3) of the Insolvency Act 1967 where it provides:

> *A petitioning creditor shall not be entitled to commence any bankruptcy action - (a) against a social guarantor; and (b) against a guarantor other than a social guarantor unless the petitioning creditor has obtained leave from the court.*

The definition of social guarantor can be found in Section 2 of the same Act where it states *a person who provides, not for the purpose of making profit, the following guarantees:*

> *(a) a guarantee for a loan, scholarship or grant for educational or research purposes;*
> *(b) a guarantee for a hire-purchase transaction of a vehicle for personal or non-business use; and*
> *(c) a guarantee for a housing loan transaction solely for personal dwelling;*

Under the old law Bankruptcy Act, the creditor is required to demonstrate that he had exhausted all avenues of recovery against principal debtor before commencing any proceeding bankruptcy against a social guarantor. However, this new amendment provides a total prohibition of bankruptcy proceeding against social guarantor. This is taking into account that the kind of punishment is unfair against him since he did not benefit from the loan. Thus, the creditor will only be able to enforce the guarantee provided by social guarantor through limited modes of execution as stated in the Rules of Court 2012 and bankruptcy proceeding is no longer available as the option.

Whereas, regarding the other guarantors, the amendment had made it clear that in order to commence bankruptcy action against all other guarantors (other than social guarantor), prior

[1] https://www.thestar.com.my/news/nation/2017/03/30/fairer-system-for-guarantors-they-wont-be-declared-bankrupt-if-borrowers-fail-to-repay-debts/

leave of court is required by virtue of Section 5(3) of the said Act. In order to obtain such leave, Section 5(4) and Section 5(6) of the Act further elaborates that the creditors should satisfy the court that they had exhausted all modes of execution and enforcement to recover the debts including seizure and sale, judgment debtor summon, garnishment and bankruptcy or winding up proceedings against the principal debtor. However, these do not protect them from any other legal proceedings.

The Court of Appeal's decision in the case Hong Leong Bank Berhad v Ong Moon Huat [2018] MLJU 1576 has clarified two important issues under this new Insolvency Act 1967 on bankruptcy actions against guarantors which are (a) whether the word "debtor" in "to recover the debts owed to him by the debtor" in section 5(4) of the Act refers to the guarantor or the principal debtor; and (b) when or at what point should an application for leave under section 5(3)(b) of the Act be made? In allowing the appeal, the court stated that the word debtor refers to the principal debtor or the borrower according to purposive approach as adopted by the court of this section which is to protect the guarantor against bankruptcy proceedings and it is supported by the decision. It is further supported by the decision of the Federal Court in the case of Hong Leong Bank Bhd v Khairulnizam bin Jamaludin [2016] 4 MLJ 302. Whereas the second issue, the Court held that the application for leave may be made at any time before presentation of the creditor's petition since such leave is no longer required for the issuance of the bankruptcy notice.

These amendments are prospective in nature.[2] This means that the provisions are only applicable to debtors who are adjudicated bankrupt after the coming into operation of the Insolvency Act. However, all ongoing proceedings or those before the enforcement of this Act will still be continued.

Nevertheless, guarantors are still required and relevant in order to secure the debt. It is true that the creditor cannot bring bankruptcy proceeding against the guarantor without the prior leave of court. However, it must be considered that bankruptcy is only one of the few modes for the execution or enforcement that can be made against the judgement debt in order to recover the debt. We can see that these amendments might cause hardship in financing approval where the financial institution might be stricter and may request for other kind of securities. In any event all the modes of execution has been proved to be exhausted but the debt still cannot be recovered, then the court will give permission for a petition bankruptcy proceeding against the guarantor.

To conclude, these new amendments were made by the Government in order to reduce the number of bankruptcy cases in Malaysia as well as to provide an opportunity for a debtor to

[2] https://www.thestar.com.my/business/business-news/2019/04/04/govt-does-not-intend-to-amend-bankruptcy-act/#GA8RVSyS0oCQbiBO.99

rearrange his debts.[3] Somehow, these amendments would give some impacts to the creditor and guarantor especially with regards to the process to recover the debt after the principal guarantor failed to settle the debt.

[3] https://www.thestar.com.my/business/business-news/2019/04/04/govt-does-not-intend-to-amend-bankruptcy-act/