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Case Update: *Chin Chee Keong v Toling Corporation (M) Sdn Bhd* [2016] 6 CLJ 666 (CA)

This is a note on a recent Court of Appeal decision on s 304(1) of the Companies Act 1965 ("the Act") which provides for the lifting of the veil of incorporation in the specific circumstances of fraudulent trading and whether a claim under s 304(1) of the Act may be made in separate proceedings.

On 4 October 2006, Toling Corporation (M) Sdn Bhd ("Toling") brought an action against another company, Pacific Industries Sdn Bhd ("Pacific Industries") in the Penang High Court for the recovery of monies in respect of goods sold and delivered totalling RM588,093. Toling obtained judgment in default against Pacific Industries for the said sum.

Toling subsequently brought this action against the directors of Pacific Industries for a declaration that the directors be personally liable without any limitation of liability for the payment of RM588,093. The High Court found that Toling had established a case against the directors under s 304(1) of the Act and ordered the directors to pay the sum of RM588,093 which, in essence, was the judgment debt entered earlier against Pacific Industries. One of the directors, being dissatisfied, appealed.

The Court of Appeal held that in order for a claim to succeed under s 304(1) of the Act, a plaintiff must satisfy three conditions against the defendant:

- (a) there must be intent to defraud creditors;
- (b) the defendant was knowingly a party to the carrying on of the business in that manner, and
- (c) the plaintiff is eligible to make a claim under s 304(1) of the Act.

Once the conditions are fulfilled and the case is proved on a balance of probability, the court may make extensive orders including an order that the directors, in this case, be personally liable for all or any of the company's debts.

The Court of Appeal, in dismissing the appeal, found that the business of Pacific Industries had been carried on with intent to defraud creditors such as Toling. The director of Pacific Industries had, on behalf of Pacific Industries, placed orders with Toling despite knowing that it could not pay or that there was no reasonable prospect that Toling would be paid during the material period. Toling was also right to firstly initiate an action against Pacific Industries before commencing a separate action against its directors as the court must first make a finding against Pacific Industries before it can make the declaratory order and other consequential orders against its directors. Toling became a creditor of Pacific Industries by virtue of the court's findings in the suit against Pacific Industries.

In this case, it is important to note that, aside from satisfying the conditions of s 304(1) of the Act, Toling had firstly commenced an action against Pacific Industries before commencing a separate action against the directors of Pacific Industries where Toling gained creditor status and thereafter proceed to claim against the directors of Pacific Industries under s 304(1) of the Act. This suggests that unless the evidence of fraudulent trading emerged during the winding-up proceedings of a company, it is advisable to commence an action against the company to gain creditor status to apply for the relevant orders under s 304(1) of the Act.

The Court of Appeal decision may also be viewed here:

<http://www.kehakiman.gov.my/directory/judgment/file/P-02-411-03-2014L.pdf>

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