NOTES

Insolvency Law
MRL301-M

1. INTRODUCTION TO INSOLVENCY LAW

1.1. Meaning of "insolvency"

Section 2 of the Insolvency Act, 24 of 1936 ("Act") – Definitions

'insolvent' when used as a noun, means a debtor whose estate is under sequestration and includes such a debtor before the sequestration of his estate, according to the context.

'insolvent estate' means an estate under sequestration.

Everyday language → A person is unable to pay his debts = merely evidence of insolvency

Legal test of insolvency → A debtor's liabilities, fairly estimated, exceed his assets, fairly valued.

A person is not treated as insolvent for legal purposes unless his *estate* has been sequestrated by an order of court, being a formal declaration that a debtor is insolvent granted either at request of:

- the debtor (voluntary sequestration); or
- one or more of the debtor's creditors (compulsory sequestration).

Ways to sequestrate an estate

Only after a sequestration order has been granted, the consequences of the Act will apply for example Sections 26, 29, 30 and 31 making provision for some dispositions[1] to be set aside. Although the dispositions have taken place before sequestration, the relevant sections of the Act may be invoked only after the court has sequestrated the debtor's estate.

1.2. Purpose of a sequestration order

The main objective of a sequestration order is to secure the orderly and equitable distribution of a debtor's assets where they are insufficient to meet the claims of all his creditors. Once an order of sequestration is granted, a ***concursus creditorum*** (coming together of creditors) is established and the interests of creditors as a group enjoy preference over the interests of the individual creditor. Creditors who have proved a claim have the right to share with other proved creditors in the proceeds of the estate assets replacing their right to recover claims by judicial proceedings.

Court won't grant a sequestration order if no advantage to creditors has been shown and generally not when there is only one creditor. If debtor's assets aren't enough to cover the costs of sequestration, there is no sense in sequestrating his estate as creditors won't get anything thus being a waste of time and money. The debtor is divested of his estate and can't burden it with more debts.

1.3. What may be sequestrated?

The Act provides for the sequestration of the 'estate' of a 'debtor'

An **Estate** is usually conceived as:

- an estate that includes assets and liabilities;
- an estate that consists of liabilities only;
- the joint estate of spouses married in community of property;
- the separate estates of spouses married out of community of property; and
- a new estate of a debtor whose estate has been sequestrated.

A **Debtor** may be:

- a natural person;
- a partnership;
- a deceased person and a person incapable of managing his own affairs;
- an external company that does not fall within the definition of external company, eg a foreign company that has not established a place of business in South Africa; and
- an entity or association of persons that is not a juristic person, eg a trust.

[1] Refer to paragraph 10 below

Section 2 of Act – Definitions

'debtor', in connection with the sequestration of the debtor's estate, means a person or a partnership or the estate of a person or partnership which is a debtor in the usual sense of the word, except a body corporate or a company or other association of persons which may be placed in liquidation under the law relating to Companies.

A body corporate established in terms of the Sectional Titles Act, 95 of 2986, is a body corporate as defined in the Companies Act, 61 of 1973 and, therefore, not a debtor for purposes of the Act.

1.4. **Jurisdiction of the court**

Which court has jurisdiction?

As a rule, only a Provincial or Local Division of the High Court ("HC") may adjudicate upon an insolvency matter, but a Magistrate's Court ("MC") may preside over prosecutions for criminal offences under the Act, setting aside of voidable dispositions and a few other matters if the jurisdictional limits are not exceeded.

Jurisdiction over a debtor and his estate

In terms of Section 149 of the Act, a court has jurisdiction over a debtor and his estate if:

- on the date of lodging, the debtor is domiciled or owns property, or is entitled to property, situated within the jurisdiction of the court; or
- at any time within the 12 months immediately preceding lodging, the debtor ordinarily resided or carried on business within the jurisdiction of the court.

A person is domiciled at a particular place if he is lawfully present there and has the intention to settle there for an indefinite period (Section 1(2) of the Domicile Act, 3 of 1992).

Jurisdiction in litigation against third parties

Section 149 of the Act: It is not relevant where the trustee of an estate litigates against third parties.

Competing courts – removal to another court

A court having jurisdiction over a debtor may refuse or postpone proceedings if it appears to the court equitable or convenient that the estate should be sequestrated by another court. The inquiry is not where the sequestration order may more conveniently be granted, but where the estate may more conveniently be administered.

1.5. **The Master**

A Master is appointed in terms of the Administration of Estates Act, 66 of 1965, to each of the areas of the Provincial Divisions of the HC and one of his most important functions is the custody of all documents relating to insolvent estates. For the performance of various functions the Master is entitled to charge fees, some being in cash, some by means of revenue stamps. The Master is a "creature of statute" and only has the powers granted to him by legislation.

1.6. **Condonation of irregularities**

In terms of Section 157(1) of the Act, irregularities in procedure can be condoned in the following instances:

- where the irregularity has not caused a substantial injustice; or
- where the irregularity has caused a substantial injustice, but the prejudice to creditors can be remedied by an order of court.

The courts have recognised the following additional grounds whereby an irregularity can be condoned:

- where a deviation is so slight as to fall within the maxim de minimis non curat lex (the law is not concerned with trifles);
- where all interested parties have waived compliance with the provisions of the Act;
- where the provision in question is not peremptory and has substantially been complied with; and
- where it was impossible to comply with the Act.

1.7. **Historical overview**

South Africa followed Roman Dutch law regarding insolvencies, but in 1843 a landmark ordinance was passed changing the law and more specifically abolishing the ***cessio bonorum*** (voluntary

surrender of goods by a debtor to his creditors). The Constitution provides a basis for the further reform of Insolvency Law as it poses a potential threat to a number of fundamental rights, but mere conflict does not render a provision constitutionally invalid. Constitutional invalidity involves a twofold inquiry:

- Does the provision conflict with a fundamental right?
- If so, is the limitation reasonable and justifiable in an open and democratic society based on human dignity, equality and freedom?

2. VOLUNTARY SURRENDER

2.1. Who may apply

The following persons may apply to surrender the estates mentioned:

Estate	Person
Estate of natural person	Debtor or his agent, expressly authorised to do so
Estate of deceased	Executor
Estate of debtor incapable of managing own affairs	Party entrusted with administering the estate, ie the *curator bonis*
Partnership estate	All members of partnership residing in South Africa, or their agent[2]
Joint estate of spouses married in community	Both spouses

2.2. Requirements

The court may accept the surrender of a debtor's estate only if it is satisfied that:

(1) The debtor's estate is, in fact, insolvent

A debtor is insolvent if the amount of his total liabilities exceeds the value of all of his assets. The test is whether it is established that the debtor is without funds to pay his debts in full and it is improbable that the assets will realise enough for this purpose.

(2) The debtor owns realisable property of sufficient value to defray all costs of sequestration which will be payable out of the free residue of his estate

The "costs of the sequestration" include not only the costs of surrender, but also all the general costs of administration in terms of Section 97 of the Act.

Section 2 of Act – Definitions

'free residue', in relation to an insolvent estate, means that portion of the estate which is not subject to any right of preference by reason of any special mortgage, legal hypothec, pledge or right of retention.

A logical result of the requirement that the debtor must own sufficient property to meet the costs of sequestration is that a debtor who has no assets and only liabilities cannot surrender his estate even against a guarantee being furnished to the Master for the costs of sequestration. Such an estate can, however, be compulsorily sequestrated.

(3) Sequestration will be to advantage of creditors

The debtor has to prove that sequestration will be to the advantage of the creditors whereas, in an application for compulsory sequestration, the creditor has to show merely that there is reason to believe that it will be. The onus is thus more strenuous in voluntary surrender.

2.3. Preliminary formalities

Court must be satisfied that certain formalities have been observed as set out in Section 4 of Act:

(1) Notice of intention to surrender

How	A debtor must publish a notice of surrender in the Government Gazette and in a newspaper circulating in the magisterial district where he resides or, if he is a trader, in the district where he has his principal place of business.
Why	Alerting the debtor's creditors of the intended application should they wish to oppose.
Format	Form A, First Schedule of the Act[3]

[2] Two exceptions: 1) special partnerships, which have been repealed and can be ignored; 2) partners *en commandite*, who are not liable to creditors for partnership debts or co-partners for any losses – they merely contribute

Contain	• Full names, address and occupation of debtor; • Date upon which, and the particular division of the HC before which the application for acceptance of the surrender will be made; and • When and where the debtor's statement of affairs will lie for inspection.
Time	Publication of the notice must take place not less than 14 and not more than 30 days before the stated date of hearing of the application.
Proof	Filing copies/cuttings of the Government Gazette and the newspaper with the relevant HC OR attach copies/cuttings from the Government Gazette and the newspaper to an affidavit and file them with court.

(2) Notice to creditors and other parties

Within 7 days after publication of the notice to surrender, the debtor must furnish copies of the notice to:

→ every one of his **creditors** whose address he knows or can ascertain;

→ to every registered **trade union** that, to his knowledge, represents his employees. In addition, notice to the **employees** themselves by –

- affixing a copy to notice board
- affixing a copy to the front gate of debtor's premises if employees have no access
- affixing a copy to the front door of the premises from which the debtor conducted business immediately prior to the surrender;

→ SARS.

(3) Preparation and lodging of statement of affairs

Preparation of statement

The statement of affairs referred to in the notice of surrender must be framed substantially in accordance with Form B, First Schedule of the Act and contain:

Form B	Balance sheet
Annexure I	List of immovable assets, estimated values, as well as any mortgages
Annexure II	List of any movable property not incl. in Annexures III or V and their value
Annexure III	List of debtors with their residential and postal addresses, details of each debt and an estimate extent (good, bad or doubtful)
Annexure IV	List of creditors, addresses, particulars of each claim and security held
Annexure V	List of any movable assets pledged, hypothecated, subject to a lien or under attachment in execution of a judgment
Annexure VI	List and description of every accounting book used by the debtor at the time of surrender or ceasing to carry on business
Annexure VII	Detailed statement of the causes of the debtor's insolvency
Annexure VIII	Personal information about debtor incl. prior insolvency and rehabilitation
Affidavit	Made by the debtor verifying the statement of affairs is true, complete and estimated amounts fairly and correctly estimated

When a partnership estate and a private estate of a partner are surrendered simultaneously, separate statements of affairs must be prepared and costs are part of sequestration costs.

Lodging of statement

The statement with supporting documents must be lodged in duplicate at Master's Office and lie for inspection by creditors at all times during office hours for 14 days. On expiry of

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NOTICE OF SURRENDER OF A DEBTOR'S ESTATE (SECTION 4(1))

Notice is hereby given that application will be made to the …… Division of the Supreme Court on …… the …… day of …… … 20… at …… o'clock in the forenoon or as soon thereafter as the matter can be heard, for the acceptance of the surrender of the estate of …… of …… and that a statement of his affairs will lie for inspection at the office of the Master of the Supreme Court at …… (and at the office of ……) for a period of fourteen days as from the ……day of …… 20...

XYZ
Attorney for ……

……
……20…

inspection period, a certificate is issued to the effect that it's duly lain for inspection and whether any objections were lodged, which is filed with Registrar before application is heard.

2.4. **Effect of notice of surrender**

(1) Stay of sales in execution

After publication of the notice, it is unlawful to sell any property in the estate which has been attached under a writ of execution or other similar process, unless the person charged with the sale could not have known of the publication. If the sale proceeded, the trustee of the estate cannot claim it if ownership thereof has been transferred unless he proves that the buyer acted in bad faith and with knowledge that the sale was unlawful.

The court or the Master may, however, order that such an asset should nevertheless be sold if, in his opinion, the value does not exceed R 5,000.00 and direct how the proceeds of the sale must be applied. The creditor must show that it would be more to the advantage of the general body of creditors to proceed with the sale. Publication of a notice of surrender has no effect on other civil and criminal proceedings and attachments in execution of judgments may be made, although sale in execution is stayed.

(2) *Curator bonis* may be appointed

Debtor is still at liberty to deal with his property as he chooses. As a safeguard against the debtor squandering his assets after publication, the Master may appoint a *curator bonis* to debtor's estate, who takes estate into his custody and assumes control of any business or undertaking of debtor. Estate remains vested with debtor and curator is only the caretaker.

(3) Potential compulsory sequestration

If after having published the notice of surrender:

- → the debtor fails to lodge a statement of his affairs; or
- → lodges a statement which is incorrect or incomplete in a material respect; or
- → fails to make application to court on the appointed day,

and the notice is not properly withdrawn, the debtor commits an act of insolvency which entitles a creditor to apply for the compulsory sequestration of his estate. Compulsory sequestration cannot be applied for if the notice of intention to surrender has lapsed.

(4) No withdrawal of notice without consent

A notice of surrender cannot be withdrawn without the written consent of the Master.

(5) Lapse of notice of surrender

The notice of surrender lapses if:

- → the court does not accept the surrender; or
- → if the notice is properly withdrawn; or
- → if the debtor fails to make the application for surrender within 14 days after the date advertised as the date of the hearing of the application.

2.5. **Application for surrender**

Form and contents of application

Application for surrender is brought by way of a notice of motion[4]. It is supported by a founding affidavit:

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IN THE HIGH COURT OF SOUTH AFRICA
(…… Division)

Case number: ……

In the matter of
……

Applicant

NOTICE OF MOTION

TAKE NOTICE that application will be made on behalf of the above applicant on the …… day of …… 20… at 10h00 or as soon thereafter as Counsel may be heard for an order in the following terms:
1. That the surrender of the estate of the applicant is accepted.
2. That alternative relief is granted to the applicant.
FURTHER TAKE NOTICE that the affidavit of ……, annexed hereto, will be used in support of the application.

Why	To persuade the court that the 4 requirements for voluntary surrender has been satisfied
Contain	• Full name, status, occupation and address of applicant to show jurisdiction and *locus standi* • An allegation of insolvency and facts to establish this • Explanation as to how the insolvency came about • An averment that applicant owns realisable property of sufficient value to defray all the costs of sequestration which will be payable out of the free residue of the estate • An allegation that it will be to the advantage of the creditors if the debtor's estate is sequestrated, amplified by facts supporting the allegation • Details of any salary or income that the debtor is receiving • Any other information that may influence the courting granting or refusing the surrender • A description of the procedural steps followed by applicant prior to bringing the application supported by documents proving that each step has been taken
Confirm	It must be sworn in and signed before a commissioner of oaths independent of the office in which it was drawn.

Filing of application at court

The application must be filed with the Registrar of the HC prior to the date advertised in the notice of surrender.

Copy of application to consulting party

If the debtor is an employer, he must provide a "consulting party" as contemplated in Section 189 of the Labour Relations Act, 66 of 1995, with a copy of the application. Section 189 deals with the dismissal of employees for reasons based on the employer's operational requirements and require the employer to consult one of the following:

- the person whom he is required to consult in terms of a collective agreement;
- if no collective agreement, the workplace forum and registered trade union of the employees likely to be affected by the proposed dismissals;
- if no workplace forum, the registered trade union whose members are likely to be affected by the proposed dismissals;
- if no trade union, the employees likely to be affected by the proposed dismissals or their representatives.

Master's report

In the Cape, a Master's report must be obtained and filed prior to the set-down of the application.

Opposition to application

A creditor may oppose the application even if his claim is less than the amount required to entitle him to apply for compulsory sequestration and even if his claim is disputed by the debtor.

Adjudication on the application

When adjudicated upon, the following documents must be before the court:

- The notice of motion and supporting affidavit(s);
- The debtor's statement of affairs, incorporating the verifying affidavit;
- Any sworn valuation necessary in the circumstances;
- Proof of publication of the notice of surrender;
- Proof by affidavit that the applicant has delivered/posted copies of the notice as required;
- A certificate from the Master that the statement of affairs has lain for inspection;
- Any report by the Master;
- Any opposing affidavits by creditors; and
- The debtor's replying affidavit.

KINDLY place the matter on the role for hearing accordingly.
DATED at …… this …… day of ……. 20…

XYZ
Applicant's Attorney
……

TO: THE REGISTRAR OF THE HIGH COURT, ……
AND TO: THE MASTER OF THE HIGH COURT, ……

2.6. **Court's discretion**

The court has the discretion to reject the surrender even if all the requirements have been met and influencing factors may be:

- Debtor displayed gross extravagance and run up debts on a pretentious scale;
- Debtor's creditors are not pressing him for payment and are willing to give him time or to accept payment in monthly instalments;
- Debtor's had an ulterior motive, eg to avoid paying or defeat rights of creditors;
- Debtor failed to give a full and frank account of his financial position;
- Debtor's papers were deficient in a number of respects.

2.7. **Costs of surrender**

Costs incurred in surrendering are included in the costs of sequestration and are payable out of the estate. Costs occasioned by unsuccessful opposition to the application must be borne by the creditor concerned, but court may order these costs (or part thereof) to be paid out of the estate.

2.8. **Setting aside sequestration order**

No appeal lies against the order refusing to accept the surrender, but anyone aggrieved by an order accepting it may appeal against such an order. Noting of an appeal does not suspend the operation or execution of the relevant order.

One of the consequences of a rehabilitation order in terms of Section 129(1)(b) of the Act is that the debtor is discharged from all debts, the cause of which arose before sequestration (except ones out of fraud on his part). Even if all debts have not been paid in full from the proceeds of the estate, the order enables the debtor to start building up a new estate without recourse by creditors who have not been paid in full. If the debtor is not rehabilitated, but the sequestration order is simply set aside, this consequence does not follow and the debtor then remains fully liable for all debts which existed before the granting of the sequestration order.

3. COMPULSORY SEQUESTRATION

3.1. **Requirements**

The court may grant an application for the sequestration of a debtor's estate if it is satisfied that:

(1) Applicant entitled to apply in terms of Section 9(1)

Section 9(1) allows proceedings to be instituted by:

→ a creditor (or his agent) with a liquidated claim for more than R 100.00; or

→ two or more creditors (or their agents) with liquidated claims of not less than R 200.00 in aggregate.

The fact that a creditor holds security for his claim doesn't exclude him from applying even if the value of the security exceeds the amount of the claim.

A liquidated claim is a monetary claim where the amount of the claim has been fixed or determined such as:

→ price of goods sold and delivered;

→ a claim based on a provisional sentence judgment;

→ a claim for return of price paid under a sale cancelled due to the seller's repudiation;

→ a delictual claim for the theft of a fixed and determinable sum of money

An unliquidated claim does not give *locus standi* to apply for example:

→ a claim for transfer of property;

→ a claim for damages for failure to carry out obligations in terms of a consent paper;

→ a claim for payment of an untaxed attorney and client bill of costs.

Liquidated does not mean an amount is already due and payable. Section 9(2) provides that a liquidated claim "which has accrued but isn't yet due" by the time application is heard must be regarded as liquidated for these purposes. After debtor's estate has been provisionally sequestrated, debtor himself cannot make a payment to sequestrating creditor to extinguish his claim or to reduce it below R 100.00. A third person, such as a surety, may make such payment on debtor's behalf after which provisional order must be discharged. Creditor can't

refuse payment in full, but may reject part payment. Where creditor's *locus standi* is eliminated, another creditor may intervene and apply for a further provisional order to be granted.

(2) Debtor has committed an act of insolvency or is insolvent

Acts of insolvency

A debtor's estate may be sequestrated even though he is technically solvent in terms of Section 9(1) by any creditor if he commits one of the following acts of insolvency:

i) Absence from the Republic or dwelling

Section 8(a): If he leaves the Republic or, being out of the Republic, remains absent from it, or departs from his dwelling or otherwise absents himself, with the intention to evade or delay payment of his debts. The creditor must establish the debtor's intention and such may be inferred from for eg an appointment made by the debtor to make a payment and then departing without keeping it.

ii) Failure to satisfy judgment

Section 8(b): 2 acts of insolvency are created where a court has given judgement against a debtor, namely:

- if he fails, upon the demand of the officer whose duty it is to execute the judgment, to satisfy it or to indicate disposable property sufficient to satisfy it; or
- if it appears from the return made by the officer, without presenting the writ to the debtor, that he has not found sufficient disposable property to satisfy the judgment.

"Disposable property" is any property which may be attached and sold in execution. If the debtor point out insufficient disposable property to satisfy the writ, the sheriff may refuse to attach it and make a *nulla bona* return, in which event the creditors may apply for sequestration.

iii) Disposition prejudicing creditors or preferring one creditor

Section 8(c): If he makes, or attempts to make, any disposition of any of his property which has the effect of prejudicing his creditors or preferring one creditor above another. Only the effect of the disposition need be considered and it does not matter if the debtor acted on purpose or recklessly as his intention is irrelevant. A debtor commits this act, for example, if he:

- refuses to meet one debt while paying another in full;
- sells an asset deliberately below its market value whilst failing to meet debts;
- passes a mortgage over immovable property to secure his debt to 1 creditor, while his business ventures are in financial difficulties and he's not paying creditors.

iv) Removal of property with intent to prejudice or prefer

Section 8(d): If a debtor removes, or attempts to remove, any of his property with the intent to prejudice his creditors or to prefer one above another. Differs from Section 8(c) insofar as a disposition of property is not required, mere removal is sufficient, and the intent of the debtor, not the effect, is important – Eg sending money or goods to a foreign country so that they aren't available for the settlement of the creditor's claims.

v) Offer of arrangement

Section 8(e): If he makes, or offers to make, any arrangement with any of his creditors for releasing him wholly or part of his debts, it qualifies as an act of insolvency if it is indicative of the debtor's inability to pay his debts.

vi) Failure to apply for surrender

Section 8(f): 3 acts of insolvency are created where a debtor has published a notice of surrender of his estate which hasn't lapsed or been withdrawn and 1 of following done:

- he fails to comply with the requirements of Section 4(3) - lodging a statement of affairs with the Master; or
- he lodges a statement which is incorrect or incomplete in any material respect; or
- he fails to apply for acceptance of the surrender on the specified date.

vii) Notice of inability to pay

Section 8(g): If he gives notice in writing to any one of his creditors that he is unable to pay any of his debts. One looks at the content of the notice to determine whether it is an act of insolvency and not the debtor's intention. Usually, the notice must be reasonable interpreted to have intended to give notice of inability to pay any single debt. Mere unwillingness to pay is not an act of insolvency.

viii) Inability to pay debts after notice of transfer of business

Section 8(h): If, being a trader, he gives notice in the Gazette in terms of Section 34(1) of his intention to transfer his business and is thereafter unable to pay all his debts.

Section 2 of Act – Definitions

'trader' means any person who carries on any trade, business, industry or undertaking in which property is sold, or is bought, exchanged or manufactured for purpose of sale or exchange, or in which building operations of whatever nature are performed, or an object whereof is public entertainment, or who carries on the business of an hotel keeper or boarding-house keeper, or who acts as a broker or agent of any person in the sale or purchase of any property or in the letting or hiring of immovable property; and any person shall be deemed to be a trader for the purpose of this Act (except for the purposes of subsection (10) of section twenty-one) unless it is proved that he is not a trader as hereinbefore defined: Provided that if any person carries on the trade, business, industry or undertaking of selling property which he produced (either personally or through any servant) by means of farming operations, the provisions of this Act relating to traders only shall not apply to him in connection with his said trade, business, industry or undertaking; **≠Farmer**

As soon as the notice is published, every liquidated liability of the trader in connection with his business which would have become due at some future date, falls due if the creditor demands payment. It follows that the act of insolvency is still committed if the trader cannot pay a debt which bears no relation to his business.

Debtor in fact insolvent

Instead of relying on an act of insolvency by the debtor, the sequestration creditor can rely on the fact that the debtor's estate is insolvent and that his liabilities exceed his assets. If the creditor relies on an act of insolvency and can't establish that it's been committed, but it's clear that the debtor is insolvent, court may grant a final sequestration order on latter ground.

Factual insolvency may be established:

Directly → by evidence of the debtor's liabilities and the market value of assets; or

Indirectly → by evidence of facts and circumstances from which the conclusion of insolvency is fairly and properly derivable.

(3) Reasons to believe sequestration will be to the advantage of creditors

Before the court can grant a final order of sequestration, it must be satisfied that there is reason to believe that it will be to the advantage of the creditors. Creditors means all or the general body of creditors.

Question: Will a substantial portion of creditors get an advantage from the sequestration?

If, after the costs of sequestration have been met, there is no payment to creditors, or only a minimal payment, there is no advantage. The court must compare the position of the creditor if there is no sequestration with the position if there is sequestration and it will only be to the advantage of the creditors if it will result in a greater dividend than would otherwise be the case. The onus of establishing an advantage remains on the sequestrating creditor even if the debtor committed an act of insolvency.

The *onus* of satisfying the court of these 3 matters rests on the sequestrating creditors, no *onus* on debtor to disprove any element.

Friendly sequestration

A debtor can arrange with a friend to whom he owes a debt and whom he is unable to pay, that he will commit an act of insolvency by, for example, write saying he cannot meet the debt so that his friend can apply for compulsory sequestration. An application for compulsory sequestration

brought by a creditor who is not at arms length is referred to as 'friendly' sequestration and the legal position is as follows:

- Creditor's co-operation/motivation to assist debtor doesn't preclude granting of sequestration.
- Court must be mindful of proceedings not at arm's length – potential collusion and malpractice.
- Example of abuse: **Mthimkhulu v Rampersad –** Debtor seeks attorney, writes a letter to his "creditor" who brings application and debtor disappears just before service of court order, which result in return date being extended numerously until genuine creditors have lost interest.
- May be brought with sole purpose of getting a stay of civil proceedings / of a sale in execution. Debtor can use it to free himself from his debts: Where granted and free residue doesn't cover costs of sequestration any creditor who has proved a claim is obliged to contribute. They're made to believe that there is a risk that they will be called to contribute should they prove their claim, thus they refrain. Where no claims proved within 6 months after the sequestration, the debtor can apply for rehabilitation and be released from his debts.
- Courts must scrutinize friendly sequestrations to ensure the requirements of the Act aren't undermined and the interests of the creditors aren't prejudiced. Court should require the following from the sequestrating creditor:
  - Full details of claim;
  - Documentary evidence establishing that he has actually performed as alleged;
  - Full details of debtor's realisable assets, including convincing evidence of likely realisation;
  - If another creditor has already attached debtor's property in execution, proof that prior notice of the application has been given to that creditor; and
  - If he requires an extension of the return date of the rule *nisi*, an affidavit setting out proper reasons for the extension.

3.2. Application for sequestration

(1) Form and content of application

Application is brought by way of a notice of motion[5]. It is supported by a founding affidavit:

Why	To set out sufficient facts to establish the requirements for a sequestration order
Contain	• Full name, status, occupation and address of sequestrating creditor. His *locus standi* should reflect and in case of an agent, his authorisation • Full names, date of birth, identity number and marital status of the debtor and, if married in community of property, that of his/her spouse – Section 17(4)(b) of the Matrimonial Property Act: application to sequestrate joint estate must be made against both spouses • Amount, cause and nature of claim - if secured, the nature and value of the security • The act(s) of insolvency committed by debtor and/or his *de facto* insolvency • An averment that sequestration will be to the advantage of creditors explaining why • Any other relevant facts which might influence Court's discretion

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IN THE HIGH COURT OF SOUTH AFRICA
(…… Division)

Case number: ……

In the matter of
……. Applicant
and
……. Respondent

NOTICE OF MOTION

TAKE NOTICE that application will be made on behalf of the above applicant on the …… day of …… 20… at 10h00 or as soon thereafter as Counsel may be heard for an order in the following terms:

1. That this application be regarded urgent and that usual rules as to notice and service in terms of Rule 6(12) are dispensed with.
2. That the estate of the Respondent is provisionally sequestrated.
3. That a rule *nisi* is issued calling on the Respondent and any other interested parties to show cause to this Court on the …… day of …… 20… at 10h00 why the Respondent should not be finally sequestrated.

FURTHER TAKE NOTICE that the affidavit of ……., annexed hereto, will be used in support of the application.
KINDLY place the matter on the role for hearing accordingly.
DATED at ……. this …… day of …… 20…

XYZ
Applicant's Attorney
……

TO: THE REGISTRAR OF THE HIGH COURT, ……
THE MASTER OF THE HIGH COURT, ……
THE RESPONDENT, ……

	• Statement that security will be furnished to Master and his certificate obtained as required by Section 9(3) • Statement that copy of papers will be lodged with Master to obtain report i.t.o. Section 9(4) • A statement confirming that copies of the application will be furnished to interested parties
Confirm	It must be sworn in and signed before a commissioner of oaths independent of the office in which it was drawn.

(2) Steps prior to adjudication on application

i) Security for costs

Applicant bound to prosecute at own costs until a trustee or a provisional trustee has been appointed and is required to deposit security for payment of all fees with Master.

ii) Search of Master's records

In Western Cape HC (formerly CPD), applicant's attorney must file an affidavit stating that he searched Master's records and it doesn't appear that debtor's estate already under sequestration.

iii) Filling of application[6] at court with the Registrar

iv) Master's report

Master makes a written report to the court of any facts which would justify the court in postponing the hearing or dismissing the application.

v) Copy of papers to debtor and other interested parties

Applicant also required furnishing copy to:

- Every registered trade union that represents any of debtor's employees;
- Debtor's employees themselves; and
- SARS.

(3) Provisional sequestration

Creditor must approach the court twice:

i) To obtain a provisional order of sequestration

At this stage there must be ***prima facie*** (at first sight) satisfaction of the requirements and the following must be before court:

- Notice of motion
- Master's certificate that security has been given
- Affidavit of search through records by applicant's attorney
- Master's report
- Applicant's affidavit responding to Master's report (if any)
- Affidavit setting out manner in which others were informed

After considering these, the court may make an order:

- Sequestrating provisionally – simultaneous **rule *nisi*** (order calling upon debtor to show cause, on day mentioned, why his estate should not be finally sequestrated)
- Dismissing application
- Postponing hearing

ii) To have the provisional order confirmed and made final

At this stage the requirements are proved on a balance of probabilities.

(4) Service of rule nisi

Rule *nisi* must be served on debtor, with application papers if not already served therewith. If debtor is absent for 21 days from usual place of residence and business, court may direct it to be attached to the door of the courthouse and published in the Gazette. Also copies to:

→ Any registered trade union that represents the debtor's employees;

→ The employees themselves; and

[6] Notice of motion, founding affidavit and supporting documents

→ SARS.

(5) Opposition of application

After granting of the rule *nisi*, debtor and other interested parties may oppose application by filing affidavits with Registrar setting out grounds of opposition and serving applicant in sufficient time to enable him to reply before the return day.

(6) Anticipation of return date

On application of debtor, court may anticipate return day of rule *nisi* for purpose of discharging provisional order, provided 24 hours' notice of application has been given to applicant. Court must be satisfied that all creditors received notice and none has valid objection.

(7) Intervention by another creditor

Fullard v Fullard: Creditor entitled to intervene to have provisional order set aside or to obtain a fresh sequestration order. If latter, first order must be set aside and a new order must be issued. Intervening creditor must imply case for sequestration, furnish security as if original applicant without restating facts appearing from records in existing proceedings.

(8) Final sequestration

On return day, court must have in addition to provisional stage:

→ Sheriff's return of service of rule *nisi*;

→ Any opposing affidavits of the debtor and/or other interested parties;

→ Replying affidavit of applicant; and

→ Any affidavit by the provisional trustee

Court may confirm provisional order if it's satisfied applicant has established requirements on a balance of probabilities. If not satisfied, it must either dismiss application and set aside the provisional order or require creditor to produce further proof of allegations in his application and postpone the hearing for a reasonable period.

3.3. **Court's discretion**

Even if the court is satisfied that the requirements have all been established on a balance of probabilities, it's not bound to grant the final order of sequestration.

3.4. **Costs of proceedings**

Trustee must, from first available funds from estate, reimburse sequestrating creditor for his taxed costs in sequestrating the estate. Costs of opposition not part of sequestration costs.

3.5. **Unwarranted or vexatious proceedings**

As safeguard court may, when satisfied that application is abuse of court's procedures or is malicious or vexatious, allow debtor to prove damage suffered and award compensation it deemed fit.

3.6. **Setting aside sequestration order**

Any person aggrieved by a final order of compulsory sequestration, or by an order setting aside an order of provisional sequestration may appeal against the order. The aggrieved person must first obtain leave to appeal from the appropriate court. No appeal lies against the granting of a provisional sequestrating order or the refusal of such an order.

4. THE LEGAL POSITION OF THE INSOLVENT

Sequestration of a debtor's estate imposes on him a form of reduction in status, which limits his capacity to contract, earn a living, litigate and hold office.

4.1. **Contracting**

The debtor retains a general competency to make binding agreements, but certain restrictions are imposed to protect creditors.

(1) Prohibited contracts

The debtor may not make a contract which:

→ purports to dispose of any property of his insolvent estate; or

→ adversely affects (or is likely to) his estate or any contribution (moneys earned by the insolvent due to trustee only once the Master indicated that it is not necessary for the

support of the insolvent or his dependants) which he is obliged to make towards his estate, without written consent of the trustee.

Mervis Brothers v Hannekom: M sued H, an insolvent, for the amount of a debt incurred before sequestration based on an undertaking given by H after sequestration without the trustee's consent. MC held that undertaking likely to affect any contribution which H would be obliged to make, if called upon to do so, and therefore not binding. On appeal the court found that at time of contracting, H was not obliged to make a contribution as Master hadn't assessed a contribution so consent was not necessary and the undertaking binding.

(2) Effect of contract which is not prohibited

Where trustees' consent is not necessary or has been given, the contract is valid and binding between the parties. However, according to **De Polo v Dreyer**, insolvent may not enforce performance in his favour unless the Act specifically gives him the right to do so. If the Act is silent, the trustee is the proper person to enforce the claim.

(3) Effect of prohibited contract

Contract is voidable at option of the trustee or remains binding on the parties. Same rules apply regarding performance for a contract which is not prohibited. Section 24(1) provides protection to third parties who contract with debtor, ignorant of his insolvency. If an insolvent purports to alienate, for valuable consideration and without consent, property he acquired after sequestration, to a person who proves he was not aware, and had no reason to suspect that his estate was under sequestration, the alienation is nevertheless valid. This Section:

→ applies only to new assets which came into insolvent's possession after sequestration. **Wessels v De Klerk**: Insolvent sold immovable property that formed part of insolvent estate and received two promissory notes in part payment. He endorsed these to a bona fide purchaser. Court held sale was not validated and therefore voidable;

→ places the *onus* on third party to prove his unawareness.

4.2. **Earning a livelihood**

Insolvent is allowed to follow any profession or occupation or enter into any employment and he may make whatever contracts which are reasonably necessary for this purpose. But insolvent may not, without written consent of the trustee, carry on, be employed in any capacity or have any direct or indirect interest in, the business of a trader who is a general dealer or a manufacturer – farmer not a trader for purposes of Act. **S v Van der Merwe**: General dealer is someone who trades at a fixed and recognised place in all sorts of wares, not just in 1 kind or a few particular kinds – eg milk depot (**Ex parte Du Plessis**) or a restaurant (**R v Papangelis**). If trustee gives or refuses to consent, any of the creditors or insolvent may appeal to Master.

4.3. **Instituting and defending legal proceedings**

Proceedings which may be brought/defended personally by insolvent

An insolvent may sue or be sued in the matters relating to:

- status, eg divorce;
- a right which does not affect the insolvent estate, eg to receive maintanence from the insolvent;
- recovery of remuneration or reward for work done;
- a pension to which he is entitled for services rendered;
- compensation in respect of loss or damage suffered by reason of defamation or personal injury;
- a delict committed by him after sequestration of his estate.

When there is an irregularity or the *bona fides* of the trustee or the creditors is under suspicion, the insolvent may interfere with the administration of his insolvent estate.

Security for costs

An insolvent who enters into legal proceedings may be obliged to give security for costs of action

	MC	HC	Factors in HC
Case flows from the Act	Plaintiff compelled if defendant claims security	Cannot claim security	May claim if action will probably not succeed
Case doesn't flow from the Act	Plaintiff completed if defendant requires security	Plaintiff not compelled to lodge security	May claim security if action is reckless or vexatious

Entitlement for costs

When insolvent obtains an award of costs in his favour in a matter in which he is entitled to litigate, the judgment for costs belongs to him personally and may dispose of it as he likes - **Schoeman v Thompson**. Damages for maladministration on the part of trustee accrue to insolvent estate, but an award of costs against trustee is for the benefit of the insolvent - **Ecker v Dean**.

4.4. Holding Office

An unrehabilitated insolvent is disqualified from being a trustee of an insolvent estate and, if he's one when his estate is sequestrated, he must vacate office. He is not capable of being a member of the National Assembly, National Council of Provinces or the Provincial Legislature. The insolvent can't, except with permission of court, be a director of a company or take part in the management of a close corporation.

5. VESTING OF THE ASSETS OF THE INSOLVENT

5.1. Vesting of estate in trustee

The function of trustee is to collect assets in estate, realise them and distribute proceeds amongst creditors in the order of prefrence laid down by the Act. Estate will remain vested in trustee until:

- the discharge of the sequestration order by the court;
- the acceptance by creditors of an offer of composition (an offer to creditors of an amount in final payment of insolvent's debts which will discharge the sequestration) made by insolvent which provides that insolvent's property will be restored to him; or
- an order for the insolvent's rehabilitation is granted in terms of Section 124(3) on the following grounds:
  - no claims have been proved against the estate;
  - insolvent has not been convicted of any offence with regard to his insolvency; and
  - insolvent's estate has not been sequestrated before.

If a trustee vacates his office, is removed from office or dies, the estate revests in the Master until a new trustee is appointed or in the co-trustee, if there is one.

5.2. Property which falls into estate

The insolvent estate comprises of:

- all property of insolvent at date of sequestration, inculding property (or proceeds) in the hands of a sheriff under a writ of attachment;
- all property which insolvent acquires or which accrues to him during sequestration, including any property he recovers for the benefit of estate where trustee fails to take necessary action.

Property may be movable or immovable property wherever situated in South Africa and includes contingent interests in property, excluding contingent interests of a **fideicommissary** (a person who receives a gift of property, usually by will, to be held on behalf of another who cannot receive the gift directly) heir or legatee.

Whenever insolvent has acquired property which is claimed by the trustee, it's deemed to belong to the insolvent estate until the contrary is proved. However, if a person who became a creditor of the insolvent after sequestration alleges that an asset does not belong to the estate and claims a right to the asset it is deemed to not belong to the estate until the contrary is proved.

Du Plessis v Pienaar: Sequestration of a joint estate makes both spouses 'insolvent' for purposes of the Act resulting in the property of both of them vesting in trustee and being available to meet claims of creditors. Property inherited by a spouse to a marriage in community of property forms part of insolvent estate, even if the will contains a provision excluding property from any community of property – **Badenhorst v Bekker**. Property inherited by an insolvent during his insolvency falls into his insolvent estate, notwithstanding a contrary provision in the will - **Vorster v Steyn**.

The reasoning and decision in **Badenhorst v Bekker** was approved by the Supreme Court of Appeal ("SCA") in **Du Plessis v Pienaar** and it was held that a debtor, not the estate of the debtor, incurs the debt. So where spouses are married in community of property their creditors may recover debts from both of them: not only from each spouse's undivided interest in the joint estate, but also from his or her separate estate outside the joint estate. Once the joint estate is sequestrated both spouses are insolvent and property owned by each of them (including separate property) becomes available to the creditors.

The effect of these decisions must now be considered in the light of the decision in **Wessels NO v De Jager**: Insolvent has a competence or power to accept the bequest or nomination and he acquires no right to property or benefit until he has accepted. Repudiating the right to property or benefit will result in it not vesting in his estate and will ensure that it passes to someone other than the trustee and the creditors of his insolvent estate.

5.3. **Property which does not fall into estate**

- Wearing apparel, bedding, household furniture, tools and other means of subsistance as the creditors may determine;
- Remuneration for work done less the portion the Master is of the opinion is not necessary for the support of the insolvent and his dependants due to the trustee;
- Any pension to which he may be entitled for services rendered by him;
- Compensation for any loss or damage by reason of defamation or personal injury;
- Compensation for occupational injuries or diseases (loss/damage due to personal injury);
- Benefits payable to a miner;
- Unemployment insurance benefits (UIF);
- Insurance policies
  - Policies covering liability to third parties

    If insolvent insured against liability to third persons prior to sequestration and incur liability covered by the policy, his rights against the insurer pass, upon sequestration, directly to the third party and not the insolvent estate. In terms of Section 156 of the Act, the third party can claim directly against the liability insurer and does not have to rely on a concurrent claim against the insolvent estate. The third party is also exposed to all the same defences which, in the absence of Section 156, the insurer could have raised against the contracting party (the insolvent).

    It may be illustrated with the decision in **Canadian Superior Oil v Concord Insurance** where insolvent incurred liability towards the Plaintiff, who wished to claim the damages directly from the insurer in terms of Section 156. The insurance contract between insolvent and the insurer stated that the insurer would be liable to compensate the insured only for moneys already paid by the insured (the insolvent) and, because the insolvent (as a result of the intervening insolvency) had not made any payments towards his liability, the insurer was therefore also not obliged to make any payments to the insolvent. The same defence could therefore be raised against the third party (the Plaintiff).
  - Life policies

    Section 63(1) of the Long Term Insurance Act, 52 of 1998, excludes certain insurance benefits from the insolvent estate, namely:

    → policy benefits provided (or to be) to insolvent under an assistance, life, disability or health policy, which has been in force for at least 3 years and in which insolvent or spouse is the life insured; and

    → any assets which insolvent acquired exclusively with such policy benefits within a period of 5 years from the date on which they were provided.

    The policy benefits or assets are excluded to an aggregate of R 50,000.00, eg if insolvent is named the beneficiary of policies totaling R 80,000.00, he is entitled to R 50,000.00 and remaining R 30,000.00 vests in his insolvent estate.

    Section 63(1) has no application if the policy benefits in question are payable to a third party and not the insolvent as the rights to the benefit vests in the third party and will not become part of the insolvent estate – **Pieterse v Shrosbree**. A life policy taken out by insolvent in favour of a third person is an asset in insolvent estate to the extent that the trustee is vested with any right that insolvent had to surrender the policy prior to his death and obtain payment of the surrender value.
- Share in accrual;
- Trust property or funds
  - Assets in a trust will not usually form part of the personal estate of the trust trustee if that trustee's personal estate is sequestrated. Assets in a trust are therefore protected assets.
- Right of labour tenant to land or right in land;
- Property acquired with money from above sources.

5.4. Disposal of estate property by insolvent

An insolvent cannot dispose of any property and if he unlawfully disposes of immovable property, the trustee may recover compensation from:

- the insolvent personally;
- the person who acquired the property knowing that its part of the insolvent estate; or
- a person who did not know, but who acquired it without giving sufficient value in return.

Exceptions to the rule that insolvent may not deal with property falling within the insolvent estate:

- Section 25(3): If insolvent brings about any act of registration (mortgage or transfer) in respect of immovable property in his estate after expiry of every ***caveat*** (entered on the deeds of the immovable property of the insolvent estate to prevent an insolvent from transferring the property or registering any right over it) entered against that property by the Registrar of Deeds, the act of registration is valid.
- Section 24(1): If an insolvent purports to alienate, for valuable consideration and without consent, property he acquired after sequestration, to a person who proves he was not aware, and had no reason to suspect that his estate was under sequestration, the alienation is nevertheless valid.

5.5. Acquisition of new estate during insolvency

The insolvent may, during the course of his insolvency, acquire a new estate and hold it with a title adverse to the trustee, due to the fact that various property does not vest in the trustee. This property can in turn be sequestrated.

6. VESTING OF THE ASSETS OF THE SOLVENT SPOUSE → Out of community of property

Marriage in community of property

As there is only 1 joint estate, if one of the spouses is declared insolvent, the other automatically becomes insolvent and both spouses are under sequestration → Section 21 doesn't apply

Marriage out of community of property

Each spouse continues to have a separate estate consisting of assets and liabilities and there is no joint estate of the spouses → Section 21 applies

6.1. Vesting of assets in trustee

Section 21(1): Additional effect of a sequestration order (including provisional order) is to vest the separate property of the spouse of the insolvent in the Master and subsequently the trustee, as if it were property of the insolvent estate, and to empower the Master or trustee to deal with the property accordingly. Transfer is not intended to be permanent since the solvent spouse may secure the release of assets falling within categories set out in Section 21(1), but until the release the solvent spouse has none of the ordinary powers of ownership.

Section 21 was introduced to prevent, or at least hamper, collusion between spouses to the detriment of creditors of the insolvent estate by making it difficult for insolvent and spouse to deprive the estate of assets to which it is entitled by pretending that they are the separate property of the solvent spouse.

In **Harksen v Lane** it was contended that Section 21 is invalid for violating the solvent spouse's constitutional rights. The majority of the Constitutional Court ("CC") rejected this argument as:

- It doesn't expropriate solvent spouse's property since it doesn't contemplate permanent transfer to the Master and trustee;
- It differentiates between the solvent spouse and other persons, but this differentiation does not infringe the right to equality and is legitimate as it has a rational connection; and
- It does not amount to unfair discrimination.

Meaning of 'solvent spouse'

Married out of community of property (otherwise both insolvent and Section 21 doesn't apply.

Section 21(13) of the Act defines "spouse" as not only a wife or husband in the legal sense, but also a wife or husband by virtue of a marriage according to any law or custom, and also a woman living with a man as his wife or a man living with a woman as her husband, although they are not married to one another.

Since the commencement of the Civil Union Act (“CUA”), the definition of the term "spouse" in the Act has by implication been amended to include persons of the same sex or of the opposite sex who have entered into a civil union. The CUA was introduced in order to accord same-sex couples the same family law rights and obligations, and the same status, benefits and responsibilities accorded to opposite-sex couples and Section 1 thereof defines "civil union" as the voluntary union of two persons who are both 18 or older, which is solemnised and registered by way of either a marriage or a civil partnership, according to the procedures described in the CUA, to the exclusion, while it lasts, of all others. Furthermore, a "civil union partner" means a spouse in a marriage or a partner in a civil partnership, as the case may be, concluded in terms of the CUA and the CUA applies to civil union partners joined in a civil union.

A consequence of a civil union is that the legal consequences of a marriage in terms of the Marriage Act, 25 of 1961, apply, with relevant contextual changes, to a civil union. Furthermore, a reference to marriage in any other law, including common law, includes a civil union. In addition, a husband, wife or spouse in any law includes a civil union partner

Accordingly, for the purposes of Section 21(13) of the Act, this alteration to the law would mean that a civil union partner falls within the definition of the word "spouse" and that Section 21 of the Act will now apply with equal force to such partners in a civil union.

Duty of solvent spouse to lodge statement of affairs

Sheriff must serve a copy of the order on solvent spouse if she has a separate estate that has not been sequestrated and she must, within 7 days of service, lodge with the Master a statement of her affairs in the correct form and verified by an affidavit.

Postponement of vesting

Section 21(10): If the solvent spouse is carrying on the business of a trader apart from the insolvent spouse, or if it appears to the court that the solvent spouse is likely to suffer serious prejudice through the immediate vesting of her property, the court may exclude her property or part of it from the operation of the order.

The sort of contingencies against which the insolvent state must be protected are alienation or fraudulent abandonment of the assets by the solvent spouse, malicious or accidental damage to the property by the solvent spouse or a third person, and theft of assets by a third person.

6.2. **Release of solvent spouse’s property by trustee**

The trustee is obliged to release property of the solvent spouse which is proved to fall in any of the following categories:

- Property owned before the marriage to the insolvent
- Property acquired under a marriage settlement
- Property acquired by valid title during the marriage
  - This would include property bought by the solvent spouse from her own earnings or the proceeds of her personal property and donations received by her from friends and family.
- Property protected under certain other provisions
  - Section 21(2)(d) provides for the release of property protected by various other provisions, but this section has become obsolete.
- Property acquired with proceeds of the above

Clear distinction between the release of property in terms of Section 21(2) of the Act and the setting aside of an impeachable disposition: Property acquired in terms of a marriage settlement must be released in terms of Section 21(2)(b). Dispositions in terms of an antenuptial contract will usually be dispositions without value under Section 26 of the Act. Although trustee must initially release the property to the solvent spouse under Section 21(2) of the Act, the trustee will still be able to set aside such a disposition as a disposition without value if the requirements of Section 26 are proved and the solvent spouse cannot prove the requirements of Section 27 of the Act.

Section 21 of the Act used to be especially important in the case of donations made by the insolvent spouse to the solvent spouse. At common law, donations between spouses (except donations in terms of an antenuptial contract) were void. The solvent spouse could therefore not obtain the release of such a donation, because the donated asset had not been acquired by a valid title as against the creditors of the insolvent spouse. Now, however, donations between spouses are valid. The release of the donated item may therefore be obtained, subject to the possibility of

the trustee's challenging the donation and having it set aside as a disposition without value in terms of Section 26 of the Act.

7. UNCOMPLETED CONTRACTS AND LEGAL PROCEEDINGS NOT YET FINALISED

7.1. Contract completed by insolvent but not by other party

If insolvent has carried out his side and only the other party's performance is outstanding, that right to performance is an asset in the insolvent estate and vests in the trustee. The trustee may either sell it or enforce performance and then sell the subject-matter of the performance.

7.2. Contract not completed by insolvent

Continuance of contract

General rule - Sequestration does not suspend or put an end to the contract.

The trustee's election

Trustee may elect to perform in terms of the contract or not and the only power he has is to exclude the right of the other party to invoke the remedy of specific performance[7]. Once trustee has elected to repudiate or continue the contract, he cannot change his mind. If he fails to reach a decision within a reasonable time, it is assumed that he does not intend to perform in terms of the contract.

Repudiation is a breach of contract in that the repudiating party indicates by words or conduct that he does not intend to perform his obligations under the contract. Repudiation gives the other party to the contract (aggrieved party) the right to claim the appropriate remedies for breach of contract.

Statutory controls on the exercise of the trustee's election

Regarding certain contracts, the Act lays down when and how trustee should exercise his election:

(1) Contract to acquire immovable property **Section 35 → Immovable**

Section 35: Where insolvent contracted to acquire immovable property and property has't been transferred[8] to him, trustee must make his election within 6 weeks after receiving written notice from the other party calling upon him to do so. If he fails, the other party may apply to court for cancellation[9] of contract thus providing for a procedure that the seller must follow in order to prevent the immovable property from falling into the insolvent estate. The other party may also prove a concurrent claim for loss suffered due to non-fulfilment[10].

If immovable property has, however, been transferred to the estate of the insolvent by being registered in the name of the acquirer in the Deeds Office and the acquirer is then declared insolvent before making his performance under the contract, the situation is not dealt with under this section and the seller is in an weak position at common law. He no longer owns the immovable property and merely has a personal right under the law of contract to claim the insolvent debtor's performance. As the remedy of specific performance won't be granted in favour of this creditor against trustee of the insolvent estate, his claim against the insolvent estate will be an ordinary, concurrent claim for damages for breach of contract and he will, therefore, rank for a dividend.

(2) Hire of property

Trustee may only repudiate the lease by giving written notice to the lessor. If he doesn't notify the lessor of his desire to continue the lease on behalf of the lessee's estate within 3

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[7] The Plaintiff seeking this remedy requests the court to order the contracting party who is in breach of contract to carry out his obligations under the contract; in other words, to do what he promised. Usually, the court would exercise its discretion to grant or to refuse the order of specific performance, but where sequestration has occurred before the insolvent has performed his contractual obligations, the court would refuse to grant specific performance in favour of the creditor who requests the order of specific performance. If the court were to grant specific performance in favour of this particular creditor, this creditor would thus be granted an unfair advantage over the other creditors in the *concursus creditorum*. This particular creditor awarded the order of specific performance would be entitled to receive full performance from the trustee under the terms of the original contract, whereas the other creditors in the *concursus creditorum* would have to be content with less than full performance.

[8] Until transfer by the registration of the relevant title deed in the appropriate Deeds Office, the seller is still the registered owner of the immovable property and, accordingly, the property is part of the estate of the seller, not the purchaser. If the purchaser's estate is sequestrated, the immovable property does not automatically fall into the insolvent estate.

[9] Cancellation puts an end to the contract and when it's cancelled the parties are usually also obliged to return what they can of each other's performances to each other. Duty of restitution may, however, be excluded by a forfeiture clause (see Consequences later), which prevents the party who is in breach of contract from claiming the restitution of his or her own performance.

[10] The purpose is to put the aggrieved party, so far as this aim can be achieved by an award of money, in the position that he would have been if the contract had been performed. Damages claimed will be a non-preferent claim against the insolvent estate.

months of his appointment, he is deemed to have repudiated it. Repudiation deprives the insolvent estate of any right to compensation for improvements, other than those made in terms of any agreement with the lessor. The lessor has:

→ a preferent claim for rent payable from date of sequestration to date of determination of lease (included in cost of administration);

→ if the property is immovable, a secured claim by reason of his tacit hypothec, for rent owed at time of sequestration; and

→ a concurrent claim in respect of any other loss sustained because of the non-performance of the lease.

Consequences of repudiating contract

If trustee elects to repudiate the contract, the opposite party is precluded from obtaining an order for specific performance even if he has performed his obligation in full. If he decides to accept the repudiation and cancel the contract, he may use other remedies for breach of contract:

- he may recover any property handed over in performance and still owned by him;
- he is obliged to make restitution in accordance with normal principles of law of contract unless there is a forfeiture clause in the contract; and
- he has a concurrent claim in respect of property which he has transferred, and payments which he has made, to the debtor, and for loss which he suffered because of the breach.

Consequences of abiding by contract **Section 36 → Movable**

If trustee elects to complete the contract, he 'steps into the shoes' of insolvent. He may insist on receiving performance owed by other party and he is bound to carry out the counter-performance owed by insolvent.

Bryant & Flanagan: When trustee upholds the contract, he must uphold the contract in full. He can't uphold in part and repudiate in part. He and the other party must then perform the contract in full. Exception is if the contract is divisible, where the contract may be upheld and repudiated in part.

Section 36 regulates the position in a cash sale[11] of movable property where the buyer's estate is sequestrated before he has paid the full purchase price, but after the property has been delivered to the buyer. **≠ apply to instalment sale agreements**

This section recognises that the seller of movable property under a cash sale remains the owner thereof until the purchase price is paid. It, nevertheless, places some limitations on that principle by limiting the right of the other party to exercise an accrued right of cancellation where the sale is a cash sale of movable property. Seller of movable property for cash, who has delivered property, but who has not been paid, cannot reclaim it from trustee of buyer's insolvent estate unless:

- he has given notice in writing to the buyer or his trustee within 10 days after delivery (not sequestration) that he reclaims the property; and
- if the trustee disputes his right to reclaim the property, he institutes legal proceedings within 14 days after receiving notice of the trustee's objection.

Contracts which are suspended or terminated on sequestration

(1) Employment contract **Section 38 → Contract of service**

The sequestration of an employer's estate suspends the employment contract between him and his employee with immediate effect. During the period of the suspension:

→ the employee isn't obliged to render services and isn't entitled to his salary or wage;

[11] A contract of sale is a cash sale if the purchase price is to be paid on delivery of the property and is the case when it was expressly agreed that the purchase price were to be paid on delivery or when there was no agreement as to time of payment. In a credit sale, on the other hand, parties expressly agree that property will be delivered, but that payment will only be made on an agreed later date. Difference between a cash sale and a credit sale relates to passing of ownership: Cash sale → ownership passes to buyer only when property has been delivered to him and he has paid full purchase price; Credit sale → ownership passes already when property is delivered to buyer, unless parties expressly agree that ownership will pass only at a later stage. If buyer has to pay purchase price against delivery, but seller still allows buyer to take possession of the property without simultaneously paying the purchase price, contract remains a cash sale, eg cheque dishonoured. Ownership of the movable property sold passes only when the purchase price is paid and as the seller remains the owner till then, he should be able to recover the possession of that property from the buyer.

→ no employment benefits accrues to the employee, although he may receive unemployment benefits from the date of suspension.

Subsequently, the contract of employment may be terminated by:

→ the decision of the trustee provided he has engaged in consultation aimed at reaching consensus on appropriate measures to rescue the whole or part of the insolvent employer's business; or

→ the expiry of the period of 45 days after the appointment of the trustee if no measures have been adopted which result in the continuation or end of the contract.

On termination of contract, the ex-employee is entitled to recover any resultant loss he has suffered plus severance benefits in accordance with Basic Conditions of Employment Act, 75 of 1997. He will have a preferent claim against the insolvent estate, but if he is entitled to an amount of arrear remuneration which exceeds the limits of preference, he must prove an ordinary concurrent claim for that remuneration. A concurrent claim may be proved for loss which he has sustained because of the premature termination of his employment contract.

Sequestration of an employee's estate doesn't terminate his contract of employment unless he is precluded from holding his position or office while insolvent by statutory provision.

(2) Mandate

In **Goodricke & Son v Auto Protection Insurance** it was held that a contract of mandate[12] ***ipso iure*** (by operation of law) comes to an end on the insolvency of the mandatory, thus not being suspended but terminated, and the Roman-Dutch authority found in **Voet** confirms this proposition. However, this proposition probably needs to be qualified:

→ A mandate to perform a juristic act (eg conclude a contract) shouldn't terminate since any juristic act performed by a mandatary is deemed to have been concluded between mandatory and other person, and mandatary isn't party to resultant legal relationship.

→ If mandate doesn't call for any special skill or expertise and could be satisfactorily executed by the trustee, there seems to be no cogent reason to denying the trustee the option of enforcing the contract – **Natal Law Society v Stokes**.

Contracts which trustee cannot repudiate

(1) Lease of immovable property

Due to the principle of *"huur gaat voor koop"*[13], trustee cannot repudiate a lease of immovable property concluded by the insolvent as a lessor. However, trustee may be compelled to repudiate lease if property is subject to a real right (eg mortgage bond) which was registered prior to lease. Trustee is then required to put property up for sale subject to lease. If highest bid isn't sufficient to cover amount due to holder of the real right, trustee must, at the request of the holder, sell the property free of the lease. The lessee then has a concurrent claim for damages in respect of loss suffered because of the breach of contract.

(2) Sale of land on instalments

The trustee's right to repudiate may be excluded where the insolvent has:

→ sold land on instalments; or

→ alienated land which has subsequently been sold on instalments; and

→ the land has not been transferred pursuant to the transaction(s) in question.

This is a sale of land[14] on instalments in which the purchase price is payable in 2 or more instalments over a period exceeding 1 year. To provide for the case where land is disposed of under successive transactions without being transferred, Chapter II of Alienation of Land Act, 68 of 1981 ("ALA"), uses the concepts of an 'intermediary'[15] and a 'remote purchaser'[16]. The main effect of Chapter II is:

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[12] An agreement to perform some task or render a professional service to another, ie between attorney and client

[13] According to that rule, a lessee of immovable property establishes a real right to the subject of the lease

[14] Used, or intended to be used, mainly for residential purposes and exclude agricultural land

[15] A person who sells land to a remote purchaser or a person who has alienated land which, after alienation, is sold by another person to a remote purchaser and which, at time of sale, has still to be transferred to the first-mentioned person.

[16] A person who purchases land in terms of a contract from another person who is not the owner of the land

- → Where insolvent sold land, buyer may compel trustee to pass transfer in his favour, provided he arranges to pay all transfer costs plus whichever is the larger of:
  - o the total amount outstanding under the deed of alienation; or
  - o the sum: administration costs; any endowment, betterment or enhancement levy; and the amount required to discharge the mortgage bond.
- → Where insolvent has alienated land to an intermediary, the intermediary is in the same position as the buyer under contract and can compel transfer in his favour.
- → Where insolvent alienated land and it was subsequently alienated to an intermediary or remote purchaser, the latter are entitled to transfer if:
  - o they fulfil or undertake to fulfil the obligations in terms of their own deed of alienation; and
  - o the obligations of every intermediary between owner and themselves are fulfilled.
- → If transfer is not claimed by any persons entitled to it and trustee abandons agreement made by the insolvent and realises the land for creditors, the purchaser of the land under a contract which has been recorded against the title deed of the land has a preferent claim in respect of the proceeds of the realisation.

The ALA aims at making sure that every party who has right to transfer is aware of his right and can exercise it. A remote purchaser is required to notify owner of the land immediately of the conclusion of the contract, of his address and of contract itself. Owner must pass these details on to trustee. Trustee is under a duty to notify every person who he has reason to believe purchased the land in terms of a contract, or is an intermediary, of his right to take transfer thereof. If land is sold on instalments, but does not fall within ALA, common law is applicable. Trustee becomes owner of property and must decide whether to perform or not, having regard to the best interests of creditors.

(3) Sale of goods in terms of instalment agreement

Where seller of goods under an instalment agreement is declared insolvent before full price has been paid and ownership has passed to buyer, trustee isn't entitled to repudiate and vindicate the goods, provided that buyer continues to fulfill his obligations in terms of the contract. There is no clear case authority for this view.

(4) Resale of immovable property not yet acquired

The trustee's right to repudiate is excluded where he obtains transfer of immovable property which the insolvent bought and resold (without receiving transfer) prior to the sequestration. On receiving transfer, he is bound to pass transfer of the property to the purchaser against payment of the price, if not already paid. Thus he is not entitled to, having upheld the first contract, to repudiate the second.

Purchase of goods in terms of instalment agreement **Section 84 → Purchaser insolvent**

Special rules apply where insolvent has purchased goods in terms of an agreement failing within paragraphs (a), (b) and (c)(i) set our below:

Section 1 of the National Credit Act ("NCA"), 34 of 2005 – Definitions

"instalment agreement" means a sale of movable property in terms of which –

(a) all or part of the price is deferred and is to be paid by periodic payments;

(b) possession and use of the property is transferred to the consumer;

(c) ownership of the property either-

  (i) passes to the consumer only when the agreement is fully complied with; or

  (ii) passes to the consumer immediately subject to a right of the credit provider to re-possess the property if the consumer fails to satisfy all of the consumer's financial obligations under the agreement; and

(d) interest, fees or other charges are payable to the credit provider in respect of the agreement, or the amount that has been deferred;

Section 84(1) of the Act provides that, on sequestration of buyer's estate, the seller automatically acquires a hypothec over the ***res vendita*** (the thing sold), whereby the balance outstanding under the agreement is secured. No one may have a hypothec over his own property, thus owner-ship in the *res vendita* passes from the seller to the insolvent estate.

The effect of sequestration of buyer's estate is that the seller loses his right of ownership in the property and simultaneously becomes a creditor with a hypothec over the property. Trustee must, if required by seller, deliver the *res vendita* to the seller who holds it as security for his claim and has the right to realise his security as prescribed by the Act. The type of agreement envisaged is a sale of movable property in terms of which:

- all or part of the price is deferred and is to be paid by periodic payments;
- possession and use of property is transferred to the buyer;
- ownership of property passes to buyer only when the agreement is fully complied with.

A transaction meeting these requirements will be governed by Section 84(1), even if it falls outside the ambit of the NCA. Section 84(1) presupposes that an agreement is still in force and that the seller is the owner of the *res vendita*. It will, however, not apply in cases of physical impossibility and the possessor's ability to assert a right which defeats the trustee's right – **Venter NO v Avfin**.

In terms of Section 82(2), if debtor returns property to seller within 1 month before sequestration, the trustee may demand that seller to deliver to him the property or its value at the date of return, subject to payment to creditor by trustee or to deduction by creditor from value of property of difference between total amount payable and total amount actually paid. The legislature clearly intended to enable trustee to reclaim the property for the benefit of concurrent creditors.

Difference:

- Section 84(1): Hypothec created by statute arises automatically by operation of law, no choice.
- Section 84(2): Trustee may elect to demand return of the property

Transaction on exchange

In terms of Section 35A, these special rules apply in regard to a transaction to which the rules of an 'exchange'[17] apply and in which the insolvent was a 'market participant'[18]:

- The exchange or any other market participant may, in respect of the obligations owed to it, terminate transaction in accordance with the rules of the exchange, and trustee is bound by it;
- Any resultant claim is limited to amount due upon termination under the rules of the exchange;
- Trustee is bound by the rules and practices of the exchange if the transaction is to be settled on a date after sequestration or settlement is overdue on that date.

Agreement on informal market

Section 35B makes special provision where insolvent was party to a 'master agreement'[19]. All unperformed obligations arising out of agreement terminate automatically on sequestration. The market values of obligations as at date of sequestration must be netted and this amount is payable.

8. MEETINGS OF CREDITORS AND PROOF OF CLAIMS

8.1. Meetings of creditors

By means of a system of meetings, the insolvent's creditors establish their claims, elect the trustee and give directions to the trustee on the winding up of the estate.

(1) First meeting

When	Immediately on receipt of final sequestration order
Convene by	The Master
Notice	In Gazette not less than 10 days prior to meeting
Purpose	To enable creditors to prove claims and elect a trustee

(2) Second meeting

When	After first meeting and appointment of the trustee on a date fixed by Master

[17] An 'exchange' means an exchange as defined in Section 1, and licensed under Section 10, of the Securities Services Act, 36 of 2004, and includes a central securities depository as defined in Section 1 of that Act and which is also licensed as a clearing house under Section 66 of that Act, or a clearing house as defined in Section 1 of that Act;

[18] A 'market participant means an authorised user, a participant, a client or a settling party as defined in Section 1 of the Securities Services Act, 36 of 2004, or any other party to a transaction.

[19] A 'master agreement' includes, *inter alia*, an agreement in accordance with standard terms published by the International Swaps and Derivatives Association, the International Securities Lenders Association, the Bond Market Association or the International Securities Market Association

Convene by	The trustee
Notice	In Gazette and 1 or more newspapers circulating in the district in which the insolvent resides or has principal place of business in Afrikaans and English
Purpose	To enable creditors to prove claims, receive trustee's report on affairs and condition of estate and to give trustee directions on administration of estate

(3) Special meeting

Proof of claim	
When	After second meeting when trustee is called upon by any interested party tendering payment of expenses to be incurred in connection with meeting
Convene by	The trustee
Notice	In Gazette
Purpose	To enable creditors to prove claims
Interrogation of the insolvent	
When	At any time, provided Master gives consent, trustee may and must if so required by creditor who has proved claim against estate
Convene by	The trustee
Notice	In Gazette
Purpose	Interrogating the insolvent

(4) General meeting

When	At any time or when required to do so by Master or creditors representing ¼ of the value of all claims proved
Convene by	The trustee
Notice	In Gazette and 1 or more newspapers circulating in the district in which the insolvent resides or has principal place of business in Afrikaans and English and must state matters to be dealt with
Purpose	Giving trustee instructions concerning administration of estate, also for considering offer of composition

(5) General provisions relating to meetings

i) Date and venue of meetings

Master determines first, trustee the rest. Every meeting must be held at a place which is accessible to the public, such as the Master's office.

ii) Presiding officer at meetings

In a district where there is a Master's Office, the Master (or officer in public service designated by him) must preside over the meeting. In another district, meeting must be held in accordance with directions by the Master, by the magistrate of the district (or officer in public service designated by him).

iii) Record of proceedings

The presiding officer must keep a record of the proceedings at every meeting, certify it at conclusion and transmit it to the Master. The minutes constitute *prima facie* proof.

iv) Statement privileged

The publication of any statement at a meeting is privileged to same extent as the publication of a statement made in a court of law.

9. THE ELECTION OF THE TRUSTEE

9.1. Election and appointment

Election

At the first meeting, the creditors who have proved their claims may elect 1 or 2 trustees. If more than 1 person is nominated, the person who obtains a majority of votes in both number and value must be elected sole trustee. If 1 person obtains a majority in value and another person majority in number, both must be elected sole trustee. Where the trustee is eleced at a meeting not presided over by the Master, the election is not valid until confirmed by the Master.

Appointment

The Master may refuse to accept the person the creditors elected as trustee. If he accepts, once the person has given satisfactory security for the proper performance of his duties as trustee, the Master must confirm the election and appointment by delivering a certificate of appointment. The trustee must then give notice of his appointment and his address in the Gazette.

Refusal to appoint

The Master may refuse to confirm the election of a person elected as trustee if:

- he was not properly elected;
- he is disqualified from being a trustee;
- he has failed to give the required security; or if,
- in the opinion of the Master, he should not be appointed as a trustee to the estate in question[20].

If the creditors have elected a trustee unlawfully, the Master is obliged not to confirm the election and to convene a new meeting to elect another trustee. If the Master declines to confirm, he must notify the party in writing and state the reasons for declining.

Objection to appointment or refusal to appoint

Any person aggrieved by:

- the appointment of a trustee; or
- refusal to confirm the election of, or to appoint, a trustee;

may, within 7 days from the date of appointment or refusal, request the Master, in writing, to submit his reasons for the appointment or refusal to the Minister. The Master must comply with the request within 7 days, submitting along with his reasons any relevant documents, information or objections which he has received. The Minister may then give appropriate directions in this regard and his decision is final.

Joint trustees

If more than 1 trustee has been appointed or the Master has appointed a co-trustee, the trustees must act jointly and are jointly and severally liable for every ac they perform jointly. If one acts unlawfully without the knowledge or consent of the other, the latter is not liable. Disagreements must be referred to the Minister for his directions.

9.2. **Persons disqualified from being trustee**

Certain persons are not competent to be appointed trustee in any estate, while others are merely disqualified from being the trustee of a particular estate.

Absolute disqualification

The following persons may not be a trustee in any estate:

- an insolvent;
- a minor or other person under legal disability;
- a person who reside residing outside South Africa;
- a company, close corporation or other corporate body;
- a former trustee disqualified under Section 72;
- a person declared by the court under Section 59 to be incapacitated for election while it lasts, or any person removed by the court from an office of trust on account of misconduct;
- a person who has been convicted of theft, fraud, forgery, uttering, or perjury and who has been sentenced to a term of imprisonment without option of a fine, or to a fine exceeding R 2,000.00;
- a person who was at any time party to an agreement with a debtor or creditor whereby he undertook that he would, while acting as a trustee, grant or obtain for a debtor or creditor a benefit not provided for by law.
- a person who has, by misrepresentation, rewarded, or the direct or indirect offer of reward, induced or attempted to induce, a person to vote for him as a trustee or to assist him in becoming elected.

[20] The Master exercised a subjective discretion in deciding suitability and he should consider the person's personality, experience, age and diligence, as well as the complexity or otherwise of the problems presented by the estate.

Relative disqualification

The following persons are disqualified in respect of a particular estate:

- a person related to the insolvent in blood or by marriage within the 3rd degree;
- a person having an interest opposed to the general interest of the creditors;
- a person who acted as a bookkeeper, accountant or auditor of the insolvent at any time during a period of 12 months immediately preceding the date of sequestration;
- an agent authorised to vote on behalf of a creditor at a meeting and who acts or purports to act in terms of that authority.

9.3. **Vacation or, or removal from, office**

Vacation of office

A trustee must vacate his office if:

- his estate is sequestrated;
- an order is issued for his detention under the Mental Health Act, or if he is declared by the court to be incapable of managing his own affairs;
- he is convicted of an offence and senteced to imprisonment without the option of a fine; or
- he is convicted of theft, fraud, forgery, uttering a forged document, or perjury.

Removal from office by Master

The Master may remove a trustee from office on the grounds that:

- he was not qualified for appointment, or that his election or appointment was illegal, or that he has become disqualified;
- he has failed to perform his duties satisfactorily or to comply with a lawful demand of Master;
- he is mentally or physicaly incapabe of performing his duties as trustee satisfactorily;
- the majority of the creditors has requested in writing that he be removed; or
- he is no longer suitable, in the opinion of the Master.

Disqualification or removal from office by court

On application of an interested party, court may declare that the person appointed or propossed as trustee is:

- disqualified from holding the office; and
- incapable of being elected or appointed trustee during his lifetime or such other period as the court may determine.

The court may make this order if the person:

- has accepted, or expressed his willingness to accept, a benefit from someone who performs work on behalf of the estate; or
- in order to obtain the vote of any creditor for his appointment as trustee, has:
  - wrongfully omitted or included the name of a creditor from any record required by the Act;
  - given or offered consideration of any kind;
  - offered to abstain from investigating previous transactions of the insolvent; or
  - split claims for the purpose of increasing the number of votes.

The effect of **Fey NO and Whiteford NO v Serfontein** is that there are two ways in which to remove a trustee from office on the grounds of misconduct, namely:

- The Master may remove the trustee from office in terms of Section 60(e) of the Act; or
- The court may remove the trustee from office in terms of the common law. The Act itself does not grant the court the authority to remove a trustee on the grounds of misconduct.

10. IMPEACHABLE DISPOSITIONS[21]

10.1. Meaning of 'disposition'

Section 2 of Act – Definitions

'disposition' means any transfer or abandonment of rights to property and includes a sale, lease, mortgage, pledge, delivery, payment, release, compromise, donation or any contract therefor, but does not include a disposition in compliance with an order of the court.

Term	Explanation
Property	Movable or immovable property wherever situated within SA, including contingent interests in property other than those of a fidei commissary heir or legatee and property situated outside SA.
Sale	A contract by which one party agrees to transfer or deliver a thing to another party in return for the payment of a sum of money.
Lease	A contract by which one party provides the use of a thing to another party in return for the payment of a sum of money.
Mortgage	Mortgagor provides security to mortgagee (bank) for performance of mortgagor's obligations under loan by passing a mortgage bond over his immovable property. This bond is registered against property in Deeds Office and if mortgagor doesn't perform his obligations as promised under the loan agreement, mortgagee may have it sold and recover amount of outstanding debt from proceeds of property.
Pledge	As security for the repayment of a loan, a person may agree to provide the lender with movable property as pledge and if the loan is not repaid, the lender can recover the outstanding amount owed from the proceeds of the pledged item.
Delivery	The transfer of possession of a movable item.
Payment	Payment may take various forms and is often used in the sense of paying a debt.
Release	Parties agree that a pre-existing duty is discharged before it's performed in full.
Compromise	Parties to the agreement of compromise settle a dispute or an uncertain issue.
Donation	A non-obligated party agrees to give another party something for free.

The following should be noted:

- A beneficiary has competence or power to accept or repudiate inheritance (bequest or legacy) or an insurance benefit and it is not part of the estate until he accepts. Thus, repudiating the inheritance or insurance benefit, is not a transfer or abandonment of any right;
- A "disposition" includes a contract providing for the alienation or abandonment of rights to property, which is sometimes referred to as an "uncompleted disposition", and also suretyship;
- If the creditor obtained a court order by fraud or by collusion with the insolvent and with the intention of prejudicing other creditors, the exclusion does not apply as for other court orders.

10.2. Dispositions which may be set aside

The dispositions which may be set aside are those:

Voidable
- made not for value;
- having the effect of preferring one creditor above another ("voidable preferences");
- intended to prefer one creditor above another ("undue preferences");
- made in collusion with another person and having the effect of prejudicing creditors or preferring one above another; and

- made in ***fraudem creditorum*** (in fraud of creditors) → **may be set aside in terms of common law**

Until a disposition is set aside by the court, it remains valid and binding and only disposition made by the insolvent are impeachable under the Act.

Dispositions made not for value

(1) What must be proved **Section 26 → Disposition without value**

Section 26(1) allows the court to set aside a disposition made for no value. The *onus* is on the trustee to prove:

[21] Juristic acts which the insolvent executed prior to the sequestration of his estate, and which had the effect of adversely disturbing the contemplated equitable treatment of the creditors, or which had the effect of unfairly prejudicing the general body of creditors. The Act and the common law of insolvency empower the trustee to set aside these juristic acts in order to restore the balance.

→ that the insolvent made the disposition;

→ when the insolvent made the disposition; and

→ that he received no value for it.

It's not necessary to prove that the insolvent intended to prejudice the creditors, the object of Section 26 is simply to prevent a person in insolvent circumstances from impoverishing his estate by giving away assets without receiving any appreciable advantage in return. Section 26(1) will apply if the disposition was made:

→ more than 2 years before sequestration, court can only set it aside if trustee proves that, immediately after it was made, the liabilities of the insolvent exceeded his assets;

→ within 2 years of sequestration, the court must set it aside unless the person claiming under or benefited by it can prove that, immediately after it was made, the assets of the insolvent exceeded his liabilities.

For a disposition to have "value", the mutual benefit need not be monetary or tangible, but it must be adequate (not a trifling amount) - eg being allowed to remain a member of Tattersall (**Estate Wege v Strauss**) or payment of a lawful debt where the payer receives counter-value in the discharge of his liability (**Estate Jager v Whittaker**). To establish "value", due consideration is given to all the circumstances in which the transaction was made.

If it's proved that the liabilities at any time after making a gratuitous disposition, exceeded assets by less than the value of property disposed of, the disposition may be set aside only to that extent – eg gift of R 5,000.00 causes insolvent's liabilities to exceed his assets by R 10,000.00, he then acquired assets which reduced his margin of insolvency to R3,000.00 – disposition may only be set aside to the extent of R 3,000.00.

(2) Exception to Section 26 – disposition in terms of ANC

Section 27 → ANC

Section 27 provides that the settlement of property under an antenuptial contract by a husband to his wife or any child to be born of the marriage is not liable to be set aside as a disposition without value on the insolvent's insolvency if these requirements are met:

→ The disposition must be an "immediate benefit"[22];

→ The disposition must have been given in good faith[23];

→ The antenuptial contract must have been duly registered at least 2 years prior to the sequestration.

(3) Beneficiary's rights to share in estate limited

Section 26 → Disposition without value

In terms of Section 26(2), the beneficiary to a disposition which has been set aside by the court has no right to claim in competition with creditors of the insolvent estate. Same applies if it hasn't been set aside, but hasn't been completed by the insolvent.

One exception: Where uncompleted disposition was made by way of suretyship, guarantee or indemnity → In this event the promisee may compete with the creditors of the estate for an amount not exceeding the amount by which the value of the insolvent's assets exceeded his liabilities immediately before the disposition was made.

Suretyship and similar contracts are usually regarded as dispositions without value (**Lange-berg Koöperasie v Inverdoorn**), thus Section 26(2) used to create problems, especially for banks. As a result this section was amended at their insistence and its provisions are now qualified as far as they pertain to dispositions without value "by means of suretyship, guarantee or indemnity". Therefore, a careful creditor who ensured that the surety's assets sufficiently exceeded his/her liabilities at the time of granting the suretyship will still have a provable claim against estate of insolvent surety if principal debtor doesn't pay. It's merely a wise practical precaution for that creditor to take. If he/she does ascertain that the surety's assets will sufficiently exceed his/her liabilities when the suretyship is granted, the creditor can be confident of being able to rely on Section 26(2) should the surety subsequently be declared insolvent, and thus the creditor can be confident of being allowed to compete with the other creditors of the insolvent surety's estate in respect of the amount not exceeding the

[22] "Immediate benefit" means a benefit given by a transfer, delivery, payment, cession, pledge, or special mortgage of property completed before the expiration of a period of three months as from the date of the marriage.

[23] "Good faith" in this context refers to the absence of any intention to prejudice creditors in obtaining payment of their claims or to prefer one creditor above another.

amount by which the value of the insolvent's assets exceeded his liabilities immediately before the making of the disposition.

Dispositions which prefers one creditor above another: voidable preference

(1) What must be proved

Section 29 → Voidable preferences

Section 29(1) allows the court to set aside a disposition meeting the following requirements and the *onus* is on the trustee to prove them:

- → that the insolvent made the disposition;
- → not more than 6 months before the sequestration of his estate or his death; and
- → if the disposition had the effect of preferring one of the insolvent's creditors above another and immediately after the disposition was made, the liabilities of the insolvent exceeded the value of his assets.

The policy behind this section is to prevent a person on brink of insolvency to select one or a few of his creditors for full payment and to disregard the rest. Disposition doesn't have to be made directly to the creditor concerned - it must merely have had the effect of preferring him.

Test whether a creditor was preferred: Were the proper distribution of assets as envisaged in the Act defeated or has the creditor benefited more or was he paid earlier than would have been the case if he had been paid in accordance with the Act?

(2) Exception to Section 29 – disposition in course of business and not intended to prefer

Section 29 enables the trustee to set aside transactions made and assets alienated by the insolvent while being close to insolvency, unless it was made in the ordinary course of business and it was not intended to prefer one creditor over another. The beneficiary must prove both of the following elements in order to defeat the trustee's claim:

i) Ordinary course of business

An objective test is applied in deciding whether a disposition was made in the ordinary course of business: Was disposition 1 which would normally be entered into between solvent business persons (**Hendriks NO v Swanepoel**); or is it in conformity with ordinary business methods adopted by solvent persons of business (**Van Zyl & others NNO v Turner**)?

ii) No intention to prefer

Insolvent won't be held to have intended to prefer if it is established that, when he made disposition, he didn't contemplate or expect sequestration; or his main purpose in making the disposition was something other than conferring of an advantage on the creditor concerned[24]; or to comply with a contractual obligation to give possession of his movable property to creditor concerned to perfect latter's security under a general notarial covering bond – **Cooper & another NNO v Merchant Trade Finance**. It has been held in **Swanepoel NO v National Bank of SA** that proof that the insolvent entertained the hope of tiding over his financial difficulties is not sufficient to prove the intention to prefer.

Disposition intended to prefer one creditor: undue preference

(1) What must be proved

Section 30 → Undue preference to creditors

Section 30 allows the court to set aside a disposition meeting the following requirements and the *onus* is on the trustee to prove them:

- → that the insolvent made the disposition;
- → at any time before sequestration;
- → with the intention of preferring one of his creditors above another; and
- → when he made the disposition, his liabilities exceeded his assets.

If proved, judgment must be given in the trustee's favour as there are no defences available to beneficiaries of such dispositions.

[24] Eg to shield himself from criminal prosecution or to cover up a misappropriation of assets and save himself from exposure – **Pretorius' Trustee v Van Blommenstein**.

A subjective test is applied in deciding whether the insolvent had the intention to prefer: Was his dominant, operative or effectual intention in making the disposition to disturb the proper distribution of assets on insolvency? It stands to reason that the insolvent must have applied his mind and if he didn't actually consider whether he was conferring a preference, he could not have intention to prefer. Court must weigh up all relevant facts and decide on a balance of probabilities.

The following factors are relevant in determining whether the insolvent's dominant intention was to confer preference:

→ Whether the insolvent contemplated insolvency when making the disposition;

→ Whether the insolvent was, at time of disposition, in a position to exercise free choice;

→ Whether there is any relationship between the insolvent and the creditor.

(2) Differences between trustee's powers under Sections 29 and 30

	Section 29 Voidable preference	Section 30 Undue preference
Time	Within 6 months before sequestration of the estate or insolvent's death	At any time before sequestration of the estate
Solvency	Debtor may be solvent when he makes it, provided he is insolvent immediately after	Debtor must be insolvent
Onus	Trustee to prove that disposition had the *effect* of preferring 1 creditor above others	Trustee to prove that the debtor *intended* to prefer 1 creditor above the others
Defences	1 defence with 2 elements	No defendances

Collusive disposition which prejudices creditors or prefers one creditor

Section 31

Section 31 provides that the court may set aside a transaction entered into by the debtor before sequestration in terms of which he, in collusion with another, disposed of his property in a manner which had the effect of prejudicing his creditors or preferring one above another. To succeed, the trustee must prove that:

- the insolvent made a disposition of his property;
- disposition was made "in collusion with another person" - both knew that one was insolvent and expected disposition to have effect of prejudicing creditors or preferring one above another; and
- the disposition had the effect of prejudicing creditors or preferring one above another.

The trustee may also recover from any person who was party to the disposition:

- any loss which the disposition caused to the insolvent's estate; and
- a penalty determined by the court, but not exceeding the amount by which the party would have benefited if the disposition was not set aside.

This may be recovered from the costs of setting aside and if the other party is a creditor, he forfeits any claims he may have had against the estate.

Disposition in fraud of creditors (*actio Pauliana*)

The Act doesn't deprive the creditors of their right under common law to have a disposition set aside as being in *fraudem creditorum*. The common law action is known as the *actio Pauliana* and the Plaintiff must prove the following to succeed:

- the transaction diminished the debtor's estate;
- the person who received from the debtor did not receive his own property;
- there was an intention to defraud and
- the fraud[25] took effect.

Creditors may invoke the *actio Pauliana* to recover not only the assets disposed of, but also any benefits accruing from the insolvent's fraud.

10.3. Exemptions of certain dispositions from Act

In certain instances, the provisions of the Act governing dispositions don't apply:

[25] Not criminal-law connotation: test is simply whether the object of the transaction was to give one creditor an unfair advantage over the others in insolvency – **Trustees Estate Chin v National Bank of SA**.

- Sections 26, 29 or 30: To property disposed of in accordance with the rules of an exchange or property disposed in terms of a master agreement;
- Sections 29, 30 or 31: If a prosecution of an offences has been instituted against the defendant, proceedings haven't been concluded and the estate of the defendant who has made an affected gift to another person is sequestrated - Section 35(2)(a) of the Prevention of Organised Crime Act, 121 of 1998.

10.4. **Transfer of business without prescribed notice** **Section 34 – Voidable sale of business**

Section 34(1) provides that, if a trader, without giving notice as prescribed by Act, transfers[26] in terms of a contract a business belonging to him, or its goodwill[27], or any goods or property forming part of it (except in ordinary course of that business or for securing payment of a debt), the transfer is void as against his creditors for 6 months thereafter, and it is void against his trustee if his estate is sequestrated at anytime within that period.

The notice referred to is a publication of a notice of intended transfer in the Government Gazette and two issues of both an Afrikaans and English newspaper circulating in the district in which that business is carried on. It must appear not less than 30 days and not more than 60 days before the date of transfer.

The following should be noted in regard to the scope and effect of Section 34(1):

- It is designed to protect the creditors of a business;
- It applies only to traders[28];
- It applies to the transfer of part of a business or the goodwill, goods or property forming part of the business;
- It doesn't apply to the transfer of goods or property of a business if the transfer is "in the ordinary course of that business";
- It doesn't apply where the transfer is to secure the payment of a debt;
- If a trustee alleges that a transfer falls within the section, he must prove that the goods formed part of the insolvent's business at time of transfer and that it wasn't in the ordinary course of the insolvent's business;
- An unadvertised transfer is not void in any absolute sense, only against the trustee.

10.5. **Transfer of business after proceedings instituted** **Section 34 – Voidable sale of business**

Where a trader transfers his business after another person has instituted proceedings against him for the purposes of enforcing a claim against him in connection with the business, Section 34(3) renders transfer void as against the person concerned for purpose of such enforcement if either:

- transferee is aware, at time of transfer, that proceedings have been instituted; or
- proceedings have been instituted in a HC or MC having jurisdiction in the district in which the business is carried on.

The following should be noted in regard to Section 34(3):

- The section applies irrespective of whether the trader gives notice of transfer;
- The creditor is protected if he has instituted proceedings prior to the transfer;
- Protection is not limited as to time;
- To apply section, claim sought to be enforced must be one "in connection with the business";
- Creditors not denied protection of section where agreement on which his claim is based has been amended or superseded by another agreement, provided sufficient close connection between the proceedings and second agreement;
- The section only renders the transfer of the business void against the creditor who instituted proceedings and to the extent of his claim.

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[26] "Transfer", for these purposes includes the transfer of possession, actual or constructive. (I.e. the trader does not have to transfer ownership to the other party).

[27] "Goodwill" is an intangible asset pertaining to an established and profitable business, for which a purchaser of the business may be expected to pay, because it is an asset which generates, or helps to generate, turnover and, consequently, profits.

[28] See definition paragraph 3.1(2)(viii)

11. CREDITOR'S CLAIMS AND THEIR RANKING – THE DIFFERENT TYPES OF CREDITORS

11.1. Types of creditors

(1) Concurrent creditors

→ They don't enjoy any advantage over other creditors of the insolvent;

→ They are paid out of the free residue[29] after any preferent creditors have been paid;

→ Concurrent creditors all rank equal and, if the free residue is insufficient to meet their claims, each receives an equal portion of his claim by way of a dividend, eg.

Calculating concurrent creditor's dividends if the free residue is insufficient:

① $\frac{\text{Free residue}}{\text{Total amount of concurrent creditor's claims}}$ = **Proportion of cents in the Rand**

② $\frac{\text{Concurrent creditor's claim X Proportion of cents in the Rand}}{100}$ = **Dividend**

(2) Secured creditors

→ A secured creditor holds security for his claims in the form of a special mortgage, landlord's hypothec, pledge or right of retention[30].

→ A secured creditor is entitled to be paid out of proceeds of the property under security, after payment of certain expenses and any secured claim which ranks before his. If proceeds of the encumbered property are insufficient to cover his claim, he then has a concurrent claim for the balance.

→ A secured creditor may, when proving his claim, choose to rely exclusively on his security and, in doing so, waives any right to participate in the free residue, but he is less likely to be called upon to contribute towards the costs of sequestration than one who elects to preserve his right to share in free residue.

(3) Preferent creditors

Section 2 of Act – Definitions

"preference", in relation to any claim against an insolvent estate, means the right to payment of that claim out of the assets of the estate in preference to other claims;

Strictly speaking, secured creditors are preferent creditors, but the term "preferent creditor" is reserved for a creditor whose claim isn't secured but nevertheless ranks above the claims of concurrent creditors and whose preference is created in terms of the Act:

Section 96	Funeral and death-bed expenses
Section 97	Costs of sequestration
Section 98	Costs of execution
Section 98A	Salaries or wages of former employees of insolvent
Section 99	Certain statutory obligations
Section 101	Income tax
Section 102	Claims of holders of general bonds and certain special bonds

Those unsecured, preferent creditors admittedly have a preference among themselves and above concurrent creditors, but they are not secured creditors, because their claims are not paid out of the proceeds of a specific asset.

A preferent creditor is entitled to payment out of the free residue of the estate, ie that portion which is not subject to any security interest, and a predetermined order of preference, as well as maximum amounts, is laid down by the Act. If a claim exceeds the statutory maximum, the creditor concerned has a concurrent claim for the balance.

11.2. Types of security conferring preference

(1) Special mortgage

Section 88 – Certain mortgages invalid

In terms of Section 2 of the Act, a special mortgage[31] is:

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[29] See definition paragraph 2.2(2) - the unencumbered part of the estate

[30] The definition in Section 2 contemplates real security only: a creditor whose claim is secured by suretyship is not secured

- → a mortgage bond hypothecating immovable property;
- → a notarial bond hypothecating specially described movable property registered after 7 May 1993 ito Section 1 of Security by Means of Movable Property Act 57 of 1993; or
- → a notarial bond hypothecating specially described movable property registered before 7 May 1993 in terms of Section 1 of the Notarial Bonds Act, 18 of 1932.

It excludes any other bond hypothecating movable property, thus a general notarial bond[32] doesn't qualify as a special mortgage. However, it does confer a preference in respect of the free residue. Section 88 lays down that a bond (other than a *kustingbrief*[33] and including a general notarial bond) gives no security or preference if:

- → the estate was sequestrated within 6 months after lodging of the bond with the Registrar of Deeds for registration;
- → the debt was incurred more than 2 months prior to lodging of the bond; and
- → the debt was not previously secured.

(2) Landlord's legal hypothec

Section 85 – Exclusion or limitation of preference under legal hypothec

A landlord who is owed rent has a hypothec over movable property brought on to the leased premises for the use by the tenant. On insolvency, the landlord has a secured claim in respect of all movable assets owned by the insolvent which are covered by the hypothec in terms of Section 85(2). The claim is secured up to an amount of:

Rent payment interval	Claimable amount
Monthly or shorter intervals	3 months' rent
> 1 month, but < 3 months	6 months' rent
> 3 month, but < 6 months	9 months' rent
> 6 months	15 months' rent

In respect of any excess, the landlord has a concurrent claim and he obtains no preference in relation to goods belonging to third parties that are subject to the hypothec.

(3) Pledge

A valid pledge is constituted where there is delivery of movable property to a creditor on the understanding that it will be retained by him until his claim has been satisfied.

(4) Right of retention

A party has a right of retention (or lien) over specific property belonging to another if he has expended labour or incurred expenses in respect of the property and there are two types:

i) Enrichment liens

So called as they are based on unjustified enrichment and there are 2 kinds:

- o Salvage liens
- o Improvement liens

The holder of an enrichment lien may retain the property until compensated for his expenses and labour, but cannot insist on payment of more than the amount by which the owner has actually been enriched.

ii) Debtor and creditor liens

These are based on contract and a creditor who holds one is entitled to retain the property as against the debtor until he has paid the amount due in terms of contract.

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[31] Provides security

[32] A general notarial bond over movable property is a bond which binds all the mortgagor's movable property in general and merely provides a (relatively weak) preference in terms of Section 102 of the Act. It's not possible to register a general bond over all the mortgagor's immovable property.

[33] A "kustingsbrief" is a bond which is registered simultaneously with the transfer of the piece of land concerned, in order to secure either the outstanding purchase price of the land, or the repayment of a loan made to the buyer to enable him to pay the purchase price of the land. Example: A sells his farm to B. B pays half the purchase price against registration of transfer, and the rest of the purchase price is secured by a bond over the land which is registered in favour of A simultaneously with the transfer to B.

(5) Instalment agreement hypothec

If movable property has been delivered to a debtor under an installment agreement, the seller acquires, on sequestration, a hypothec over the property which secures his claim for the balance outstanding under the contract in terms of Section 84(1).

11.3. **Ranking of claims**

Act lays down order in which claims against insolvent estate must be paid. The estate, for purposes of distribution, consists of proceeds of both encumbered and unencumbered assets. The proceeds of each encumbered asset are applied to pay the claim(s) secured by that asset. Any balance remaining after payment of secured creditors is combined with proceeds of unencumbered assets to pay the remaining creditors. The free residue is then used first to satisfy the preferent creditors in full (in their order of preference) and thereafter to pay the claims of the concurrent creditors.

(1) Encumbered assets[34]

i) Initial costs — **Section 89 – Costs to which securities are subject**

In terms of Section 89(1), the proceeds of each encumbered asset must be applied to the payment of certain costs before payment of the claim(s) secured by the asset. The costs are the following:

- Costs of maintaining, conserving and realizing the asset in question;
- Trustee's remuneration in respect of the asset;
- A proportionate share of costs incurred by trustee in giving security;
- A proportionate share of the Master's fees;
- If the asset is immovable property, any tax which is, or will become, due on it for a period not exceeding 2 years immediately preceding the date of sequestration; for the period from the date of sequestration to the date of transfer of the property; and together with any interest or penalty which may be due on the tax.

ii) Secured claims — **Section 95 – Application of proceeds of securities**

After payment of the initial costs, balance of the proceeds of the encumbered asset, including any interest earned on the price obtained for the asset, must be used to pay all the claims secured by the asset, in proper order of preference – Section 95(1). Secured claims rank among themselves in the following order:

- Immovable property
  - Enrichment lien;
  - Special mortgage bond(s) and contract recorded in terms of the ALA in the order in which they were registered or recorded;
  - Debtor and creditor lien.
- Movable property
  - Enrichment lien;
  - Pledge;
  - Special notarial bonds in the order in which they were registered;
  - Debtor and creditor lien;
  - Instalment agreement hypothec;
  - Landlord's hypothec.

Interest due on a claim for a period not exceeding 2 years immediately preceding the date of sequestration is secured as if it were part of the capital sum. Interest from date of sequestration to date of payment is also secured.

(2) Unencumbered assets (free residue) — **Listed in order of preference**

i) Funeral expenses

Funeral expenses of the insolvent, his wife or minor child to a maximum of R 300.00.

ii) Death-bed expenses

Death-bed expenses of the insolvent, his wife or minor child incurred for medical attendances, nursing and medical necessaries to a maximum of R 300.00.

[34] An asset that serves as real security.

iii) Costs of sequestration

- Sheriff's charges incurred since sequestration;
- Master's fees;
- Miscellaneous charges comprising of the:
  - taxed costs of sequestration;
  - fee allowed by the Master to a person who assisted the insolvent or spouse in drawing up a statement of affairs;
  - remuneration of *curator bonis* (if any);
  - remuneration of the trustee; and then
  - all other costs of administration and liquidation.

iv) Costs of execution

- The taxed fees of the sheriff in connection with any execution upon the insolvent's property and the proceedings leading to that execution; and
- Any other taxed costs in those proceedings, not exceeding R 50.00.

Amount paid mustn't exceed proceeds of property in question if it was under attachment or if proceeds of sale were in hands of execution officer at date of sequestration.

v) Salary or remuneration of employees

- Salary or wages due to an employee, for a period not exceeding 3 months, to a maximum of R 12,000.00;
- Payment in respect of leave due to an employee, to a maximum of R 4,000.00;
- Payment in respect of paid absence, for a period not exceeding 3 months, to a maximum of R 4,000.00;
- Any retrenchment pay due to an employee, to a maximum of R 12,000.00;
- Any contributions which were owing to any pension etc, maximum of R 12,000.00.

If an employee's claim for salary, wages, leave or other payments exceeds the limits of the preference, he has a concurrent claim for the excess under Section 38(10) of the Act as loss suffered because of the suspension or the termination of the contract before its expiry.

vi) Statutory obligations

- Any amount due to the Compensation Commissioner in terms of the Compensation for Occupational Injuries and Diseases Act, 130 of 1993;
- Any tax which the insolvent deducted or withheld from remuneration, royalties, but did not pay to SARS;
- Any amount due to the Mines and Works Compensation Fund;
- Any customs, excise, sales duty, interest, penalty or fine due;
- Any amount provided to the insolvent by the State from the National Supplies Procurement Fund;
- Any VAT, interest, fine or penalty due;
- Any contribution, penalty or other payment owed by the insolvent in his capacity as employer to the UIF.

vii) Income tax

Any tax on income or profit and interest on tax for which insolvent is personally liable.

viii) Claim secured by general and special bond

Held over movable property registered before 7 May 1993 and the preference is not limited to the proceeds of the bonded property, but extends to the entire free residue.

ix) Claims of concurrent creditors

- Concurrent creditors – Section 103(1)(a);
- Secured creditors whose claims exceed the sums payable to them from proceeds of their securities and who didn't state in their affidavits that they relied solely on the proceeds of their securities – Sections 83(12) and 89(2);
- Preferent creditors for non-preferent balance of their claims – Section 103(1)(a);

- The balance must be distributed among the various creditors in proportion to the amounts owing to each of them – Section 103(1)(a).

12. COMPOSITION

Section 119 – Composition

A debtor who is in financial difficulty or whose estate has been provisionally sequestrated can avert insolvency by entering into a compromise with his creditors. There are two forms of compromise:

- Common-law compromise:

  Based on a contract and requires approval of all creditors to be of any practical value. Creditors may be in a better position, as they will get dividends earlier than in sequestration and it may be higher due to savings of sequestration costs. For debtor advantage of a common law composition is that he is released from his debts without having to suffer consequences of sequestration.

- Statutory composition:

  A Section 119 composition is a statutory mechanism under which the decision of the majority of the creditors binds the dissenting minority. The disadvantage is that the sequestration order isn't discharged and debtor remains an unrehabilitated insolvent but can apply for early rehabilitation.

Difference	Common-law compromise	Statutory composition
Legal basis	Law of contract	Statutory
Acceptance	Written consent of all concurrent creditors	Majority of creditors binds the minority

12.1. Common-law compromise

After a provisional order of sequestration has been granted, or even before, insolvent may enter into a written agreement with his creditors and the provisional trustee to pay certain dividends on the creditors' claims, on condition that he is released from his debts and any provisional order of sequetsration is discharged.

12.2. Offer of composition in terms of Section 119

Submission of offer to creditors via trustee

At any time after first meeting, insolvent may submit a written offer of composition to trustee, who, if of opinion that creditors will probably accept, must post it immediately in a registered letter or delivered it. If trustee, however, sees no likelihood that they will accept, he informs insolvent that it is unacceptable and that he doesn't propose to send it to them. Insolvent may then appeal to the Master, who may direct trustee to send it after consideration.

When it is sent to creditors, a meeting to consider the offer must simultaneously be convened - date of the meeting must not be earlier than 14 days, and not later than 28 days, after posting or delivery of notice. Notice must contain specific reference to offer of compensation as a matter to be dealt with at the meeting

Terms of composition

An offer may contain any terms insolvent sees fit to incorporate init, including terms to the effect that he should immediately be reinvested with his assets and that he should be released from further liability in respect of his debts. Requirements and restrictions imposed by Act:

- Where an offer of composition provides for the giving of security, the nature of the security should be specified fully and, if the security is to consist of a surety bond or guarantee, every surety should be named;
- An offer of composition may not be accepted if it contains a condition entitling one creditor to obtain, as against another creditor, a benefit to which former wouldn't have been entitled upon the distribution of the estate in the normal way;
- A condition which makes an offer of composition subject to the rehabilitation of the insolvent is of no effect.

12.3. Acceptance of Section 119 composition

To give rise to a binding composition, the offer must be accepted by the creditors whose votes amount to not less than ¾ in value and ¾ in number of the votes of all proved creditors, and payment in terms of the composition must've been made or security for the payment is given

Zulman & others v Schultz: Where creditors accept an offer of compromise, not in the honest belief that compromise is in interests of the estate or for benefit of creditors generally, but from feelings of pity or compassion, or with a view to benefit debtor, the acceptance is invalid.

12.4. Consequences of Section 119 composition

(1) All concurrent creditors bound

An offer which has been accepted is binding on insolvent and all creditors in so far as their claims aren't secured or otherwise preferent. Basis of liability isn't contractual since creditors may be held bound even though they voted against acceptance or weren't able to as their claims haven't been proved. Liability of a surety for a concurrent debt of insolvent would fall away when a composition is accepted, as composition has effect of discharging original debt by replacing it with another. Exception to this general rule: Section 120(3) of Act expressly states that the liability of a surety isn't affected by acceptance of a composition.

Composition is best described as a statutory novation which discharges claims of concurrent creditors, whose rights are thereafter determined by the provisions of composition itself.

(2) Restoration of property to insolvent

No transfer or delivery is necessary, revesting takes place by operation of law if it's a term of composition.

(3) Restoration of property to solvent spouse

A composition isn't binding on creditors of solvent spouse and, on acceptance, property of the solvent spouse which vested in the trustee must be restored.

(4) Trustee to frame accounts, administer composition and report to creditors

Trustee is obliged to frame a liquidation account and plan of distribution of assets which are, or will become, available for distribution among creditors under composition. All provisions of Act which relate to a liquidation account and plan of distribution are applicable. Any moneys to be paid and anything done for benefit of creditors in pursuance of composition, must be paid and done through trustee. He is, however, under no duty to a creditor who fails to prove a claim before he has made a final distribution among proved creditors. Trustee is obliged to investigate affairs and transactions of insolvent prior to insolvency and to report on them to creditors in usual way, notwithstanding composition acceptance.

(5) Right to prompt rehabilitation

Insolvent must wait for a certain period of time before applying for rehabilitation. Where offer of composition is accepted, however, insolvent may be entitled immediately to apply.

13. REHABILITATION

Section 124 – Application for rehabilitation

Rehabilitation enables insolvent to make a new beginning and discharges him from all disabilities that flowed from the sequestration of his estate, and debts which arose before sequestration may no longer be recovered from him, although creditors retain their rights against insolvent estate itself. It takes place automatically, by lapse of a prescribed period of time, but insolvent usually asks court to rehabilitate him before expiry of the prescribed period.

13.1. Automatic rehabilitation after 10 years

Insolvent not rehabilitated by court within period of 10 years from date of sequestration is deemed to be rehabilitated unless court, on application by an interested person[35], orders otherwise before expiry of 10-year period. If order is issued, Registrar must send a copy thereof to every Registrar of Deeds, who must enter a *caveat*[36] against transfer of all immovables, or cancellation or cession of any bond belonging to or registered in name of insolvent. This remains in force until rehabilitation.

13.2. Rehabilitation by court within 10 years

The Act sets out circumstances under which rehabilitation may be sought prior to expiration of the 10-year period and the procedure to be followed to obtain an order of court.

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[35] Examples of reasons to apply: i) Just before the completion of the 10-year period, the trustee becomes aware of some possible impeachable dispositions; ii) Insolvent's conditional rights as *fideicommissary* heir will probably become unconditional shortly after the lapse of the period of 10 years.

[36] See paragraph 5.4 for definition

(1) Circumstances in which rehabilitation may be sought

i) Composition of not less than 50 cents in the Rand

Insolvent may immediately seek order of rehabilitation if a certificate from Master has been obtained that creditors accepted offer of composition and payment was made, or security was given for payment of not less than 50 cents in Rand for every concurrent claim proved. If less than 50 cents was accepted, only after lapse of prescribed period.

ii) Lapse of prescribed period after confirmation of first account

Subject to qualifications below, insolvent may apply for his rehabilitation after 12 months have elapsed from confirmation by Master of the first account in the estate:

- If estate has been sequestrated before, the period which must elapse before he can apply is 3 years from the date of confirmation of the first account;
- If convicted of a fraudulent act in relation to insolvency, the period which must elapse before he can apply is 5 years from the date of conviction;
- If Master has recommended rehabilitation, order may be obtained within 4 years.

iii) No claims proved after 6 months

An insolvent may apply for his rehabilitaion after a period of 6 months has elapsed from the date of sequestration if:

- at the time of application, no claim has been proved against his estate;
- he hasn't been convicted of any fraudulent act in relation to his insolvency; and
- his estate hasn't been sequestrated before.

iv) Full payment of all proved claims

At any time after confirmation by Master of a plan of distribution providing for payment in full of all proved claims with interest and all costs of sequestration, insolvent may apply for sequestration.

(2) Court's discretion

The rehabilitation of an insolvent is a matter which lies solely within court's discretion and the following is guidelines as to how the court will exercise its discretion:

i) Postponement of rehabilitation

Where further information is needed; where criminal proceedings against insolvent are pending; or as a mark of disapproval of applicant's conduct.

ii) Grant of rehabilitation subject to a condition

Ex parte Meine: Court won't impose a condition on rehabilitation unless there is something out of the ordinary to justify it. There must be special circumstances which make it just and equitable to impose the condition and it must be properly motivated.

Ex parte Fowler: Court won't impose a condition that insolvent pay unpaid claims simply because he has managed to accumalate an estate during sequestration and is in a position financially to discharge claims.

Section 127(3) provides that, among conditions that may be attached to rehabilitation, court may require insolvent to consent to judgment being entered against him for payment of unsatisfied balance of debt which was, or could be, proved against estate.

iii) Refusal of rehabilitation

Examples of factors which may persuade court to refuse an order of rehabilitation are that insolvent:

- conducted his business in an improper and negligent manner;
- failed to keep proper books of account;
- ran up excessive debts prior to sequestration;
- was difficult and refused to co-operate with trustee in administration of estate;
- was highly obstructive in the administration of his estate and made numerous unfounded allegations against trustee and Master's staff;

- sidestepped the inhibitions of insolvency by living in luxury without making contributions to creditors;
- failed to set out all circumstances relating to his insolvency in his application; and
- didn't disclose anything to suggest that his learned his lesson in his application.

Court won't ordinarily refuse rehabilitation merely because there was a large excess in liabilities over assets, but it may influence if there are other unsatisfactory features.

iv) Considerations in favour of unconditional rehabilitation

Certain factors contribute to an unconditional rehabilitaion, such as:

- The insolvent only incurred very small debts;
- The insolvent wasn't to blame for his sequestration, it came purley by misfortune;
- Neither creditors nor trustee bothered to take steps under Section 23(5) to obtain part of insolvent's earnings during his insolvency;
- No opposition from creditors, trustee or Master.

13.3. Effect of rehabilitation

Puts an end to sequestration and relieves insolvent of every disability resulting from sequestration and discharges all debts which were due or cause of which arose before sequestration. It doesn't reinvest insolvent with his former estate, except where:

- a compensation provides that the estate will reinvest in insolvent; and
- the basis of rehabilitation was that no claims were proved within 6 months of the sequestration.

13.4. Declaratory order regarding property

If insolvent can show that neither trustee nor creditors laid claim to an asset in his estate, he may, on applying for rehabilitation, or thereafter, ask for an order declaring that he is entitled to it. To obtain the order, insolvent must comply with the following requirements:

- Publish notice of intention to apply in the Government Gazette;
- Service copy of notice to Master, trustee and all creditors whose claims haven't been satisfied;
- In application, he must show that trustee and creditors have full knowledge of the facts and he must give full information to establish that the property was acquired adversely to the trustee.

14. PARTNERSHIP AND SEQUESTRATION

Section 13 – Sequestration of partnership estate

Without specific provisions in Act it wouldn't have been possible to sequestrate a partnership, as a partnership isn't considered to be a separate juristic person in eyes of law. It's an established rule that creditor of partnership must sue partnership for debt and must first attach partnership assets. Only when proceeds of partnership assets are insufficient to satisfy, creditor may attach individual partners' assets for execution. Rules to bring about a degree of separation between partnership and individual partners are also found in Act.

14.1. Voluntary surrender of partnership estate

Application to surrender a partnership estate must be brought by all partners or their agents, but the following need not apply:

- a partner not residing in South Africa;
- a partner *en commandite* (anonymous partner)[37];
- a special partner[38].

Simultaneously with an application for surrender of a partnership estate, each partner (except ones stated above) must apply for the acceptance of the surrender of his private estate. Notice of intention to surrender both can be done in one application with separate statements of affairs.

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[37] A partner *en commandite*, unlike an ordinary partner, doesn't participate in the management and business of the partnership. He merely makes an initial contribution (either money or goods) to the partnership assets and leaves it to the other partners to manage the partnership. Although, like the ordinary partners, he shares in the profits of the partnership, he is not liable to the partnership creditors for the partnership debts. The only risk which he runs is the loss of his initial contribution to the partnership property in the form of money or goods. Because he cannot be held liable for partnership debts, there is no reason that his private estate should be sequestrated when the partnership estate is sequestrated.

[38] Because there're probably no more partnerships under repealed Natal and Cape legislation, "special partnerships" are ignored.

14.2. **Compulsory sequestration of partnership estate**

If court sequestrates estate of a partnership, it's bound to sequestrate private estate of every member of partnership simultaneously, except for:

- a partner not residing in South Africa;
- a partner *en commandite* (anonymous partner);
- a special partner.

Partnership itself never becomes an "insolvent", simultaneous sequestration of partners' estates isn't just procedural, but vital. Court won't sequestrate private estate of a partner if he undertakes to pay partnership debts within a period fixed by court and gives security for such payment.

Where private estate of partner is unable to meet costs of sequestration payable out of that estate fully, balance must be paid out of assets of partnership, but opposite doesn't apply. A partnership estate may be compulsory sequestrated on the grounds of an act of insolvency committed by a partner, only if he acted in his capacity as a partner.

14.3. **Sequestration of partner's estate**

If estate of a partner is sequestrated, it isn't necessary for partnership estate or private estates of other partners to be sequestrated. However, it terminates the partnership, *ipso iure*, which must be wound up as a result. When the partnership is dissolved, partnership assets are divided among partners in terms of the partnership contract or common law and the insolvent partner's share vests in the trustee. Remaining partners may then form a new partnership.

14.4. **Composition**

(1) Composition by partnership

Some suggest a partnership can make a valid composition and be reinvested with its assets even though it ceases to exist in terms of common law. It's probably more correct that a new partnership takes the place of the old one, which dissolved.

(2) Composition by partner

When partnership and private estates are simultaneously under sequestration, acceptance of an offer of composition doesn't take effect until 6 weeks expired as from date of written notice of acceptance given by trustee of private estates to trustee of partnership estate in terms of Section 121(1).

Because trustee of partnership estate is entitled to any surplus out of partner's estate after payment to that partner's private creditors, interest of partnership creditors must be protected if a partner has entered into a composition with his private creditors. Protection is that trustee of partnership estate has a choice of taking over all private assets of the partner, provided that trustee is prepared to carry out composition.

14.5. **Proof of claims**

Principle: partnership assets are applied to payment of partnership debts; separate estate assets to payment of separate estate debts – Section 49(1). Therefore, if partnership and individual estates are sequestrated simultaneously, creditors of partnership aren't entitled to prove against separate estates of partners and creditors of individual estates aren't entitled to prove against partnership estate. However, SARS may prove claims for income tax and interest against a partnership estate for amounts due by partners – Section 49(2).

14.6. **Separate administration of estates**

Administration of partnership and partner estates must be kept entirely separate and separate accounts must be framed for each estate – Section 92(5).

14.7. **Surplus of either estate**

If, after all estates have been administered, surplus remains in a partner's separate estate, trustee in partnership estate is entitled to this surplus for benefit of partnership creditors – Section 49(1). Similarly, trustee of an individual estate is entitled to share in any surplus in partnership estate to which the partner would've been entitled.

14.8. **Rehabilitation**

As a partnership is ***ipso facto*** (by the mere fact) terminated on sequestration of its estate, a partnership estate can never be rehabilitated – Section 128. Court won't refuse rehabilitation of a

partner merely because there is a deficiency in the partnership estate or because the partnership estate hasn't been finalised.

15. WINDING-UP OF COMPANIES

"Winding-up" means the procedure by which a company's assets are sold, its debts are paid and any money left over is divided amongst members (shareholders) according to their rights. Both solvent and insolvent companies may be wound up. After completion of winding-up process, the company is dissolved and Registrar of Companies ("RC") publishes a notice to this effect. The Act expressly excludes the sequestration of companies, but the Companies Act, 61 of 1973 ("CA") extends many of the principles of insolvency to companies.

15.1. Modes of winding-up

Section 343 of CA

- Winding-up by the court (compulsory winding-up) - initiated by an application to court; or
- Voluntary winding-up may be either a creditors' or a members' voluntary winding-up and both are initiated by a special resolution of members.

On application by a creditor, member or Master, court may convert a voluntary winding-up into a compulsory one and confirm any steps already taken in die voluntary winding-up.

15.2. Winding-up by court

(1) Jurisdiction of court

Section 12(1) of CA

Court which has jurisdiction is Provincial or Local Division of the HC having jurisdiction over the area in which the company has its registered office or main place of business. If registered office or main place of business is in different areas, both courts have jurisdiction.

(2) When company may be wound up by court

Section 344 of CA

Section 344 of CA sets out the various grounds on which a company may be wound up.

i) Special resolution

Court may wind up a company if it has passed a special resolution to be wound up by court at a general meeting of members and lodged it with the RC for registration within 6 months after it was adopted. If this isn't done, resolution lapses and may no longer serve as a ground for winding-up, unless court orders otherwise. Apart from this requirement, a special resolution acquires legal force only when it has been registered and application for winding-up on this ground may therefore not be brought immediately after resolution has been adopted, but only after its registration.

ii) Premature Commencement of business

Court may wind up a company if it has commenced business before the RC has certified that it was entitled to do so.

iii) Failure to commence or continue with business

Court may wind up a company if it hasn't commenced business within a year from its incorporation or if it has suspended its business for a whole year.

iv) Public company's members less than seven

Court may wind up a public company if the number of its members has fallen below 7. This ground for winding-up of the company is contained in Section 66 of the CA, which stipulated that a member of a public company (except a wholly-owned subsidiary) is personally liable for the company's debts if company carries on business for a period of more than 6 months while it has fewer than 7 members. Such a member is then liable for the debts incurred after expiry of the period of 6 months if he knew that the company carried on business while it had fewer than 7 members. This being the case, such a member must be enabled to prevent his becoming liable for the company's debts and this he may do by applying for the winding-up of the company.

v) Loss of capital

Court may wind up a company if 75% of its issued share capital has been lost or become useless for its business.

vi) Inability to pay debts **Section 345 of CA**

Court may wind up a company if it's unable to pay its debts as described in Section 345 of CA, which determines that a company is deemed unable to pay its debts in the following cases:

- A creditor, to whom at least R 100.00 is due, has left a demand for payment which has been neglected for 3 weeks[39];
- A warrant of execution issued on a judgment against company has been returned by sheriff with endorsement that he couldn't find disposable property sufficient to satisfy judgment or that the property he found didn't, upon sale, satisfy the process;
- It is proved to the satisfaction of court that the company is unable to pay its debts.

vii) Dissolution of external company

Court may wind up an external company if it has been dissolved in country in which it was incorporated, or has ceased to carry on business, or is carrying on business only for purpose of winding up its affairs. It may be liquidated as if it were an independent entity, even if the foreign company to which it is 'related' isn't liquidated or dissolved.

viii) Just and equitable

Court may wind up a company if it appears that it is just and equitable that it should be wound up. However, "just and equitable" ground is not regarded as some limitless ground for winding up a company and court only resorted thereto in specific cases as they are reluctant to extend its application. The following instances have been held as just and equitable by the court:

- Where main object for which company was formed isn't possible of being attained.
- Where company's objects are illegal.
- Where there is a justifiable lack of confidence in the conduct and management of the company's affairs.
- Where a voting power deadlock cannot be resolved except by winding-up.
- Where the company is a "quasi-partnership"[40] and circumstances exist which would be good grounds for dissolving a partnership.
- Where minority shareholders are oppressed by controlling shareholders

(3) Parties who may apply **Section 346 of CA**

Onus in each case is on applicant to establish that he has *locus standi* to bring application.

i) The company

When general meeting of members has resolved that company be wound up by court, the special resolution is a ground for winding-up as well as an authority to the directors to make application. If a different ground for winding-up is relied upon, authority will have to be given to make application by a general meeting of members. However, there is a measure of uncertainty on whether the board of directors may, on their own authority, decide to apply for winding-up on behalf of the company.

ii) One or more creditors

Application may be brought by one or more creditors, including contingent or prospective creditors. The claim need not be equal or exceed a particular amount.

iii) One or more of its members

Application may be brought by one or more of company's members, or by a person appointed as executor, trustee, liquidator, curator or guardian in respect of a member who is deceased, insolvent or under a disability. However, a member may not apply unless he has been registered as such in register of members for at least 6 months prior to the date of the application or his shares devolved upon him through the death

[39] In **Rand Air v Ray Bester Investments** it was decided, *inter alia*, that a summons is not a demand as contemplated in Section 345(1)(a). A summons is a document in which sheriff is ordered to convey certain information to debtor. It isn't a demand to pay addressed to debtor himself. Further, on proof of inability to pay debts by means of a return by sheriff to effect that he couldn't find sufficient disposable property to comply with a judgment, it would've been unnecessary if summons already qualified as a demand.

[40] Founded on personal relationship of confidence and trust similar to partners in partnership. Usually requires members to act reasonably and honestly towards each other and with friendly co-operation in running company's affairs. If 1 or more members acts contrary to spirit of this relationship and, in so doing, effectively destroys it, court may hold it just and equitable to wind up company.

of a formed holder. Further, a member may not apply on the grounds of special resolution, inability to pay debts or dissolution of external company. The various ways of initiating the winding-up of a company:

- Members may resolve by special resolution to proceed with a members' voluntary winding-up of the company.
- Members may resolve by special resolution to proceed with a creditors' voluntary winding-up of the company.
- Members may resolve by special resolution that the company should apply to the court for a winding-up order.
- One or more members (who meet certain requirements) may apply to court for a winding-up order.

iv) Any or all of the above

Application may be brought jointly by some or all of the parties mentioned above (ie, the company, creditors and members).

v) The Master

Master may apply to convert a voluntary winding-up into a winding-up by court. The reason usually being to make available the procedure for examination and enquiry under Section 417 and 418 of the CA.

vi) A provisional or final judicial manager

A provisional judicial manager may bring the application where the provisional order of judicial management is discharged.

(4) Steps prior to application **Section 346 of CA**

i) Security for costs

Party applying for winding-up must give sufficient security for payment of all fees and charges.

vii) Master's report

Before presenting his application to court, applicant must serve a copy on Master, who may report to court any facts which he has ascertained which may justify postponing or dismissing the application.

viii) Notification of certain interested parties

When presenting application to court, applicant must also furnish a copy of it to the following:

- Every registered trade union which represents any of the company's employees;
- The employees themselves;
- SARS; and
- The company, unless application was made by the company

(5) Powers of court **Section 347 of CA**

Court may grant or dismiss any application for winding-up. In practice, court usually doesn't make a final order immediately, but makes a provisional winding-up order and issues a rule *nisi*. Court's power to grant application for winding-up is discretionary, but is limited where creditor has proved that company is unable to pay its debts, in which event, creditor is entitled to a winding-up order and court needn't be satisfied that winding-up will be to advantage of company's creditors.

The reason for refusing is essentially that the application amounts to abuse of the winding-up procedure. Where application is brought by members of company, court won't make a winding-up order if some other remedy is available and they act unreasonably in seeking to have company wound up instead of pursuing the remedy.

Where application is founded on fact that company commenced business before the RC certified that it was entitled to, court may, instead of granting a winding-up order, direct the company to obtain the certificate from the RC.

15.3. Voluntary winding-up

A company may be wound up voluntarily if it has adopted a special resolution to that effect and that resolution has been registered by the RC.

(1) Members' voluntary winding-up

Section 350 of CA

A members' voluntary winding-up can take place only if company is unable to pay its debts in full. In terms of Section 350(1) of the CA, a resolution to proceed with a members' voluntary winding-up is void unless, prior to registration of the resolution, either:

- → security is furnished to Master's satisfaction for payment of the debts of company within 12 months from commencement of winding-up; or
- → Master dispenses with the security on production of both an affidavit by the directors of company that it has no debts and a certificate by the auditor of company that, to his best knowledge and belief, and according to the records of company, it has no debts.

This is a clear example of a case where a solvent company can be wound up. The winding-up is simply the process used to distribute the assets of company among the shareholders, after provision has been made for the payment of outstanding debts

(2) Creditors' voluntary winding-up

May be resorted to where the company is unable to pay its debts and because an application to court is avoided, voluntary winding-up may bring about a saving of costs. Master may intervene and convert the voluntary winding-up into a winding-up by the court.

15.4. Consequences of winding-up

(1) Commencement of winding-up

Section 348 of CA

A winding-up by the court is deemed to commence at the time of the presentation to court of the application for winding-up. A voluntary winding-up commences when the relevant special resolution of members is registered with the RC.

Determining the precise time of commencement is important because various consequences of winding-up come into effect when the winding-up commences, as opposed to when the court makes a provisional or final winding-up order.

(2) Directors divested of powers and control

Winding-up establishes a *concursus creditorum*, which is aimed at ensuring that company's property is collected and distributed among creditors in the prescribed order of preference. Company doesn't lose its corporate identity, nor does it lose its assets unless so ordered. From the moment winding-up commences, the following consequences ensue:

- → Powers of directors cease and directors become ***functus officio*** (no longer in office).
- → Company's property is deemed to be in custody and under control of the Master until a provisional liquidator has been appointed.
- → Company may not continue with its business except in so far as may be necessary for its beneficial winding-up.

(3) Subsequent unauthorised dispositions void

After winding-up has commencement:

- → any transfer of shares without the liquidator's permission is void; and
- → if company is unable to pay debts, every disposition of its property not sanctioned by court is void.

(4) Stay of proceedings

Once a winding-up order is made or special resolution for voluntary winding-up is registered, all civil proceedings by or against company are suspended until appointment of liquidator. Any attachment or execution put in force against the assets is void.

After appointment of liquidator, civil proceedings may continue or commence, including execution proceedings put in force before commencement of the order.

(5) Notice of winding-up

Master must, on receipt of a winding-up order, give notice of the winding-up in Government Gazette and transmit a copy thereof to certain sheriffs and Registrars of Deeds.

A company which has passed a resolution for its voluntary winding-up must, within 28 days after registration of resolution, give notice in Gazette and lodge a certified copy of resolution to Master together with the following:

- → In the case of members' voluntary winding-up: A certified copy of any resolution passed by the company nominating a liquidator
- → In the case of creditors' voluntary winding-up: Two certified copies of a statement setting out affairs of the company.

A copy of the winding-up order must also be served on::

- → Every registered trade union which represents any of the company's employees;
- → The employees themselves;
- → SARS; and
- → The company, unless application was made by the company

15.5. **The liquidator**

(1) Appointment of provisional liquidator

After the winding-up order has been made, or a special resolution has been registered, the Master may appoint any suitable person as the provisional liquidator, who must give security to the satisfaction of the Master for the proper performance of his duties.

(2) Appointment of liquidator

The Master must appoint as liquidator(s):

- → in the case of members' voluntary winding-up, the person nominated in resolution;
- → in the case of creditors' voluntary winding-up and a winding-up by the court, the person(s) nominated by first meeting of creditors and initial meeting of members.

Master may decline to appoint nominee who wasn't properly nominated, is disqualified from being appointed or fails to give security timeously and the Master may, at any time, appoint a co-liquidator. Any person aggrieved by Master's refusal or appointment may call upon him to submit his reasons to the Minister, who may confirm or set aside the Master's decision

(3) Persons disqualified from being liquidator **Section 372 of CA**

The following persons are disqualified from being nominated or appointed as a liquidator:

- → An insolvent;
- → A minor or any other person under legal disability;
- → A person declared to be incapable of being appointed as a liquidator for dishonesty or abuse of his position;
- → A person who has been removed from an office of trust by court or who has been disqualified from being a director;
- → A body corporate;
- → A person who has been convicted of theft, fraud, forgery, uttering a forged instrument or perjury and has been sentenced to imprisonment without the option of a fine or a fine exceeding R 20.00;
- → A person who, by misrepresentation or reward, induced or attempted to induce any person to vote or to nominate him;
- → A person not residing in South Africa;
- → A person who has acted as director, officer or auditor of company within 12 months before winding-up;
- → An agent authorised to vote for or on behalf of a creditor at a meeting who acts or purports to act under such authority.

(4) Removal of liquidator from office

The liquidator may be removed from office by the Master if:

- → he isn't qualified, or has become disqualified
- → he has not performed his duties satisfactorily;
- → if his estate has become insolvent or he has become mentally or physically incapable;

- → the majority in number and value of creditors or members, has requested the Master in writing;
- → if the Master is of the opinion that the liquidator is no longer suitable;

If Master doesn't remove, court may, but only if it's satisfied that removal of the liquidator will be to the general advantage and benefit of all interested in the winding-up

15.6. **Impeachable transactions**

Section 340 of CA

In terms of Section 340(1) of CA, every disposition by a company of its property which, if made by an individual, could, for any reason, be set aside in the event of his insolvency, may, if made by a company, be set aside in the event of the company being wound up and unable to pay all its debts, and the provisions of the law of insolvency apply, *mutatis mutandis*, to the disposition.

16. JUDICIAL MANAGEMENT AND COMPROMISE

A company unable to pay its debts has two alternatives to winding-up: judicial management and compromise between company and its creditors.

16.1. **Judicial management**

Judicial management is resorted to where a company is in financial trouble but has the potential to recover. The independent judicial manager (appointed by court) will observe and rectify financial maladies of company and enable the company to become a successful concern, although desired result is not always achieved.

Judicial management may be seen as a half-way house between a healthy company and winding-up. Because it costs money which will be wasted if the company eventually has to be wound up in any event, court will have to be satisfied that there is a reasonable probability that the company will become successful again if it is placed under judicial management.

(1) When company may be placed under judicial management

Section 427 of CA

In terms of Section 427(1) of CA, court may grant an order placing a company under judicial management where:

- → company, because of mismangment or any other cause, is unable to pay its debts or unable to meet its obligations;
- → company hasn't become or has been prevented from becoming a successful concern;
- → there is a reasonable probability that, if the company is placed under judicial management, it will be enabled to pay its debts or meet its obligations and become a successful concern; and
- → it appears just and equitable to grant the judicial management order.

The *onus* is on the applicant to establish a proper basis for judicial management. A judicial management order is a special concession and is granted only in exceptional circumstances.

(2) Who may apply

Same parties who may apply for winding-up of a company may apply for judicial management – Section 427(2) of CA (see paragraph 15.2(3)). In an application, court may also ***mero motu*** (motion of a party's own free will) order judicial management if circumstances permit.

(3) Impeachable dispositions

If company under judicial management is unable to pay its debts, the judicial manager may apply to court for the setting aside of any disposition which, in the case of insolvency of an individual, could have been set aside under the Act – Section 436(1) of CA.

A winding-up is deemed to commence at moment at which application is filed with the RC. The same principle applies with respect to a judicial manager who wishes to have a disposition set aside. For purposes of application of relevant provisions of the Act, the date on which the application for judicial management is filed is deemed to correspond to the date of a sequestration order – Section 436(2) of the CA.

16.2. **Compromise**

The CA sets out procedure by which a company may conclude a compromise with its creditors. It is also possible for a company which cannot pay its debts to conclude a common-law compromise with its creditors, but this procedure is seldom used in practice because of the difficulty of securing consent of each creditor.

(1) Procedure for compromise

Where a compromise is proposed between a company and its creditors, the court may, on application, order a meeting of creditors. Before a court will order a meeting, it must be satisfied that the offer of compromise is *prima facie* fair and reasonable and that it should be placed before the creditors for their consideration.

If the compromise is agreed to by majority in number representing ¾ in value of creditors, court may sanction the compromise or arrangement. However, court retains a discretion to refuse it even if the required majority voted in favour of it. An important factor in this regard is whether the company will be able to trade successfully after the compromise.

(2) Effect of compromise

If the compromise is approved by court, it binds all creditors, even those who rejected it. It also binds the liquidator or judicial manager.

17. WINDING-UP OF CLOSE CORPORATIONS

Winding-up of close corporations is dealt with by the Close Corporations Act, 69 of 1984 ("CCA"), but it effectively incorporates many of provisions of the CA on winding-up and makes them applicable to close corporations

A close-corporation ("CC") may be wound up voluntarily or by court and such a voluntary winding-up may be either a members' winding-up or a creditors' winding-up. Although a CC is capable of being wound up, it cannot be put under judicial management and cannot conclude a statutory compromise, but however, may enter into a composition.

17.1. Voluntary winding-up

A CC may be wound up voluntarily if all its members so resolve at a meeting called to consider the winding-up. The members must sign a written resolution, a copy of which must be lodged with the Registrar of Close Corporations ("RCC"), in duplicate and in the prescribed form, together with the prescribed fee. This resolution only takes effect once it's registered and lapses if not registered within 90 days.

17.2. Winding-up by court

(1) Jurisdiction of court

Although only a HC has jurisdiction to wind up a company, both a HC and MC have jurisdiction to wind up a corporation determined by CC's registered office or main place of business.

(2) When corporation may be wound up by court

Section 68 of CCA

Section 68 sets out the grounds on which a court may wind up a CC.

i) Resolution of members

Court may wind up a CC if members having 50% or more of total of votes at a meeting called for the purpose of considering the winding-up of the CC. Members must adopt and sign a written resolution that the CC be wound up by court.

ii) Failure to commence or continue with business

Court may wind up a CC if it hasn't commenced business within a year from its Registration or if it has suspended its business for a whole year.

iii) Inability to pay debts

Court may wind up a CC if it's unable to pay its debts. A CC is deemed unable to its debts in terms of Section 69(1)(a) if any of the following are complied with:

- A creditor, with a claim of at least R 200.00, has left a demand for payment which the CC has neglected for 21 days thereafter.
- Any process on a judgment against the CC has been returned by sheriff with an endorsement that he didn't find disposable property sufficient to satisfy judgement or that the property he found didn't, upon sale, satisfy the process.
- It is proved to the satisfaction of the court that the CC is unable to pay its debts

iv) Just and equitable

Court may wind up a CC if it appears that it is just and equitable that it should be.

17.3. Appointment of liquidator

Master must, in accordance with policy determined by Minister, appoint a suitable natural person as a liquidator as soon as practicable after the provisional order has been made or resolution has been registered. Master may decline to appoint a nominee if he wasn't properly nominated or is disqualified from being appointed. Any person aggrieved by Master's appointment or refusal to appoint may, within 7 days, request Master in writing to submit his reasons to Minster. Master may appoint a person as co-liquidator if he was nominated as such at first meeting of creditors and gives security to the satisfaction of Master for proper performance of his duties.

17.4. Impeachable dispositions

Provisions of the CA relating to unauthorised dispositions made after the commencement of winding-up and impeachable dispositions made before winding-up, apply *mutatis mutandis* to the winding-up of a CC that is unable to pay its debts.

17.5. Setting aside of payments to members

In the winding-up of a CC unable to pay its debts, members may be compelled to repay money which they received from the CC prior to liquidation.

(1) Payments by reason of membership

A member who received a payment by reason of his membership (eg a distribution of profit), within 2 years before commencement of the winding-up, must repay the amount concerned to the CC unless he can prove that:

- → after the payment was made, the CC's assets exceeded its liabilities;
- → the payment was made while the CC was able to pay its debts as they became due in the ordinary course of its business; and
- → payment, in particular circumstances, didn't in fact render CC unable to pay its debts.

(2) Salary or remuneration

A member may be required to return a salary or other remuneration paid to him within 2 years prior to commencement of winding-up. Master must consider the payment and if, in his opinion, it was not *bona fide* or reasonable in the circumstances, he must direct that it, or part of it which he may determine, be repaid by the member.

(3) Liquidator's duty to investigate personal liability of members

The liquidator has a duty to establish whether any member, former member is jointly and severally liable with the corporation for one or more debts.

17.6. Composition

At any time after commencement of liquidation of a CC unable to pay its debts, any person may submit a written offer of composition to liquidator. If liquidator considers that creditors will probably accept offer, he must send a copy of the offer, together with his report thereon and an explanation of the effect of the composition, to every known creditor and Master. If the liquidator considers that creditors are unlikely to accept the offer, or that he has insufficient information at his disposal to make a recommendation, he must inform offeror in writing that the offer is unacceptable and that he doesn't propose circulating it to the creditors. When circulating an offer of composition, the liquidator must notify creditors of the meeting at which the offer will be considered. Such a meeting may only be held once a final winding-up order has been made. Once accepted, the composition binds every person who had notice and was entitled to vote at the meeting, provided that:

- it was accepted by $^{2}/_{3}$ in number and value of creditors who proved claims against the CC;
- payment under the composition is made or secured as specified in the offer;
- the rights of secured or preferent creditors are not prejudiced unless in writing.

Composition may provide for winding-up to be set aside by court and, if so, the offeror may apply to court for the relevant order. He must, at least 3 weeks before application, advertise his intention in the Gazette and serve copies of application on Master, RCC and liquidator. Offeror's application may be opposed by a creditor or interested person on the goruns that:

- the composition unfairly harms the interests of the creditor;
- the meetings for considering the composition involved a material irregularity;
- insufficient or materially inacurate information about the composition was disclosed; or
- there is another ground which the court may deem sufficient.