WRONGFUL TRADING UNDER THE INSOLVENCY, RESTRUCTURING AND DISSOLUTION ACT 2018

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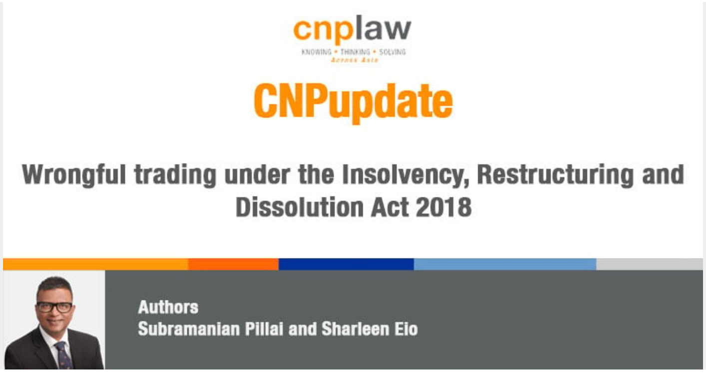

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The Insolvency, Restructuring and Dissolution Act 2018 (“**IRDA**”) consolidates Singapore’s personal and corporate insolvency, restructuring and dissolution laws into one omnibus legislation. Prior to this, the provisions pertaining to personal insolvency were contained in the Bankruptcy Act, while provisions related to corporate insolvency were contained in the Companies Act. The Bankruptcy Act and the relevant provisions in the Companies Act have since been repealed with the IRDA coming into force on 30 July 2020.

In this update, we discuss the new wrongful trading provisions which have been introduced in the IRDA.

What is wrongful trading

The IRDA introduces the concept of wrongful trading, which provides that a company trades wrongfully if:

1. the company, when insolvent, incurs debts or liabilities without reasonable prospect of meeting them in full; or
2. the company incurs debts or liabilities that it has no reasonable prospect of meeting in full and that result in the company becoming insolvent.

Persons who are party to the wrongful trading may attract both civil personal liability and criminal liability

Where a company has traded wrongfully, any person who was a party to the wrongful trading can be made personally responsible for all or part of the debts or liabilities of the company, if that person knew that the company was trading wrongfully or, as an officer of the company, ought to have known that the company was trading wrongfully.

An “officer”, in relation to a corporation, includes -

1. any director or secretary of the corporation or a person employed in an executive capacity by the corporation;
2. a receiver and manager of any part of the undertaking of the corporation appointed under a power contained in any instrument; and
3. any liquidator of a company appointed in a voluntary winding up,

but does not include -

4. any receiver who is not also a manager;
5. any receiver and manager appointed by the Court;

6. any liquidator appointed by the Court or by the creditors; or
7. a judicial manager appointed under Part 7 of the IRDA;

Such a person may also be guilty of a criminal offence and shall be liable on conviction to a fine not exceeding S$10,000 or to imprisonment for a term not exceeding 3 years, or both.
The IRDA includes a statutory defence for personal liability. In this regard, the Court may relieve the person of personal liability if the person acted honestly and having regard to all the circumstances of the case, the person ought fairly to be relieved from personal liability.

Several observations can be made in respect of these new provisions on wrongful trading

1. This represents a departure from the earlier insolvent trading framework prior to the IRDA. Under that framework, an officer of the company would only be personally liable to pay the whole or part of the debt incurred by the company, if there was a criminal conviction under the Companies Act. Consequently, the earlier insolvent trading provisions were seldom relied on to hold company officers accountable.
2. The wrongful trading provisions now dispense with the requirement for criminal liability before civil liability can be found. The upshot of this is that it may be easier to impose civil liability on those who are party to wrongful trading. Prior to the IRDA, it would have been necessary to satisfy the higher criminal standard of proof (of proving beyond reasonable doubt) before civil liability could be found, since criminal liability was a prerequisite.
3. Now, under the IRDA, the only applicable standard of proof would be the civil standard of proof (of proving on a balance of probabilities) since there is no longer a prerequisite for criminal liability.
4. These provisions herald a shift towards greater accountability, not just of directors and officers of the company. Significantly, liability can apply to any person who was a party to the wrongful trading, regardless of whether they are a director and/or officer of the company. What this means is that liability could therefore extend to other persons involved in managing a distressed company and entering into contracts on its behalf.
5. In situations where the company is insolvent or is approaching insolvency, those involved in the company's affairs (and not merely directors and officers of the company) should therefore be cautious about incurring debts and liabilities to ensure that they do not fall foul of the wrongful trading provisions.
6. It is interesting that the IRDA provides a statutory defence only to civil personal liability, and not to criminal liability. As mentioned above, the IRDA expressly includes a statutory defence to civil personal liability – the Court may relieve the responsible person from personal liability if the person acted honestly and having regard to all the circumstances, that person ought fairly to be relieved from personal liability. However, the IRDA appears to be silent on any defences for imposing criminal liability for the offence of wrongful trading.

7. It remains to be seen how the Courts will interpret and apply the defence of honesty, given that the party to the wrongful trading must have known or ought to have known of the wrongful trading in order for there to be personal liability.
8. Companies and their officers may wish to review and obtain advice on whether their directors' and officers' insurance policies afford insurance coverage if their directors and officers attract civil liability for wrongful trading. While insurance policies typically contain exclusions for fraud or dishonest conduct, there does not necessarily need to be a finding of dishonesty in order for there to be personal and criminal liability for wrongful trading. The wording of the insurance policies should therefore be scrutinised to assess whether wrongful trading claims would also fall within the exclusions.

In summary, it is important for persons involved in the affairs of a company to be especially vigilant where a company is insolvent or is approaching insolvency. Decisions on whether a company is solvent or approaching insolvency should be well documented in the event that the directors are subsequently required to justify their decisions and actions. Directors and officers should also ensure that they receive regular financial reports on the company so that they are apprised of its financial position and cash flow. If the company is approaching insolvency, directors should be wary of incurring debts and liabilities which might fall foul of the wrongful trading provisions.