



## **PART 4**

### **PROPOSALS FOR A UNIFIED INSOLVENCY ACT**

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In this part proposals will be made for the framework within which a unified insolvency statute can be developed.

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**PART 4A**

**THE CONCEPT OF A UNIFIED INSOLVENCY ACT**

<b>CHAPTER 5:</b>	<b>THE APPLICATION OF THE LAW OF INSOLVENCY TO THE WINDING-UP OF INSOLVENT COMPANIES AND CLOSE CORPORATIONS .....</b>	<b>131</b>
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In this part current winding-up law in South Africa will be discussed with particular reference to the problems contained in the “connecting provisions” in section 339 of the Companies Act and section 66 of the Close Corporations Act. Having reached the conclusion that a unified Insolvency Act is the solution to this problem, two further aspects relating to a unified insolvency statute are discussed, namely the definition of “debtor” and the treatment of specialised institutions in a unified Insolvency Act. A discussion of these aspects proves that the implementation of a unified Insolvency Act is both desirable and attainable.



## CHAPTER 5

### THE APPLICATION OF THE LAW OF INSOLVENCY TO THE WINDING-UP OF INSOLVENT COMPANIES AND CLOSE CORPORATIONS

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#### 1 INTRODUCTION

It has already been stated in this study<sup>1</sup> that the main Act that regulates insolvency law in South Africa is the Insolvency Act 24 of 1936.<sup>2</sup> It has also been shown how this came about, mainly because of the separate development of insolvency law as opposed to winding-up law, the latter always having been contained in separate legislation.<sup>3</sup> Insolvency law has shown immense growth

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<sup>1</sup> See ch 1.

<sup>2</sup> Hereinafter referred to as the Insolvency Act.

<sup>3</sup> It is interesting to note that although a hybrid of Roman-Dutch law and English law forms the basis of the South African insolvency law, and English law forms the basis of winding-up law, the “marriage” of the two systems has not yielded insurmountable problems in practice. This can also be attributed to the fact that English common law has a strong Roman law flavour.

over the past century, mirroring the growth in trade in industrialised nations. This has especially been the case in respect of international commerce, a community which South Africa recently rejoined. This growth has exposed South African insolvency law to be out of step with the rest of the industrialised world, and it has now become necessary to modernise our legislation.

The purpose of this chapter is to provide an exposition of the manner in which companies and close corporations are currently wound up under South African law. This is necessary in order to determine the need for a single insolvency statute in South Africa. In light of the fragmented nature of South African insolvency law, particular attention will be paid to:

- (a) The “connecting provisions” in section 339 of the Companies Act 61 of 1973<sup>4</sup> and section 66 of the Close Corporations Act 69 of 1984.<sup>5</sup> These provisions make the law of insolvency applicable to companies and close corporations that are unable to pay their debts, and require the law of insolvency to be applied where the Companies Act or Close Corporations Act does not contain a provision dealing with a specific matter. It will be shown that the root of the problems experienced with dual insolvency statutes in South Africa can, in the main, be attributed to these connecting provisions.<sup>6</sup>
- (b) Provisions contained in the Companies Act and Close Corporations Act that are similar to those contained in the Insolvency Act, and cross-referencing between Acts. Although section 339 of the Companies Act makes the law of insolvency applicable to companies that are being wound up and that are unable to pay their debts, the legislature thought it prudent to include in the Companies Act:

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<sup>4</sup> Hereinafter referred to as the Companies Act.

<sup>5</sup> Hereinafter referred to as the Close Corporations Act.

<sup>6</sup> However, it must be pointed out that these connecting provisions are necessary in light of the fact that the provisions relating to insolvency have not been duplicated in the Companies Act and the Close Corporations Act. England and Australia do not require these connecting provisions as the insolvency rules have been duplicated in the relevant legislation.

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- (i) Specific provisions relating to specific aspects, for example the appointment, powers and duties of liquidators<sup>7</sup> and provisions relating to interrogations;<sup>8</sup>
  - (ii) Specific references to sections of the Insolvency Act, in addition to the general connecting provision contained in section 339 of the Companies Act. Examples of these are the provisions relating to meetings<sup>9</sup> and the provisions relating to contribution by creditors;<sup>10</sup> and
  - (iii) Specific provisions that only apply to companies or close corporations. An example of this is to be found in section 419 of the Companies Act which provides for the dissolution of a company once it has been completely wound up.<sup>11</sup>

In regard to the problem identified in paragraph (a), it will be shown that the introduction of a unified insolvency statute will remove the current problems being experienced with the use of the connecting provisions in section 339 of the Companies Act and section 66 of the Close Corporations Act.

Likewise, the problems encountered in paragraph (b) will be analysed and it will be shown that the introduction of a unified statute will obviate the need for cross-referencing between Acts in addition to the general connecting provisions contained in section 339 of the Companies Act and section 66 of the Close Corporations Act. The possible manner in which the problems in paragraphs (a) and (b) can be addressed, will be discussed in the conclusion to this chapter.<sup>12</sup>

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<sup>7</sup> Ss 367 to 411 of the Companies Act.

<sup>8</sup> Ss 415 to 418 of the Companies Act.

<sup>9</sup> S 412 of the Companies Act.

<sup>10</sup> S 342(2) of the Companies Act.

<sup>11</sup> These unique provisions that relate only to corporate entities with legal personality will not be discussed here. However, these existing provisions that are found in the Companies Act and the Close Corporations Act have been included in the unified insolvency statute included as Annexure E to this study.

<sup>12</sup> In par 6 below.



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## 2 THE APPLICATION OF INSOLVENCY LAW TO THE WINDING-UP OF COMPANIES

Chapter XIV of the Companies Act, consisting of sections 337 to 426, provides for the winding-up of a company. Nearly all the provisions dealing with winding-up in the Companies Act relate to procedural aspects, with the substantive law of insolvency being regulated by the law of insolvency as contained in the Insolvency Act and the common law. Many of the provisions of the Companies Act deal with the alignment of the provisions of the Companies Act with those of the Insolvency Act,<sup>13</sup> some relate to the fundamental differences between natural and juristic persons, for example the dissolution of a company once the winding-up process has been completed<sup>14</sup> and others with the personal liability of directors in respect of fraudulent trading.<sup>15</sup>

However, the winding-up provisions of the Companies Act cannot on their own be applied in the total administration of an insolvent company. Instead of including the provisions of substantive insolvency law in the Companies Act,<sup>16</sup> the legislature saw fit to make the “law relating to insolvency” applicable also to the winding-up of companies. This was achieved by a general connecting provision that is contained in section 339 of the Companies Act. In addition to this general connecting provision, certain sections in the Companies Act make specific provisions of the Insolvency Act applicable also to companies that are being wound up and are unable to pay their debts.

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<sup>13</sup> Eg s 340 provides for the application of the Insolvency Act’s provisions dealing with impeachable transactions, and sets out the events in respect of the winding-up of a company that will correspond to the sequestration order in the case of individuals or partnerships.

<sup>14</sup> See s 419 of the Companies Act.

<sup>15</sup> See s 424 of the Companies Act.

<sup>16</sup> This is the position in Australia and England - see ch 4 above.

### 3 THE APPLICATION OF INSOLVENCY LAW TO THE WINDING-UP OF CLOSE CORPORATIONS

As in the case of the Companies Act, the Close Corporations Act also contains provisions relating to winding-up.<sup>17</sup> The Close Corporations Act contains considerably less provisions for winding-up than the Companies Act does, but there are nonetheless provisions which, again, are nearly identical to those contained in the Companies Act. Being a more recent Act, however, the Close Corporations Act does contain some innovations which are not to be found in either the Insolvency Act or the Companies Act.<sup>18</sup> The winding-up provisions in the Close Corporations Act are mainly procedural in nature, and make provision for the unique situation that a close corporation finds itself in under South African law.

In the same way that section 339 of the Companies Act makes the law of insolvency applicable to companies that are being wound up and that are unable to pay their debts, so too does section 66 of the Close Corporations Act apply in the case of a close corporation that is unable to pay its debts. Section 66 makes the Companies Act applicable to close corporations, which in turn makes section 339 of the Companies Act applicable. In other words, the law relating to insolvency will apply to a close corporation (that is unable to pay its debts) by virtue of section 339 of the Companies Act read with section 66 of the Close Corporations Act.

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<sup>17</sup> See part IX, ss 66 to 81 of the Close Corporations Act.

<sup>18</sup> Eg the Master may immediately upon the granting of a provisional winding-up order appoint a final liquidator (s 74 of the Close Corporations Act). This is not possible under the provisions of the Insolvency Act or the Companies Act.

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#### 4 THE APPLICATION OF INSOLVENCY LAW TO THE WINDING-UP OF SPECIALISED INSTITUTIONS

It has already been stated that there are various other pieces of specialised legislation that contain their own provisions in respect of winding-up.<sup>19</sup> The provisions contained in these Acts are mainly procedural in nature, and relate to the powers conferred on the governing bodies to intervene in winding-up proceedings, or to initiate such proceedings. The winding-up of these specialised institutions is dealt with in more detail in chapter 7 below.

#### 5 THE CONNECTING PROVISIONS IN SECTION 339 OF THE COMPANIES ACT AND SECTION 66 OF THE CLOSE CORPORATIONS ACT, DUPLICATION AND CROSS-REFERENCING

##### 5.1 Introduction

It is a well-accepted fact that the Insolvency Act is the central insolvency legislation in South Africa.<sup>20</sup> All other Acts which provide for winding-up, liquidation and the like, are ancillary to the Insolvency Act. In effect this means that the administration of insolvent estates takes place

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<sup>19</sup> See part VI of the Long Term Insurance Act 52 of 1998; part VI of the Short Term Insurance Act 53 of 1998; s 29 of the Pension Funds Act 24 of 1956; s 35 of the Friendly Societies Act 25 of 1956; s 18C of the Medical Schemes Act 72 of 1967; ss 27, 28 and 39 of the Unit Trusts Control Act 54 of 1981; ch X of the Co-Operatives Act 91 of 1981; s 33 of the Financial Markets Control Act 55 of 1989; s 68 of the Banks Act 94 of 1990; and ch VIII of the Mutual Banks Act 124 of 1993.

<sup>20</sup> See *Woodley v Guardian Assurance Co of SA Ltd* 1976 1 SA 758 (W). The Van Wyk de Vries Commission (*Kommissie van Ondersoek na die Maatskappywet (Hoofverslag RP 45/1970)* and (*Aanvullende Verslag en Konsepwetsontwerp RP 31/1972*) - hereinafter referred to as the Van Wyk de Vries Commission) stated it thus at ch XIX par 50.02(b): “Ons beskou die Insolvensiewet as die heersende Wet.”

under the provisions contained in the Insolvency Act, and that all other Acts which make provision for corporate insolvency are designed to slot into this process. However, the Insolvency Act only applies once winding-up has been effected under the separate legislation which governs such a corporation, for example the Companies Act or the Close Corporations Act.

In terms of the definition of “debtor” in the Insolvency Act,<sup>21</sup> only the estates of natural persons and partnerships may be sequestrated.<sup>22</sup> The liquidation of corporations, such as companies or other bodies corporate, is specifically excluded by the definition. This means that the procedure for bringing about a winding-up order is contained in separate legislation, such as the Companies Act or Close Corporations Act. Only once this procedure has been successfully implemented can the provisions of the Insolvency Act apply, and then not in all cases, as the enabling legislation often contains its own provisions in respect of certain procedures.<sup>23</sup>

## 5 2 Connecting provisions under earlier legislation

Section 339 has a brief but interesting history, and the provision itself has often been the subject of scrutiny by our courts. It is an interesting fact that section 339 has recently been considered judicially in a number of decisions.<sup>24</sup>

The Transvaal Companies Act 31 of 1909<sup>25</sup> was the first consolidated Act whereby the creation of a company with limited liability and its consequent winding-up were included in the same

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<sup>21</sup> See the definition of “debtor” in s 2 of the Insolvency Act.

<sup>22</sup> However, trusts, clubs and other associations of persons may also be sequestrated under the Insolvency Act - see *Magnum Financial Holdings (Pty) Ltd (in liquidation) v Summerly* 1984 1 SA 160 (W).

<sup>23</sup> Eg the Companies Act contains its own provisions for the appointment of liquidators, which are nearly identical to the provisions for the appointment of trustees in the Insolvency Act - see ss 367 to 385 of the Companies Act.

<sup>24</sup> These decisions are discussed in detail below.

<sup>25</sup> Hereinafter referred to as the 1909 Transvaal Companies Act.

Act.<sup>26</sup> Up to this time the provisions for the creation of a company with limited liability and its subsequent winding-up had been provided for in separate legislation.<sup>27</sup> This Act was the precursor to the Companies Act 46 of 1926,<sup>28</sup> and was the last pre-Union legislation dealing with company law and winding-up.

In this Act winding-up was dealt with in a separate chapter, namely Chapter IV.<sup>29</sup> This Act was modelled on the English Companies (Consolidation) Act of 1908.<sup>30</sup> The current Companies Act follows more or less the same division (into chapters) as the 1926 Companies Act.

In distinction to previous legislation, the 1909 Transvaal Companies Act was a lot clearer as regards the law that applied when winding-up companies that were insolvent. Section 180 of this Act provided as follows:

“180. In the winding-up of an insolvent company the same rules shall prevail and be observed with regard to the respective rights of secured and unsecured creditors and to debts provable and to the valuation of annuities and future and contingent liabilities as are in force for the time being under the law relating to insolvency, with respect to the estates of persons sequestrated; and all persons who in any such case would be entitled to prove for and receive dividends out of the assets of the company may come in under the winding-up, and make such claims against the company as they respectively are entitled to do by virtue of this section.”

In addition, section 183 provided as follows:

“183. In the case of a winding-up of any insolvent company, the provisions of the law for the time being relating to insolvency shall *mutatis mutandis* be applied in respect of any matter not specially provided for in this Act.”

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<sup>26</sup> See ch 3 above.

<sup>27</sup> See ch 3 above.

<sup>28</sup> Hereinafter referred to as the 1926 Companies Act.

<sup>29</sup> Ss 106-197.

<sup>30</sup> See De la Rey “Aspekte van die Vroeë Maatskappyereg: ‘n Vergelykende Oorsig (Slot)” 1986 *Codicillus* Vol 27 No 2 24.

This section was the precursor to the present section 339 of the Companies Act.<sup>31</sup> The applicable insolvency law at the time was Law 13 of 1895, which had repealed Ordinance 21 of 1880.<sup>32</sup> From court decisions at the time, it is evident that these connecting provisions created problems of interpretation. For example, in *Standard Bank v Liquidator of the B & C Syndicate Ltd*<sup>33</sup> the court had to decide whether the rules pertaining to liquidation and distribution accounts in insolvent estates, and especially the rules pertaining to contribution by creditors, also applied to a company in liquidation. In this case the court found it unnecessary to refer to the provisions of sections 180 and 183 of the 1909 Companies Act, finding its solution instead in the provisions of section 133 of that Act. Section 133 provided that a liquidator was obliged to draft the liquidation and distribution account in the same manner as a trustee in an insolvent estate. This case illustrates the fact that, despite the general provisions of sections 180 and 183, there were also other provisions dealing with specific issues; in this case the rules pertaining to the drafting of liquidation and distribution accounts.

Section 182 of the 1926 Companies Act provided for the law of insolvency to apply to the winding-up of companies that were unable to pay their debts:<sup>34</sup>

“182. Insolvency Law to be Applied Mutatis Mutandis. - In the case of every winding-up of a company unable to pay its debts the provisions of the law relating to insolvent estates shall, in so far as they are applicable, be applied *mutatis mutandis* in respect of any matter not specially provided for in this Act or the rules framed under section *two hundred and twenty*.”

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<sup>31</sup> However, the court still had the authority to confer on the liquidator certain powers - see *Provisional Liquidators of Edwards, Ltd v Goldstein and Engelstein* 1911 WLD 152. See also *Ex parte Liquidators of the De Deur Estates* (1908) TS 960; *Ex parte Grahamstown Brickmaking Co Ltd (in liquidation)* 17 EDC 75.

<sup>32</sup> See ch 3 above.

<sup>33</sup> 1918 TPD 470.

<sup>34</sup> For an early decision dealing with the application of this section in practice, see *Rivoy Investments (Pty) Ltd v Wemmer Trust (Pty) Ltd* 1939 WLD 151.

In *R v Schreuder*<sup>35</sup> and *R v RSI (Pty) Ltd*<sup>36</sup> the court found that a company could not be found guilty of contravening the provisions of the Insolvency Act by virtue of the connecting provision found in section 182 of the 1926 Companies Act. This problematic situation was well illustrated by the comments of Wynne J in the *RSI (Pty) Ltd* case at 416C-D:

“So far, however, as insolvency is concerned, the ‘nexus’ between the Companies Act and the Insolvency Act is to be found in two sections only of the Companies Act, viz sec 182 and sec 185 ... Sec 182 is an administrative section which applied the provisions of the law relating to insolvent estates *mutatis mutandis* to the winding-up of a company unable to pay its debts in respect of all matters not specially provided for in the Companies Act ... Nowhere in the Companies Act ... is any section to be found which renders the company itself liable for the commission of offences provided for in the Insolvency Act.”

The comment made at 29E of the *Schreuder* case is also apt:

“It seems to me, however, that sec 182 of the Companies Act, 1926, is merely administrative and does not incorporate into that Act the penal provisions of the Insolvency Act, 1936.”<sup>37</sup>

In both the above decisions the court found that section 182 was purely administrative.<sup>38</sup> However, in *S v Yousuf*<sup>39</sup> the court found that the directors of a company had been properly

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<sup>35</sup> 1957 4 SA 27 (O).

<sup>36</sup> 1959 1 SA 414 (E).

<sup>37</sup> See also *Cooper and Cooper v Ebrahim* 1959 4 SA 27 (T) where the court confirmed the approach taken by the court in the *Schreuder* case *supra*. Cf the decision of the court in *S v Gani* 1965 1 SA 222 (T) at 223D where the court reached the same conclusion that was reached in the *Schreuder*, *RSI (Pty) Ltd* and *Ebrahim* cases above, but did not refer to either. However, the court did refer to the Griqualand West decision of *R v City Silk Emporium (Pty) Ltd and Meer* 1950 1 SA 825 (GW), in deciding that s 182 of the 1926 Companies Act was merely administrative in nature. For other decisions dealing with the possible application and interpretation of s 182 of the 1926 Companies Act, see also *F & C Building Construction Co (Pty) Ltd v Macsheil Investments (Pty) Ltd* 1959 3 SA 841 (D) at 845F-G and *Parity Insurance Co Ltd (in liquidation) v Hill* 1967 2 SA 551 (A).

<sup>38</sup> In regard to s 182 only being administrative in nature, see also *Ex parte Mallac: In re de Marigny (Pty) Ltd (in liquidation): de Charmoy Estates (Pty) Ltd Intervening* 1960 2 SA 187 (N). However, the part of the *Mallac* case that dealt with the application of s 182 to leases and s 37 of the Insolvency Act, was overruled by the Appellate Division in *Durban City Council v Liquidator, Durban Icedromes Ltd* 1965 1 SA600 (A).

<sup>39</sup> 1965 3 SA 259 (T).

charged under section 134(1) of the Insolvency Act, but referred to the provisions of section 185<sup>40</sup> of the 1926 Companies Act and not section 182. This illustrates the difficulties encountered where there are additional connecting provisions in the Companies Act, such as section 185 that was found to be applicable in this case, other than the general connecting provision such as the one found in section 182.

However, the most important decision regarding section 182 of the 1926 Companies Act is undoubtedly to be found in *Woodley v Guardian Assurance Co of SA Ltd*<sup>41</sup> where Colman J made the following remark regarding this connection provision:

“I ... suggest that it is socially desirable that, as far as is practicable, all the consequences of the liquidation of an insolvent company should be similar to those [of] the insolvency of an individual ... The winding-up of a company unable to pay its debts is something closely akin to the winding-up of the estate of an insolvent individual. There are some different requirements which flow from the fundamental difference between a company and an individual: those are specifically provided for in the Companies Act. In respects other than those so provided for I cannot see why the Legislature should not have desired, not merely the procedural rules, but also the substantive rules and consequences, to be the same in both cases.”

From the above decisions it is evident that the court had in the past grappled with the connecting provisions contained in both the 1909 Transvaal Companies Act as well as similar provisions contained in the 1926 Companies Act.

### **5 3 The fragmentation of current South African insolvency law and the resultant connecting provisions**

#### *5 3 1 Introduction*

The fragmentation, or duality, of current South African insolvency law creates a number of interesting interpretational and practical problems. There are many facets to this fragmentation, ranging from the commencement of the insolvency proceeding to the duplication of provisions

<sup>40</sup> S 185 of the 1926 Companies Act made the criminal provisions relating to insolvency law also applicable to certain officers of a company.

<sup>41</sup> 1976 1 SA 758 (W).



in various Acts. Under this heading the problems caused by the current fragmentation of South African insolvency law will be discussed. Because many of these aspects overlap each other, it is necessary to first outline the various identifiable facets of the problems caused by the fragmentation of our insolvency law.

- (a) In the first place, there are currently different statutes that govern the commencement of the insolvency proceeding itself.
- (b) In the second place, there are numerous difficulties involved in determining which provisions that are contained in a variety of statutes, actually govern the winding-up process.
- (c) Thirdly, there may be different winding-up rules that apply to the same type of debtor due to the mode of winding-up that has been followed.
- (d) Fourthly, the fragmentation of our insolvency law may lead to different conclusions being reached in respect of similar disputes.<sup>42</sup>
- (e) Lastly, there are other statutes that are interpreted to override the provisions of the Insolvency Act.<sup>43</sup>

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<sup>42</sup> Reference can be made here to two decisions, namely *Klerk v SA Metal and Machinery Company (Pty) Ltd* [2001] 2 All SA 276 (E) and *Waste-Tech (Pty) Ltd v Van Zyl and Glanville* 2002 1 SA 841 (E). In both these cases the liquidators were compelled to provide security for litigation costs in terms of the provisions of the Companies Act and the Close Corporations Act. The point that needs to be made here is that these rules (regarding the provision of security) do not apply to trustees in estates that have been sequestrated in terms of the Insolvency Act, which results in different rules being applied to the same situation.

<sup>43</sup> An example of this is to be found in the provisions of the Sectional Titles Act 95 of 1986, where the arrear levies have to be paid before a sectional title unit can be transferred. In *Nel v Body Corporate of the Seaways Building* 1996 1 SA 131 (A) and *Barnard v Regspersoon van Aminie* 2001 3 SA 973 (SCA) the Appellate Division of the Supreme Court, as it was then known, and the Supreme Court of Appeal respectively found that the provisions of the Sectional Titles Act override the provisions of s 89 of the Insolvency Act, which provide for a limitation of two years in respect of the payment of arrear taxes out of the proceeds of the property. Consequently arrear levies have to be paid in full from the proceeds before

The ensuing discussion will concentrate on paragraphs (b) and (c) above, with only a brief reference to paragraph (a). However, the proposals made in this study must be seen against the background of the sum total of all these issues, as they are all symptomatic of the same thing, namely the fragmentation or duality of South African insolvency law.

### 5 3 2 *Different statutes governing the commencement of the insolvency proceeding*

Due to the fact that liquidation applications are dealt with separately under chapter 8 below, only a brief reference to this problem will be made here, and then only with reference to two specific cases that presented themselves recently.

The first case is *In re: Body Corporate of Caroline Court*<sup>44</sup> where the Supreme Court of Appeal had to decide whether the body corporate of a sectional title scheme could be wound up in terms of the provisions of the Sectional Titles Act 95 of 1986.<sup>45</sup> Without going into any detail,<sup>46</sup> the court dismissed the application brought in terms of section 48 of the Sectional Titles Act, but without really providing any answers to the questions that the court itself had raised. One of the problems in this case was the fact that section 36(5) of the Sectional Titles Act expressly excludes the application of the provisions of the Companies Act, meaning that the application could not be brought in terms of the provisions of the Companies Act. As a result of this decision one is left wondering how one should in fact go about winding-up the body corporate of a sectional title scheme, or if it is in fact possible.<sup>47</sup>

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a sectional title unit will issue a levy clearance certificate, effectively allowing the property to be transferred out of the insolvent estate.

<sup>44</sup> [2002] 1 All SA 49 (SCA).

<sup>45</sup> Hereinafter referred to as the Sectional Titles Act.

<sup>46</sup> The *Caroline Court* decision is discussed in detail in ch 6 below.

<sup>47</sup> It is submitted that this can in fact be done in a similar fashion as the method used by the premier of the Eastern Cape in *Sunny South Cannery (Pty) Ltd v Mbangxa* 2001 2 SA 49 (SCA), namely by listing the powers of the liquidators with specific reference to the provisions of the Companies Act.

The second case that is relevant here is the decision in *Fairleigh v Whitehead*<sup>48</sup> which dealt with the administration of an insolvent deceased estate in terms of section 34 of the Administration of Estates Act 66 of 1965.<sup>49</sup> Section 34 of the Administration of Estates Act provides for two possible alternative procedures, one being in terms of the Administration of Estates Act and the other in terms of the Insolvency Act.<sup>50</sup> The question that the court had to answer, was whether or not the informal procedure created in terms of section 34 of the Administration of Estates Act was one in terms of which the executor deals with an estate that has been sequestrated. Although the court answered this question in the affirmative, litigation could probably have been avoided if it were not for the fragmentation of our insolvency law.<sup>51</sup>

### 5.3.3 *The connecting provisions in current legislation, the duplication of provisions and cross-referencing between Acts*

With the promulgation of the current Companies Act, the wording of section 182 of the 1926 Companies Act was amended to the wording currently contained in section 339 of the Companies Act, which reads as follows:

“339. In the winding-up of a company unable to pay its debts the provisions of the law relating to insolvency shall, in so far as they are applicable, be applied *mutatis mutandis* in respect of any matter not specifically provided for by this Act.”

The Van Wyk de Vries Commission of Enquiry into the Companies Act was directly responsible for the promulgation of the 1973 Companies Act in its revised form, but the Commission's report itself does not shed much light on the reasons for the Commission changing the wording of this

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<sup>48</sup> 2001 2 SA 1197 (SCA).

<sup>49</sup> Hereinafter referred to as the Administration of Estates Act.

<sup>50</sup> See ch 10 below where this aspect is dealt with in detail.

<sup>51</sup> Despite the *Fairleigh* decision, this study proposes that the administration of insolvent deceased estates should remain in the provisions of the Administration of Estates Act - see ch 10 below.

section from its previous form in section 182 of the 1926 Act.<sup>52</sup> The only reference in the report that has any relevance, is the following statement made at paragraph 50.02 of the Main Report (*Hoofverslag*):

“50.02 Wat die algemene benadering van die Kommissie tot hierdie onderwerp betref, was ons gelei deur -

(a) ...

(b) die wenslikheid daarvan om die Maatskappywet met betrekking tot likwidasië te laat strook met die Insolvensiewet ten aansien van sowel beginsels as prosedure. Ons beskou die Insolvensiewet as die heersende Wet ...”

From this statement by the commission it is evident that the new wording contained in section 339 was designed to improve upon the previous connection provision contained in section 182 of the 1926 Companies Act, by making it clearer that both the principles and procedures relating to the law of insolvency should apply also to companies in winding-up. That the modification of the section was not entirely successful, is evident from the decisions that will be discussed below.

A matter that complicates the application of the “the law relating to insolvency” when applied to winding-up, is that in addition to the general connecting provision there are also specific provisions in the Companies Act that make specific provisions of the Insolvency Act applicable to companies being wound up. An example of this can be found in *Dally v Galaxie Melodies (Pty) Ltd*<sup>53</sup> where the court found that section 340(1)<sup>54</sup> renders the provisions of section 34 of the Insolvency Act applicable to the alienation by a company of its business.<sup>55</sup> Because section 340(1) makes specific provision for certain sections of the Insolvency Act to apply, it of course becomes

<sup>52</sup> See also De la Rey “Creditors’ Voluntary Liquidation: Theoretical Analysis and Practical Guide” 1980 *DJ* 47, where she agrees with the view that the Van Wyk de Vries Commission did not always provide explanations for the changes that they proposed.

<sup>53</sup> 1975 2 SA 337 (C).

<sup>54</sup> S 181(1) of the 1926 Companies Act.

<sup>55</sup> Cf *Scott-Hayward v Habibworths (Pty) Ltd* 1959 1 SA 202 (T); *Castleden v Volks Furniture Stores (Pty) Ltd* 1967 3 SA 733 (D); *Garzonis v Tokwe Ranches (Pvt) Ltd* 1969 1 SA 349 (R) dealing with similar cases under s 182 of the 1926 Companies Act.

unnecessary to apply section 339. However, such specific references to the provisions of the Insolvency Act create confusion as to why there are, in addition to section 339, sections of the Companies Act that find it necessary to make reference to specific sections of the Insolvency Act. The question that could be asked is why there is a general connecting provision *in addition to* the specific references to sections in the Insolvency Act.

One of the earliest problems encountered with the applicability of the provisions of the Insolvency Act to a company in liquidation by virtue of the provisions of section 339, can be found in *Herrigel v Bon Roads Construction Co (Pty) Ltd*.<sup>56</sup> In this case Lichtenberg J found that section 339 of the Companies Act did not envisage that the procedure and orders provided for in section 32 of the Insolvency Act<sup>57</sup> applied to a claim based on section 341 of the Companies Act.<sup>58</sup>

On the other hand, the court in *Hubert Davies Water Engineering (Pty) Ltd v The Body Corporate of "The Village"*<sup>59</sup> found that section 84(1)<sup>60</sup> of the Insolvency Act applied to companies in liquidation by virtue of the provisions of section 339 of the Companies Act. In *Venter v Avfin (Pty) Ltd*<sup>61</sup> the Supreme Court of Appeal had to determine whether sections 84 and 83 of the Insolvency Act also applied to close corporations in liquidation, by virtue of the provision of sections 66 of the Close Corporations Act read with section 339 of the Companies Act. In finding that the provisions do apply, the court referred to the *Hubert Davies* decision with

<sup>56</sup> 1980 4 SA 669 (SWA). See also *Trakman v Livschitz: In re Livschitz v Trakman* 1996 2 SA 384 (W) which dealt with security for costs where a liquidator commences proceedings to set aside impeachable dispositions in terms of the Insolvency Act.

<sup>57</sup> S 32 of the Insolvency Act deals with proceedings to set aside improper dispositions.

<sup>58</sup> S 341 of the Companies Act deals with dispositions and share transfers that are void if made after winding-up.

<sup>59</sup> 1981 3 SA 97 (D).

<sup>60</sup> S 84(1) deals with the effect of insolvency on instalment sale transactions.

<sup>61</sup> 1996 1 SA 826 (A) (also reported under [1996] 1 All SA 173 (A)).

approval.<sup>62</sup> However, in another case dealing with section 84(1) of the Insolvency Act and its application to the winding-up of a close corporation by virtue of the provisions of section 66 of the Close Corporations Act read with section 339 of the Companies Act, there is an interesting twist when applying the provisions of section 339. In *ABSA Bank Ltd v Cooper*<sup>63</sup> it was contended that before section 339 of the Companies Act could be applied, the inability of the corporation to pay its debts had to be determined. It was further contended that the relevant stage for determining such inability was the time at which the section was invoked. It was also contended that the inability to pay debts did not only involve a consideration of commercial insolvency, but reference to all the corporation's assets and liabilities. In its decision the court found, *inter alia*, that the time to determine whether the corporation was unable to pay its debts, and therefore to answer the question as to whether section 339 did in fact find application, was at the time the section was invoked. The court also found that mere commercial insolvency was not sufficient, holding that the inability of a corporation to pay its debts had to be measured in the context of its winding-up, that is in a weighing-up of its assets and liabilities. Without considering the correctness of the *ABSA Bank* case, or for that matter any of the cases dealing with the connecting provisions, it is evident that section 339 of the Companies Act and section 66 of the Close Corporations Act<sup>64</sup> cause various interpretational difficulties.

<sup>62</sup> Cf *Morgan v Wessels* 1990 3 SA 57 (O); *Van Zyl v Bolton* 1994 4 SA 648 (C); *UDC Bank Ltd v Seacat Leasing and Finance Co (Pty) Ltd* 1979 4 SA 682 (T), the latter of which was not followed in the *Venter* case. See also *Avfin Industrial Finance (Pty) Ltd v Interjet Maintenance (Pty) Ltd* 1997 1 SA 807 (T) which was decided before the *Venter* case.

<sup>63</sup> 2001 4 SA 876 (T). It should be noted that the court in *Taylor and Steyn v Koekemoer* 1982 1 SA 374 (T) had already pointed out that the time to determine whether or not the company or corporation was unable to pay its debts, is the time at which the section is invoked.

<sup>64</sup> There are many examples of where s 66 of the Close Corporations Act has been applied, often creating huge interpretational problems: *Spendiff v JAJ Distributors (Pty) Ltd* 1989 4 SA 126 (C) 135; *Du Plessis v Oosthuizen* 1995 3 SA 604 (O); *Syfrets Bank Ltd v Sheriff of the Supreme Court, Durban Central; Schoerie v Syfrets Bank Ltd* 1997 1 SA 764 (D); *Nathaniël & Efthymakis Properties v Hartebeestpruit Landgoed CC* [1996] 2 All SA 317 (T); *Townsend v Barlows Tractor Co (Pty) Ltd* 1995 1 SA 159 (W) and *Barlows Tractor Co (Pty) Ltd v Townsend* 1996 2 SA 869 (A) 881.

The words *mutatis mutandis* that appear in section 339 of the Companies Act came to be interpreted by the court in *Smith v Mann*.<sup>65</sup> Although the case dealt with a section 311 compromise in terms of the Companies Act, the question that had to be answered was whether the provisions of sections 130<sup>66</sup> and 141<sup>67</sup> of the Insolvency Act found application by virtue of section 339 of the Companies Act. Flemming J (as he then was) discussed the meaning of *mutatis mutandis* in section 339 as follows:<sup>68</sup>

“Section 339 does not create a power on the part of the court to apply a law passed for certain circumstances to other circumstances. It purports to carry the limits of the applicability which it prescribes in itself. Concededly, the applicability ‘*mutatis mutandis*’ is not capable of firm delineation. The provisions which become applicable may range over a wide field or a narrow one. The ‘changes’ in wording to adjust to the exotic circumstances may be minor or major. What remains constant is that no leeway is created to decide rather than to conclude that a statute which according to its own terms is not applicable to the present situation, should apply to a different situation. It can only follow if the Legislature, even be it in general terms, has so decreed.”

In *Bryant & Flanagan (Pty) Ltd v Muller*<sup>69</sup> the Appellate Division found that a liquidator, as in the case of a trustee, was vested with a discretion to abide by or terminate an executory contract not specifically provided for in the Insolvency Act. The common law being applicable in such a case, the court found that the liquidator was vested with the same rights as a trustee under the common law by virtue of section 339 of the Companies Act.

One of the most important cases dealing with the applicability of insolvency law to the winding-up of a company by virtue of section 339 of the Companies Act, is *Kalil v Decotex (Pty) Ltd*.<sup>70</sup>

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<sup>65</sup> 1984 1 SA 719 (W).

<sup>66</sup> S 130 of the Insolvency Act deals with illegal inducements to vote for a composition, or not to oppose the rehabilitation of a debtor.

<sup>67</sup> S 141 of the Insolvency Act deals with the consequences of the acceptance of consideration for certain illegal acts or omissions.

<sup>68</sup> At 722C-E. See also *SA Fabrics v Millman* 1972 4 SA 592 (A) 600 where the Appellate Division held that *mutatis mutandis* means with the *necessary* alterations.

<sup>69</sup> 1978 2 SA 807 (A).

<sup>70</sup> 1988 1 SA 943 (A).

In this decision of the Appellate Division<sup>71</sup> the words “in the winding-up of a company” that are used in section 339, were interpreted by the court to refer to the *process of liquidation* that commences *once an order of winding-up has been granted*. The court found that the provisions of section 339 do not apply to proceedings giving rise to a liquidation order or the refusal thereof. In this specific case the provisions of section 150 of the Insolvency Act<sup>72</sup> were found not to apply to a company where the court had refused to grant a provisional winding-up order. The court referred with approval to the decision in *Lawclaims (Pty) Ltd v Rea Shipping Co SA: Schiffcommerz Aussenhandelsbetrieb Der VVB Schiffsbau Intervening*<sup>73</sup> where it was stated that section 339 only applies in the winding-up of a company, that stage only being reached when an order to wind up a company has been made in terms of the Companies Act.<sup>74</sup>

In *Choice Holdings Ltd v Yabeng Investment Holding Co Ltd*<sup>75</sup> the court also had to decide whether or not section 150 of the Insolvency Act would apply to a company by virtue of section 339 of the Companies Act, where the directors of a company had appealed against the granting of a liquidation order by the court. The court found that section 150(3) of the Insolvency Act did in fact apply, allowing the winding-up process of the company to continue despite the pending appeal.<sup>76</sup> This case can be distinguished from the *Kalil* decision in that the *Choice Holdings* case dealt with a liquidation order that had in fact been granted, allowing the provisions of section 339 of the Companies Act to apply. In the *Kalil* case the court had refused to grant a liquidation order and, due to the fact that the company was not in liquidation, section 339, and consequently

<sup>71</sup> As it was then known. The name of this court has since been changed to the Supreme Court of Appeal.

<sup>72</sup> S 150 of the Insolvency Act deals with appeals.

<sup>73</sup> 1979 4 SA 745 (N).

<sup>74</sup> 750B-C of the *Lawclaims* case, *supra*.

<sup>75</sup> 2001 2 SA 768 (W).

<sup>76</sup> It was contended by the applicants that r 49(11) of the Uniform Rules of Court applied, having as a result that the appeal stayed all proceedings, including the winding-up process, relating to the company. S 150(3) of the Insolvency Act, on the other hand, provides that the administration process of an insolvent estate is not stayed, but continues subject to certain provisos relating to the sale of property.



section 150(3) of the Insolvency Act, could not be applied.<sup>77</sup>

There are three cases that highlight the difficulties encountered where the Companies Act does in fact contain a provision relating to the problem at hand, begging the question as to whether or not the Insolvency Act's provisions should apply by virtue of the provisions of section 339 of the Companies Act. The first case is *Townsend v Barlows Tractor Co (Pty) Ltd*,<sup>78</sup> where the court held that the proviso to section 104(1)<sup>79</sup> of the Insolvency Act could find no application to a company in liquidation, despite the provisions of section 339 of the Companies Act. In arriving at his conclusion Cloete J expressed himself as follows:<sup>80</sup>

“I find no room for the operation of the proviso in s 104(1) of the Insolvency Act to liquidations of companies or close corporations. The omission of such a proviso from s 366(2) of the Companies Act of 1973 ... is in my view inconsistent with an intention on the part of the Legislature that such a proviso would be applicable in the case of liquidations. The Companies Act having in s 366(2) dealt with the consequences of late proof of claims, there is no room for the proviso in s 104 of the Insolvency Act to be incorporated under the general provisions of s 339 of the Companies Act.”

<sup>77</sup> However, an appeal against a liquidation order must be distinguished from an application to have the proceedings relating to the winding-up of a company set aside completely. In this regard see the decision of the court in *Storti v Nugent* 2001 3 SA 783 (W), where the court gave a detailed historical account of s 354 of the Companies Act. S 339 is also referred to in this case, although no direct decision regarding its operation was made. See also *Ward v Smit: In re Gurr v Zambia Airways Corporation Ltd* 1998 3 SA 175 (SCA).

<sup>78</sup> 1995 1 SA 159 (W).

<sup>79</sup> This provision deals with the late proof of claims. In *Swaanswyk Investments (Pty) Ltd v The Master* 1978 2 SA 267 (C) it was held that the proof of creditors' claims must be both procedurally and substantively the same as in the case of insolvency. However, in regard to the possible application of s 45 of the Insolvency Act to a company being wound up under the provisions of the 1926 Companies Act, and the application of s 182 of that Act, see *Wynn and Godlonton v Mitchell* 1973 1 SA 283 (E).

<sup>80</sup> At 165C-D.

The other two cases are *Syffrets Bank Ltd v Sheriff of the Supreme Court, Durban Central* and *Schoerie v Syffrets Bank Ltd*,<sup>81</sup> where the court held that section 20 of the Insolvency Act<sup>82</sup> was not one of the provisions that applied to a company or close corporation in liquidation by virtue of the provisions of section 339 of the Companies Act.<sup>83</sup> The court arrived at this conclusion because of the fact that section 361(1) of the Companies Act specifically provides for the assets of a company to be deemed to be under the custody and control of first the Master and then the liquidator.

In *National Union of Leather Workers v Barnard and Perry*<sup>84</sup> the Labour Appeal Court, per Davis AJA, found that section 38 of the Insolvency Act<sup>85</sup> applied to a company that was wound up voluntarily as a voluntary winding-up by creditors, by virtue of the provisions of section 339 of the Companies Act. This in turn led the court to rule that the decision to wind up the company by passing a special resolution amounted to an act by the employer in bringing the contract of employment to an end in a manner recognised by law, and therefore amounting to a dismissal in terms of section 186(a) of the Labour Relations Act 66 of 1995. Once again this case illustrates the tremendous impact that section 339 can have when applying the principles of insolvency to companies that are being wound up.

In addition to the sections and case law that have been discussed above, the Companies Act also contains an interesting hybrid of provisions from the Insolvency Act and additional provisions

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<sup>81</sup> 1997 1 SA 764 (D). These cases were decided simultaneously.

<sup>82</sup> S 20 deals with the vesting of estate property in the Master and the trustee in the case of sequestration.

<sup>83</sup> Cf *Pols v R Pols - Bouers en Ingenieurs (Edms) Bpk* 1953 3 SA 107 (T) at 111G-H and *Secretary for Customs and Excise v Millman* 1975 3 SA 544 (A) at 552F-H.

<sup>84</sup> 2001 4 SA 1261 (LAC).

<sup>85</sup> S 38 of the Insolvency Act deals with the termination of service contracts upon the sequestration (or liquidation) of the employer.

contained in the Companies Act. Although many of these provisions do not create many problems in practice, they nevertheless unnecessarily complicate the administration of companies that are being wound up.

Section 340 of the Companies Act makes the provisions relating to impeachable dispositions in the Insolvency Act applicable also to companies that are being wound up and that are unable to pay their debts. Many of the problems associated with this section, especially in regard to the application of section 34 of the Insolvency Act, have already been discussed above.

Despite the connecting provision contained in section 339 of the Companies Act, section 342 provides that the rules relating to the application of a company's assets and the costs of winding-up must be applied in the same way as they would be in the case of a sequestrated estate. Section 342 reads as follows:

“342. Application of assets and costs of winding-up. - (1) In every winding-up of a company the assets shall be applied in payment of the costs, charges and expenses incurred in the winding-up and, subject to the provisions of sections 435(1)(b), the claims of creditors as nearly as possible as they would be applied in payment of the costs of sequestration and the claims of creditors under the law relating to insolvency and, unless the memorandum or articles otherwise provide, shall be distributed among the members according to their rights and interests in the company.

(2) The provisions of the law relating to insolvency in respect of contributions by creditors towards any costs shall apply to every winding-up of a company.”

The practical effect of this section is that the rules pertaining to the sale of assets and the subsequent application of the proceeds in the payment of administration expenses and claims, are the same as would be the case in the estate of an individual. This necessarily entails the application of various sections of the Insolvency Act. For example, if the asset is subject to the

rights of a secured creditor then sections 2,<sup>86</sup> 83,<sup>87</sup> 89<sup>88</sup> and 95<sup>89</sup> of the Insolvency Act will find application to the proceeds of such an asset.

However, the greatest irony contained in the application of section 342 of the Companies Act, lies in the application of the proceeds of free residue assets to the claims of statutory preferent creditors.<sup>90</sup> Although the preferences for which provision is made in sections 96 to 102 of the Insolvency Act do find application in the case of a partnership, and may in fact apply to the estate of an individual, they more often find application in the case of companies and partnerships. For example, section 98A of the Insolvency Act provides for the payment of arrear salaries and other employee claims to be paid as a preference out of the free residue assets. These claims will of course arise in the case of partnerships, hardly ever in the estate of an individual, but most often in the case of a company or close corporation. It is submitted that it would have been more sensible for provisions of this nature to be included in the winding-up provisions of the Companies Act and Close Corporations Act. In addition to section 98A, section 38 of the Insolvency Act provides for the termination of contracts of employment where the employer's estate is sequestrated. These provisions would also be better suited to companies and corporations that are being wound up, even though the provisions would find application in the case of a partnership being sequestrated in terms of the provisions of the Insolvency Act. The same principle applies to claims by the South African Revenue Service for value-added tax in terms of section 99 of the Insolvency Act.

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<sup>86</sup> Definition of "security" and "preference".

<sup>87</sup> This section deals with the sale of an asset that is subject to the secured rights of creditors.

<sup>88</sup> This section deals with the costs that must be paid from the proceeds of a security before the creditor becomes entitled to the balance of the proceeds.

<sup>89</sup> This section deals with the distribution of the balance of the proceeds of a security once the costs referred to in s 89 have been paid.

<sup>90</sup> For a comprehensive discussion of statutory preferences in corporate insolvency in South Africa and the United Kingdom, see Keay, Borraine and Burdette "Statutory Preferences in Corporate Insolvency: A Comparative Analysis" 2001 *International Insolvency Review* 1.

The Companies Act also contains some specific references to the Insolvency Act relating to the convening of meetings,<sup>91</sup> voting at meetings<sup>92</sup> and interrogations.<sup>93</sup> Although the provisions in the Insolvency Act relating to the convening of meetings and voting at meetings do not appear to create any practical problems, the application of section 65, and other sections relating to interrogations held under the provisions of the Insolvency Act, do appear to have raised some questions. The problem with section 416 of the Companies Act referring to the provisions of section 65 of the Insolvency Act, is the question whether all the provisions of this section must be applied or only aspects thereof. Henochsberg<sup>94</sup> states the following in regard to the scope of application of section 65 of the Insolvency Act to section 415 interrogations under the Companies Act:

“As to the provisions of s 65 of the Insolvency Act, which apply in relation to the interrogation of a witness under s 415, see the General Note on s 415. Apart from these provisions, it is submitted that, in view of the fact that effectively all the matters for which s 65 of the Insolvency Act provides are *mutatis mutandis* already provided for by s 415, there is in fact no scope for the application of s 65 in the winding-up (s 339).”

However, in *Vize v Wilmans*<sup>95</sup> the court did in fact find that the provisions of sections 64 and 65 of the Insolvency Act are applicable to a company in liquidation by virtue of section 339 of the Companies Act. It is submitted that this decision is clearly incorrect as the provisions find application by virtue of section 416 of the Companies Act.<sup>96</sup> From this it is evident that the extent

<sup>91</sup> Ss 364(2) and 412(1)(a) of the Companies Act refers to the manner in which meetings must be convened. It is not clear why it was considered necessary to make provision for the convening of meetings in both these sections.

<sup>92</sup> S 365(2)(a) of the Companies Act.

<sup>93</sup> S 416 of the Companies Act.

<sup>94</sup> Kunst (gen ed) *Meskin, Henochsberg on the Companies Act* (1994) 883 (hereinafter referred to as Henochsberg).

<sup>95</sup> 2001 4 SA 1114 (NC).

<sup>96</sup> One may pose the question as to whether it makes any difference whether the provisions of ss 64 and 65 of the Insolvency Act are made applicable by virtue of s 339 or s 416. However, the wording of ss 339 and 416 are not identical: in s 339 the words used are “in the winding-up of a company unable to pay its debts”, while the wording used in s 416 refers to a company “which is being wound up and is unable to

of application of these fragmented provisions is not always clear. This creates confusion and uncertainty, something that could be prevented by having uniform provisions in a unified insolvency statute.

Other sections of the Companies Act that refer to the provisions or application of the Insolvency Act are sections 386(1)(e),<sup>97</sup> 386(4)(g)<sup>98</sup> and 425.<sup>99</sup> Since no real practical problems have been experienced with these provisions in the past, they will not be discussed here.

The final aspect that needs to be discussed here is the term that effectively makes the law of insolvency applicable to winding-up, namely the term “unable to pay debts”. If one looks at the various provisions of the Insolvency Act that apply to companies and close corporations in liquidation, it is evident that the legislature only wanted the provisions to apply in cases where the company was insolvent and, consequently, wanted to protect the interests of creditors. Because the winding-up provisions in the Companies and Close Corporations Act also regulate the winding-up process of solvent companies, it was necessary to make a distinction that could determine to which companies and corporations the law of insolvency must be applied. The term “unable to pay debts” has been problematic in a number of respects, but especially in regard to

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pay its debts”. In the *Vize* case the court found that the difference in wording between ss 339 and 416 did not amount to anything substantial. Although these phrases seem to imply the same thing, it was argued in *Hudson v The Master* 2002 1 SA 862 (T), that they do not have the same meaning. Although the court rejected this argument, another court may well have come to a different conclusion.

<sup>97</sup> This section deals with general powers and duties of liquidators.

<sup>98</sup> This section deals with the liquidator’s powers in regard to contracts for the purchase of immovable property (s 35 of the Insolvency Act) and a liquidator’s powers in regard to contracts of lease (s 37 of the Insolvency Act).

<sup>99</sup> This section provides for the application of the criminal provisions relating to the law of insolvency. Parts of this aspect have been discussed above under the discussion of s 339 of the Companies Act.

the time at which this inability must be determined.<sup>100</sup> Whether this inability to pay debts is based on factual or commercial insolvency has also become a bone of contention.<sup>101</sup>

Then there are also provisions that do not refer to an inability to pay debts, but instead refer to a court order, in circumstances where it is clear that the legislature intended that the provisions should also apply to the winding-up of such a company. One such provision is contained in section 417 of the Companies Act which deals with interrogations. Section 417 states that “[i]n any winding-up of a company unable to pay its debts, the Master or the Court may, at any time after a *winding-up order* has been made ...” summon any director or other officer in order that they may provide information. In *Janse van Rensburg v Master of the High Court*<sup>102</sup> the court held that the provisions of section 417 of the Companies Act do not apply to a company that has been wound up as a voluntary winding-up by creditors. The court arrived at this conclusion due to the wording of the section requiring a court order to have been issued before the provisions will apply. This was decided despite the words “in any winding-up of a company unable to pay its debts”. It is submitted that it was the intention of the legislature for these provisions to apply to insolvent companies irrespective of the mode of winding-up, as one of the main aims of an interrogation is to recover assets for the benefit of the creditors. Due to the manner in which the provision has been drafted, the court found that it does not apply to a voluntary winding-up. With respect, it is illogical to conclude that an interrogation cannot apply merely because the section refers to a “winding-up order”. However, the *Janse van Rensburg* and *South African Phillips* cases do illustrate the difficulties that are involved when the court has to interpret the content of sections in order to determine their applicability in the case of insolvency.

<sup>100</sup> See eg *Taylor and Steyn v Koekemoer* 1982 1 SA 374 (T) where it was held that the time by reference to which it must be determined whether the company is in fact unable to pay its debts, is the time when it is sought to invoke such section. See also *ABSA Bank Ltd v Cooper* 2001 4 SA 876 (T), *Vize v Wilmans* 2001 4 SA 1114 (NC) and *Hudson v The Master* 2002 1 SA 862 (T), where this approach was also followed.

<sup>101</sup> *ABSA Bank Ltd v Cooper* 2001 4 SA 876 (T). See also *Hudson v The Master* 2002 1 SA 862 (T), where the court indicated that the liquidator must have regard to both liquidated and unliquidated claims.

<sup>102</sup> 2001 3 SA 519 (W) (also reported under [2001] 2 All SA 551 (W)). See also *South African Phillips (Pty) Ltd v The Master* 2000 2 SA 841 (W) where the court gave the same interpretation to s 417 as was the case in the *Janse van Rensburg* case.

## 6 CONCLUSION

From the above exposition of the cases dealing with the interpretation of section 339 of the Companies Act and section 66 of the Close Corporations Act, it is clear that the connecting provisions contained in these sections are, to say the least, problematic. While there is no doubt that the current system of winding-up companies and close corporations is workable, it is obvious that the dual system of insolvency employed in South Africa creates substantial problems. It is submitted that the problems underlying the shortcomings of the present system are twofold:

- (a) In the first place section 339 of the Companies Act and section 66 of the Close Corporations Act create unnecessary problems of interpretation when trying to apply the law of insolvency to the winding up of companies and close corporations. This was illustrated with reference to the court judgments in the preceding paragraph.
- (b) In the second place, and this aspect is related to the first, the fact that both the Companies Act and the Close Corporations Act contain provisions relating to winding-up in addition to the connecting provisions contained in section 339 of the Companies Act and section 66 of the Close Corporations Act, creates confusion. In other words, one cannot merely refer to the law relating to insolvency by virtue of the provisions of sections 339 and 66 - one first has to consult the provisions of the Companies Act or Close Corporations Act in order to determine whether or not there is not already a provision dealing with the subject. If there is a provision in the Companies Act or Close Corporations Act, the further question arises as to what extent, if any, similar or any provisions of the Insolvency Act will also find application.<sup>103</sup>

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<sup>103</sup> Other specific aspects of this problem are dealt with in part 4B below.



While the winding-up provisions of the Companies Act and the Close Corporations Act are admittedly not flawed to the extent that it has become impossible to wind up companies and close corporations with expedience and effectiveness, it is submitted that some very important aspects deserve consideration:

- (a) If one looks at the number of decisions that have been discussed in this chapter that deal with the interpretational problems encountered with sections 339 and 66,<sup>104</sup> it is apparent that these connecting provisions have caused a plethora of expensive litigation, a fact that can only be to the detriment of creditors who have in any event suffered financial loss due to the financial failure of the company or corporation.
- (b) In addition to the expense involved in litigation, one of the main aims of insolvency law is to ensure the speedy administration of insolvent estates, thereby allowing the creditors that have suffered losses to be paid expediently. Litigation involving the interpretation of these provisions is a lengthy and time-consuming process, which is in direct conflict with one of the most important and entrenched principles of our insolvency law.
- (c) The last aspect that plays a role here, is the confusion that is created by the use of a dual system. The fact that there has been so much litigation regarding the abovementioned provisions clearly illustrates the uncertainty surrounding the application of the various Acts, something one would assume sections 339 and 66 was intended to avoid.

Having identified what is believed to be the underlying problems surrounding the application of a dual system of insolvency, the question now is how one could possibly effectively address this shortcoming. It is submitted that there are two possible manners in which this problem can be addressed:

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<sup>104</sup> This was merely a selection of cases and does not include all the reported and unreported decisions.

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- (a) The first (and, it is submitted, the best) manner in which this problem can be addressed is by the introduction of a unified insolvency statute. If all the provisions relating to insolvency were contained in one Act none of the interpretational problems that have been discussed above would have arisen. One Act implies one set of rules applicable to all (insolvent) debtors, with exceptions to some rules being clearly spelt out in the relevant provisions.<sup>105</sup>
- (b) The second manner in which this problem can be addressed is by repeating all the provisions relating to insolvency in the relevant Acts dealing with winding-up. For example, all the provisions relating to insolvency that apply to companies can be included in the relevant chapter of the Companies Act. In this way it becomes unnecessary to refer to other Acts in order to achieve the desired effect. This is the *modus operandi* in England and Australia<sup>106</sup> and, while not the most desirable solution, seems to work reasonably well.<sup>107</sup>

For the following reasons the option set out in paragraph (b) above is, in my opinion, not a viable one:

- (a) In the first place, amendments will be complicated if the relevant provisions are scattered amongst a number of Acts. For example, an amendment to a relevant provision of the Insolvency Act will necessitate an amendment to the same or similar provision of the Companies Act and the Close Corporations Act. Since the relevant legislation does not

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<sup>105</sup> This study proposes one Insolvency Act that can apply to all debtors - see ann E.

<sup>106</sup> See ch 4 above.

<sup>107</sup> However well this system may appear to work in practice, there are some problems that can be associated with this system as well. For example, duplicating the provisions in various Acts, or even in the same Act but under separate chapters, can cause problems when amending the such legislation. Another possible problem that can arise is where the courts give differing interpretations to the same principles that are contained in different Acts. For this reason it would be preferable to have only one Act with one set of principles that apply to all debtors; consequently the introduction a unified Insolvency Act is preferable to duplicating all the insolvency provisions in the various Acts.

fall under the auspices of a single ministry,<sup>108</sup> it will require the co-operation of a number of government departments in order to bring about the amendments in question.

- (b) In the second place the duplication of clauses in various Acts opens up the possibility that the courts may attach differing interpretations to what is in essence the same provision. Although one would assume that the courts would be consistent, the mere fact that the provision on the one hand refers to an individual, and on the other to a company or corporation, may contribute towards the court interpreting the provision in a different manner.

Consequently it is submitted that the creation of a single insolvency statute would be the better option. In addition to removing unnecessary duplication and the need to interpret identical provisions in different Acts, a single statute is also relatively simple to amend should the need arise. It is also good administration to have a single statute, since it can be used to promote the uniformity and harmonisation of insolvency as a legal discipline, and does not create confusion for the persons that are required to apply it in practice.

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<sup>108</sup> The Insolvency Act falls under the auspices of the Department of Justice and Constitutional Development, while the Companies Act and the Close Corporations Act fall under the auspices of the Department of Trade and Industry.

## CHAPTER 6

### DEFINING “DEBTOR” FOR THE PURPOSES OF A UNIFIED INSOLVENCY ACT<sup>1</sup>

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#### SUMMARY

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#### 1 INTRODUCTION

Having determined in the previous chapter that a unified or a single insolvency statute should address the problems experienced with a dual system of insolvency law, the first aspect that will have to be addressed is the drafting of the unified statute in such a way as to make it applicable to all types of debtors. In doing so the definition of “debtor” plays a crucial role. Boraine and Van der Linde<sup>2</sup> point out that a correct and exact definition of “debtor” is one of the key issues

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<sup>1</sup> In this Chapter frequent reference is made to the transcriptions of a symposium held on 23 Oct 1998, transcriptions of workshops held from 7 to 10 Dec 1998 and transcriptions of a conference held on 6 Oct 1999. The symposium, workshops and conference were used in order to obtain input from the insolvency profession as to the content and technical workings of a unified insolvency statute. In this study the transcriptions will be referred to as the Symposium Transcriptions (*Final Report Containing Proposals on a Unified Insolvency Act Vol 2*), Workshop Transcriptions (*Final Report Containing Proposals on a Unified Insolvency Act Vol 2*) and Conference Transcriptions (*Final Report Containing Proposals on a Unified Insolvency Act Vol 4*) respectively. A copy of the above documents are available for perusal in the Merensky Library, University of Pretoria.

<sup>2</sup> “The Draft Insolvency Bill - an Exploration (Part 1)” 1998 4 *TSAR* 621 at 626 (hereinafter referred to as Boraine and Van der Linde (Part 1)).

in the review of our insolvency law. Keay<sup>3</sup> confirms this viewpoint and states that the key here is to find a way of defining “debtor” without being clumsy and long-winded in the drafting of the provisions.<sup>4</sup>

Formulating a definition of “debtor” for the purposes of a unified insolvency statute requires a dual approach. In the first place the definition of “debtor” will be examined in relation to individuals and partnerships regarding the concept of “sequestration”. This also entails a deliberation of the definition of “debtor” after the introduction of company law in South Africa, and the resultant exclusion of companies from such a definition in the various Insolvency Acts. It will be pointed out that the current definition of “debtor” in the Insolvency Act 24 of 1936<sup>5</sup> evolved due to the separate treatment of natural persons and juristic persons under South African insolvency law. In the second place the definition of “debtor” will be examined with a view to a unified insolvency statute, which by its very definition requires an all-encompassing approach that will include both natural and juristic persons.

## 2 HISTORICAL DEVELOPMENT

Prior to the concept of separate legal personality being introduced into South Africa in the late nineteenth century, the law of insolvency only applied to the estates of individuals and partnerships. For this reason it is unnecessary to research the old ordinances in order to determine how a debtor was defined prior to this time. What is important, however, is the definition of “debtor” at the time legal personality had already become entrenched in our law.

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<sup>3</sup> “To Unify or not to Unify Insolvency Legislation: International Experience and the Latest South African Proposals” 1999 *DJ* 62-79 (hereinafter referred to as Keay “To Unify or not to Unify”).

<sup>4</sup> The first attempt at defining “debtor” for the purposes of unified legislation, was submitted at the symposium held on 23 Oct 1998. It was, to say the least, clumsy and awkward. In response to the suggestion made by Keay in his paper, the definition was substantially amended and proved to be simple to use in the proposals contained in the Final Report. In consequence of further suggestions made at the conference on 6 Oct 1999, the definition was refined even further.

<sup>5</sup> Hereinafter referred to as the Insolvency Act.

For example, the Transvaal Law 13 of 1895 did not contain any definitions, and therefore no definition of “debtor” as it applied at the time can be found in this Act. Although Law 13 of 1895 did not expressly exclude companies from its operation, it is evident from sections 1 and 2 that it only applied to individuals and partnerships. The relevant sections provided as follows:

- “1. Any person who shall be desirous of voluntarily surrendering his estate as insolvent for the benefit of his creditors may apply by written petition to that effect to the High Court or a Circuit Court.<sup>6</sup>
2. Such petition may be made:-
  - (a) On behalf of the estate of any person who is absent from the Republic, by any one who is duly authorised by power of attorney to administer such estate.
  - (b) On behalf of the estate of a deceased person, or of a person who is legally or actually incapable of managing his own estate, by any one who is lawfully charged with the management thereof.
  - (c) On behalf of the estate of any partnership, by the majority of the partners present or represented in the Republic.”

It is apparent from the decision in *Cassere v United Party Club*<sup>7</sup> that the definition of “debtor” was only introduced into South African insolvency legislation in the Insolvency Act 32 of 1916.<sup>8</sup> The definition of “debtor” in section 2 of the 1916 Insolvency Act provided as follows:

“‘Debtor’ shall, when used in connection with an estate which is about to be sequestrated or assigned, include any person who, or any estate of a person 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 for the time being in force in any Province, relating to the winding up of companies;”

This definition does not differ substantially from the current definition of “debtor” in section 2 of the Insolvency Act, thereby illustrating that the same principles that apply today applied under the 1916 Insolvency Act. Section 3(c) of this Act also provided for the sequestration of partnerships.

The current definition of “debtor” in the Insolvency Act is contained in section 2, and reads as

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<sup>6</sup> S 7 made provision for a creditor to petition the court for compulsory sequestration.

<sup>7</sup> 1930 WLD 39 at 41.

<sup>8</sup> Hereinafter referred to as the 1916 Insolvency Act.

follows:

“‘debtor’, in connection with the sequestration of the debtor’s estate, means a person or a partnership or the estate of a person or a 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;”

The use of the term “person” in the above provision is indicative of the fact that it applies to *natural* (as opposed to juristic) persons, and the provision also expressly excludes juristic persons from its operation. Although it was implied under previous insolvency statutes that they only applied to the estates of natural persons and partnerships, our legislation has since moved away from using implied provisions to the use of an express provision. Consequently the provisions of the Insolvency Act currently only apply to the estate of natural persons or partnerships.<sup>9</sup>

### 3 DEFINITION OF “DEBTOR” IN OTHER JURISDICTIONS

#### 3.1 Definition of “debtor” in the United States

The United States, being the one insolvency jurisdiction that does have a genuinely unified insolvency statute, has a very detailed provision that determines who may be a debtor under the United States Bankruptcy Code.<sup>10</sup> This detailed provision can be ascribed to the fact that the United States bankruptcy laws have been codified. Although the provision contains various exclusions, many of these have been justified elsewhere in this study.<sup>11</sup> Section 109 of the Code determines who may be a debtor for the purposes of bankruptcy proceedings, and reads as follows:

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<sup>9</sup> There are, however, exceptions to this rule. These exceptions are discussed in par 6 below.

<sup>10</sup> 11 USC s 109 (hereinafter referred to as the United States Bankruptcy Code).

<sup>11</sup> See ch 7 below.

“Sec. 109. Who may be a debtor

- (a) Notwithstanding any other provision of this section, only a person that resides or has a domicile, a place of business, or property in the United States, or a municipality, may be a debtor under this title.
- (b) A person may be a debtor under chapter 7<sup>12</sup> of this title only if such person is not -
- (1) a railroad;
  - (2) a domestic insurance company, bank, savings bank, cooperative bank, savings and loan association, building and loan association, homestead association, a small business investment company licensed by the Small Business Administration under subsection (c) or (d) of section 301 of the Small Business Investment Act of 1958, credit union, or industrial bank or similar institution which is an insured bank as defined in section 3(h) of the Federal Deposit Insurance Act; or
  - (3) a foreign insurance company, bank, savings bank, cooperative bank, savings and loan association, building and loan association, homestead association, or credit union, engaged in such business in the United States.
- (c) An entity may be a debtor under chapter 9<sup>13</sup> of this title if and only if such entity -
- (1) is a municipality;
  - (2) is specifically authorized, in its capacity as a municipality or by name, to be a debtor under such chapter by State law, or by a governmental officer or organization empowered by State law to authorize such entity to be a debtor under such chapter;
  - (3) is insolvent;
  - (4) desires to effect a plan to adjust such debts; and
  - (5)
    - (A) has obtained the agreement of creditors holding at least a majority in amount of the claims of each class that such entity intends to impair under a plan in a case under such chapter;
    - (B) has negotiated in good faith with creditors and has failed to obtain the agreement of creditors holding at least a majority in amount of the claims of each class that such entity intends to impair under a plan in a case under such chapter;
    - (C) is unable to negotiate with creditors because such negotiation is impracticable; or
    - (D) reasonably believes that a creditor may attempt to obtain a transfer that is avoidable under section 547 of this title.
- (d) Only a person that may be a debtor under chapter 7 of this title, except a stockbroker or a commodity broker, and a railroad may be a debtor under chapter 11 of this title.
- (e) Only an individual with regular income that owes, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts of less than \$250,000 and noncontingent, liquidated, secured debts of less than \$750,000, or an individual with regular income and such individual’s spouse, except a stockbroker or a commodity broker, that owe, on the date of the filing of the petition, noncontingent, liquidated, unsecured debts that aggregate less than \$250,000 and noncontingent, liquidated, secured debts of less than \$750,000 may be a debtor under chapter 13 of this title.
- (f) Only a family farmer with regular annual income may be a debtor under chapter 12 of this title.
- (g) Notwithstanding any other provision of this section, no individual or family farmer may be a debtor under this title who has been a debtor in a case pending under this title at any time in the preceding 180 days if -

<sup>12</sup> Ch 7 of the United States Bankruptcy Code deals with straight liquidations.

<sup>13</sup> Ch 9 of the United States Bankruptcy Code deals with the adjustment of debts of a municipality.



- (1) the case was dismissed by the court for willful failure of the debtor to abide by orders of the court, or to appear before the court in proper prosecution of the case; or
- (2) the debtor requested and obtained the voluntary dismissal of the case following the filing of a request for relief from the automatic stay provided by section 362 of this title.”

Section 101(15) and 101(41) of the United States Bankruptcy Code contain the definitions of “entity” and “person” that have been used in the above provision respectively. These definitions read as follows:

“(15) ‘entity’ includes person, estate, trust, governmental unit, and United States trustee;”

“(41) ‘person’ includes individual, partnership, and corporation, but does not include governmental unit, except ...”

Consequently the United States Bankruptcy Code applies equally to all types of debtors, with specific exclusions being built into the provisions where necessary. One may argue that these definitions have been drafted too exhaustively, but this is one of the consequences of the codification of their bankruptcy laws. What is striking about these provisions is that they are all-encompassing in their nature, leaving no doubt as to the ambit of their application.

### 3 2 Definition of “debtor” in England

Traditionally much of South African insolvency law, but especially company law<sup>14</sup> and the resultant provisions dealing with winding-up, have a strong English law basis.<sup>15</sup> However, the United Kingdom’s insolvency law has undergone a great deal of change since the publication of

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<sup>14</sup> See De la Rey “Aspekte van die Vroeë Maatskappyereg: ‘n Vergelykende oorsig (Deel 1)” 1986 *Codicillus* Vol 27 No 1 4-15 (hereinafter referred to as De la Rey “Aspekte van die Vroeë Maatskappyereg (Deel 1)”) and De la Rey “Aspekte van die Vroeë Maatskappyereg: ‘n Vergelykende Oorsig (Slot)” 1986 *Codicillus* Vol 27 No 2 18-24 (hereinafter referred to as De la Rey “Aspekte van die Vroeë Maatskappyereg (Slot)”).

<sup>15</sup> See ch 3 above.

the Cork Report<sup>16</sup> and the resultant (English) Insolvency Act of 1986. Although the English Insolvency Act of 1986 purports to be a “unified Act” in the sense that it covers both personal and corporate insolvency, it still retains a definite distinction between the two.<sup>17</sup>

As is currently the case in South Africa, England at one time had legislation that provided, on the one hand, for the bankruptcy of individuals and partnerships<sup>18</sup> and, on the other hand, for the winding-up of companies and other corporations. However, in England the need was felt for special provisions relating to the insolvency of partnerships. Consequently, section 420 of the 1986 Insolvency Act makes specific statutory provision for the insolvency of partnerships. These provisions have since been further refined by the Insolvent Partnerships Order of 1994,<sup>19</sup> and basically allow for a partnership to be wound up as an unregistered company.<sup>20</sup>

Currently the Insolvency Act of 1986, despite being promulgated as one Act, makes separate provision for the insolvency of individuals, partnerships and companies and other corporations. Section 73<sup>21</sup> of the Insolvency Act of 1986 contains the provisions relating to the modes of winding-up a company, while section 264<sup>22</sup> of the same Act deals with the question as to who may present a bankruptcy petition. No specific definition of “debtor” is contained in the Act itself.

<sup>16</sup> *Insolvency Law and Practice, Report of the Review Committee* (Cmnd 8558) 1982 (hereinafter referred to as the Cork Report).

<sup>17</sup> See Fletcher *The Law of Insolvency* 2nd ed (1996) 18-20 (hereinafter referred to as Fletcher). He points out that although personal and corporate insolvencies have been consolidated into one Act, the Act itself retains the traditional distinction between the two. He also points out the apparent paradox in that the Insolvency Act now also regulates the administration of solvent companies, eg where a company is wound up as a voluntary winding-up by its members. This aspect is of extreme importance for the research undertaken in this study, since the English Insolvency Act cannot be said to be a truly unified Act. See also Keay “To Unify or Not to Unify” 65-68 and Dalhuisen *Dalhuisen on International Insolvency and Bankruptcy* (1986) par 3.08[4] 1-93 (hereinafter referred to as Dalhuisen).

<sup>18</sup> Partnerships do not have legal personality under English law - see Fletcher 77-78.

<sup>19</sup> SI 1994 No 2421.

<sup>20</sup> In terms of part V of the Insolvency Act 1986. See also Fletcher 78-80.

<sup>21</sup> Contained in part IV, ch 1.

<sup>22</sup> Contained in part IX, ch 1.

### 3.3 Definition of “debtor” in Australia

Australia follows a dual system of insolvency law similar to that used in South Africa. The Australian Bankruptcy Act of 1966 (Cth) deals with individuals and partnerships, while the Corporations Act of 2001 provides for the winding-up of corporations.<sup>23</sup>

Section 7 of the Australian Bankruptcy Act provides as follows:

“7. Application of Act

- (1) This Act extends to debtors being persons who are not Australian citizens and persons who have privilege of Parliament.
- (1A) This Act applies to debtors whether or not they have attained the age of 18 years.
- (2) A sequestration order shall not be made against, nor a debtor’s petition presented by:
  - (a) a corporation; or
  - (b) a partnership or association registered under a law of the Commonwealth, of a State, or of a Territory of the Commonwealth, that provides for the winding up of a partnership or association registered under that law.
- (3) This Act applies, with any modifications prescribed by the regulations, in relation to limited partnerships as if they were ordinary partnerships and, upon all the general partners of a limited partnership becoming bankrupt, the assets of the limited partnership shall vest in the trustee.”

From these provisions it is can be seen that only entities that are not able to be wound up in terms of the Corporations Act, are dealt with in terms of the Australian Bankruptcy Act of 1966. This is the same as the situation that currently prevails in South Africa.

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<sup>23</sup> At one stage Australia did consider adopting a unified insolvency statute. However, after consideration of this issue by the Law Reform Commission, it was seen not to be a “major issue” and no recommendation to do so was made. See Australian Law Reform Commission Report No 45 *General Insolvency Inquiry* (hereinafter referred as the Harmer Report) paras 20-32. See also Keay “To Unify or not to Unify” 65-68.

### 3 4 Definition of “debtor” in the Federal Republic of Germany

Although the *Insolvenzordnung*<sup>24</sup> does not specifically define “debtor” in the Code, section 11 does indicate to whom the Code is applicable. Section 11 provides as follows:<sup>25</sup>

#### “§ 11 Permissibility of the Insolvency Proceeding

- (1) An insolvency proceeding may be commenced with respect to the assets of any natural or legal person. An association that is not a legal person shall be deemed, to such an extent, to be a legal person.
- (2) An insolvency proceeding may also be commenced with respect to:
  1. the assets of a company without legal personality (commercial partnership, limited partnership, civil law partnership, shipyard partnership, European business association);
  2. pursuant to the provisions of §§ 315 through 334, a decedent’s estate, the community property of an extended community of marital property or the community property of a community of marital property that it is administered jointly by the spouses.
- (3) The commencement of an insolvency proceeding is also permissible following the dissolution of a legal person or a company without legal personality, as long as the distribution of the assets has not been completed.”

Clearly the German *Insolvenzordnung* is intended to be all-encompassing in its ambit, although it does not cover insolvency proceedings in regard to the assets of the Federal or State Government.<sup>26</sup> Other than these specific exclusions, the *Insolvenzordnung* covers all types of debtors.<sup>27</sup> Although Germany’s insolvency laws have also now been codified, there is a striking difference between these provisions and those contained in the United States Bankruptcy Code referred to in paragraph 3.1 above. The German provisions are simple and clear, and have not been obfuscated by detailed legalese.

<sup>24</sup> *Insolvenzordnung vom 5 Oktober 1994 (BGBl. I, S. 2866)* - hereinafter referred to as the Insolvency Code of 1994. This Code came into operation on 1 January 1999.

<sup>25</sup> A translation of the *Insolvenzordnung* by Stewart has been used - see *Insolvency Code - Act Introducing the Insolvency Code* (1997) 6.

<sup>26</sup> See s 12 of the *Insolvenzordnung*, which provides that legal persons under public law are not subject to its provisions (this section refers to federal government or state government assets).

<sup>27</sup> From these provisions it is also important to note that Germany has what may be termed a “single gateway” approach to insolvency, in other words there is only one manner in which all debtors can be placed under insolvency. This is also the case in the United States of America, while countries such as England, Australia and South Africa all have a “dual gateway” approach to insolvency.

#### 4 CURRENT DEFINITION OF “DEBTOR”

The current definition of “debtor” is contained in section 2 of the Insolvency Act, and reads as follows:

“debtor’, in connection with the sequestration of the debtor’s estate, means a person or a partnership or the estate of a person or a 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;”

By couching the definition in these terms, the legislature had as its aim the exclusion of companies and other corporate entities from the ambit of the Insolvency Act.<sup>28</sup> The obvious reason for this is the dual system of insolvency law that is applied in South Africa, and which has already been discussed above.<sup>29</sup> The challenge in formulating a definition of “debtor” for the purposes of a unified Insolvency Act, lies in couching the definition in terms that embrace not only individuals and partnerships, but also the entities which the original definition sought to exclude in the first place.

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<sup>28</sup> This definition has caused numerous problems in the past. Eg, a trust is not a natural person or a partnership, but it is also not a body corporate, company or other association of persons that can be wound up in terms of the Companies Act. In *Magnum Financial Holdings (Pty) Ltd (in liquidation) v Summerly* 1984 1 SA 160 (W), the court found that since a trust could not be wound up in terms of the provisions of the Companies Act, it was an entity that could be sequestrated under the Insolvency Act. Problems have also been experienced with external companies that cannot be wound up in terms of the provisions of the Companies Act, thereby necessitating the use of sequestration proceedings under the Insolvency Act - see *Lawclaims (Pty) Ltd v Rea Shipping Co SA: Schiffcommerz Aussenhandelsbetrieb Der VVB Schiffsbau Intervening* 1979 4 SA 745 (N). See also par 6 below where these and other problems are discussed in more detail.

<sup>29</sup> See ch 3 and ch 5 above.

## 5 DEFINITION OF “DEBTOR” IN THE DRAFT INSOLVENCY BILL<sup>30</sup>

The following definition of “debtor” appears in clause 1 of the Draft Insolvency Bill.<sup>31</sup>

“‘debtor’, in connection with the liquidation of a debtor’s estate, means a person or entity which is a debtor in the usual sense of the word, except a debtor which can be wound up under the Companies Act, 1973 (Act No. 61 of 1973) or any other Act and, unless inconsistent with the context or clearly inappropriate, includes such a debtor before the date of liquidation of his or her estate;”

Initial drafts of the Law Commission’s Draft Insolvency Bill omitted the definition of “debtor”.

The reason for this is stated as follows at paragraph 1.17 to 1.18 of Commission Paper 582:<sup>32</sup>

“1.17 Paragraph 1.22 of the Explanatory Memorandum in Discussion Paper 66 notes that a definition of ‘debtor’ will be considered once it has been decided how to deal with provisions for the liquidation of legal persons.

1.18 There is strong support for the view that the same provisions should apply to companies and individuals, at least as regards the administration of the liquidation process, with nuances for banks, insurance companies and others where such differences are justified by structural requirements. The Bill is drafted in such a way that it would not be too difficult to adapt the provisions in question for legal persons. Uniform provisions for individuals and companies have not been finalised and substantive corporate law issues like rescue procedures must also receive attention. For the time being the essence of the definitions of ‘debtor’ and ‘insolvent’ in the Insolvency Act has been retained.”

## 6 PROPOSED DEFINITION OF “DEBTOR” UNDER A UNIFIED INSOLVENCY ACT

Considering that the idea is to bring about a unified Insolvency Act, the following definitions of “debtor” are proposed for the purposes of such an Act:

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<sup>30</sup> See SA Law Commission Project 63 Commission Paper 582 (11 Feb 2000) Vol 1 (hereinafter referred to as Commission Paper 582).

<sup>31</sup> Commission Paper 582 Vol 2 cl 1 9. See also the discussion of the definition in Commission Paper 582 Vol 1 cl 1 31-32.

<sup>32</sup> Vol 1 31-32.

“debtor”, when referring to who may be liquidated in terms of this Act, means:

- (a) a natural person or the estate of such natural person (hereinafter referred to as a “natural person debtor”);
- (b) a partnership or the estate of a partnership (hereinafter referred to as a “partnership debtor”);
- (c) a trust as defined in section 1 of the Trust Property Control Act 57 of 1988 (hereinafter referred to as a “trust debtor”);
- (d) a company incorporated in terms of the Companies Act 61 of 1973, or in terms of any Act or Acts which preceded the Companies Act 61 of 1973, including an external company (hereinafter referred to as a “company debtor”);
- (e) a corporation incorporated in terms of the Close Corporations Act 69 of 1984 hereinafter referred to as a “close corporation debtor”);
- (f) any other person or entity which is a debtor in the usual sense of the word (hereinafter referred to as an “association debtor”).”

“debtor”, when used as a noun in the context of this Act, means a debtor as defined in the previous paragraph which has been liquidated in terms of the provisions of this Act and, unless inconsistent with the context or clearly inappropriate, includes such a debtor before the liquidation of the debtor’s estate.”

Up to the present time South African insolvency law has been centred around the individual and the partnership, with the liquidation of companies, close corporations and the like being dealt with in separate provisions in the Companies Act and the Close Corporations Act respectively. The proposals contained in this study envisage one Act that will regulate the administration of the estates of all types of insolvent debtors, and not only that of the individual or partnership.

The definition of “debtor” is therefore the fulcrum around which the whole Act will turn. In defining a debtor in such a way as to include all types of natural, juristic and other types of debtors, one has to have regard to the specific types of problems that may occur in this regard. For example, although a church<sup>33</sup> is an association of persons that has not been created by legislation or law of general application, it does qualify as a debtor in the normal sense of the word. A church would consequently be subject to the provisions of a unified Insolvency Act. The definition as it appears above is an attempt at being all-encompassing in respect of the type of debtor that can be liquidated under a unified Insolvency Act.

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<sup>33</sup> In regard to whether churches are sequestrated or liquidated under the current laws of insolvency, it was held in *Wilson v American Methodist Episcopal Church* 15 CTR 413 that churches are in fact sequestrated (this decision was followed in *Van der Byl v Trustees, Jewish Foreign Society* 20 CTR 774).

### 6 1 Individuals (natural persons)

Paragraph (a) of the definition of “debtor” refers to natural persons, as is the case under the present Insolvency Act. For ease of reference this type of debtor is referred to as a “natural person debtor” in the unified Insolvency Act,<sup>34</sup> as there are certain provisions of the unified statute that can only be applied to natural persons.

### 6 2 Partnerships

Paragraph (b) of the definition of “debtor” refers to partnerships, as is the case under the present Insolvency Act. For ease of reference this type of debtor is referred to as a “partnership debtor” throughout the unified Insolvency Act.<sup>35</sup>

### 6 3 Trusts

Paragraph (c) of the definition refers to trusts as defined in section 1 of the Trust Property Control Act 57 of 1988. This is a new addition to the traditional definition of debtor in section 2 of the Insolvency Act, although trust debtors are presently sequestrated in terms of the provisions of the Insolvency Act.<sup>36</sup> The reason for this is that a trust does not have juristic personality and cannot therefore be wound up under the provisions of the Companies Act or Close Corporations Act.

The definition of “trust” in section 1 of the Trust Property Control Act draws a distinction between an ownership trust and the so-called *bewind* trust. Essentially the difference lies in the fact that in the former ownership of the trust assets vest in the trustee of the trust, and in the latter

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<sup>34</sup> The proposed unified Insolvency Act is contained in ann E below.

<sup>35</sup> The proposed unified Insolvency Act is contained in ann E below.

<sup>36</sup> *Magnum Financial Holdings (Pty) Ltd (in liquidation) v Summerly* 1984 1 SA 160 (W).



the ownership vests in the beneficiaries of the trust, with the trustee merely administering the trust assets on behalf of the trust beneficiaries. For the purposes of insolvency the distinction is not an important one.<sup>37</sup>

The specific inclusion of trusts in the definition of “debtor” is important, not because trusts were previously omitted from the definition, but because certain new proposals contained in a unified Insolvency Act can also then apply to trusts generally. For example, there is no reason why a trust cannot be subjected to a business rescue regime.<sup>38</sup> Just as companies and close corporations suffer financially due to mismanagement, so too do trusts. By replacing the trustees with persons having the proper skills, many trusts could be turned around to show a profit or real growth, thereby protecting the trust beneficiaries, who are in many cases below the age of majority.

#### 6 4 Companies

Paragraph (d) of the definition refers to companies incorporated under the provisions of the Companies Act. The inclusion of companies in the definition of debtor is a major shift away from present South African legislation, as companies are presently wound up in terms of the provisions

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<sup>37</sup> The distinction is important in order to determine whether vesting has taken place in a certain instance, but in both cases the trust would be one which could be liquidated.

<sup>38</sup> It often happens in practice that trustees maladminister trusts. With proper management such a trust could conceivably be turned around to profitability. Considering that many trusts have minors as beneficiaries, subjecting a trust to possible business rescue regimes may be the best protection of their interests. There are, however, some aspects that may make the application of a business rescue regime to trusts inappropriate: Eg, the costs involved in placing the trust under a business rescue regime may be too high to warrant this remedy. It may also be difficult to subject a discretionary trust to the rigours of a business rescue regime, as no vesting of rights has taken place.

## Chapter 6

## Defining “Debtor” in a Unified Insolvency Act

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of the Companies Act. This part of the definition is one of the major changes which has to be made in order to have truly unified insolvency legislation.<sup>39</sup> The definition includes external companies that have been incorporated under the Companies Act. For ease of reference this type of debtor is referred to as a “company debtor” in the proposed unified Insolvency Act.<sup>40</sup>

### 6 5 Close corporations

Paragraph (e) of the definition refers to close corporations established under the provisions of the Close Corporations Act. As is the case with companies, this is a major shift away from current South African insolvency law, where close corporations are wound up in terms of the winding-up provisions of the Close Corporations Act and the Companies Act.<sup>41</sup> For ease of reference this type of debtor is referred to as a “close corporation debtor” in the proposed unified Insolvency Act.<sup>42</sup>

### 6 6 Other debtors

Paragraph (f) of the definition has proved to be the most problematic to formulate. The idea with this paragraph is to include any possible type of debtor which is not included under the previous paragraphs. For example, a university which is created by statute would not be covered by one of the paragraphs above, but is an entity which takes part in commercial intercourse and which should, ideally, be able to be liquidated should the circumstances warrant this.

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<sup>39</sup> Something which the Cork Report could not achieve. Although the English Insolvency Act is a single statute, the liquidation of each type of debtor is dealt with separately, in the main repeating the provisions relating to each type of debtor. See Fletcher 18 and Keay “To Unify or not to Unify” 65-68.

<sup>40</sup> The proposed unified Insolvency Act is contained in ann E below.

<sup>41</sup> The provisions of the Companies Act apply by virtue of the provisions of s 66 of the Close Corporations Act.

<sup>42</sup> The proposed unified Insolvency Act is contained in ann E below.

A club is an example of a debtor that does not fall under any of the previous paragraphs in the definition of debtor, but which is an economic entity which should be capable of being subjected to a liquidation. There are various examples in our case law dealing with the sequestration or liquidation of clubs. In one of the earliest decisions in this regard, the court in *In re Panmure Club*<sup>43</sup> decided that it could not accept the surrender of the Panmure Club’s estate. The court found that the club was not a partnership that could be sequestrated in terms of the third section of Ordinance 6 of 1843, the insolvency ordinance that found application at the time. In *Re The Cape Town Club*<sup>44</sup> the question had already been asked whether or not a club could be liquidated in terms of the provisions of the Companies Act 25 of 1892. In *Cassere v United Party Club*<sup>45</sup> the court considered the possibility of sequestrating a club in some detail, arriving at the conclusion that an unincorporated body of persons capable under its constitution of holding property apart from its members, was a “debtor” in terms of section 2 of the 1916 Insolvency Act.<sup>46</sup> In *Silverman v Silver Slipper Club*<sup>47</sup> the full bench of the Transvaal Provincial Division of the Supreme Court referred with approval to the *Cassere* decision before granting a final order placing the Silver Slipper Club under sequestration.<sup>48</sup>

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<sup>43</sup> 5 EDC 170 (15 June 1886).

<sup>44</sup> 1902 19 SC 420.

<sup>45</sup> 1930 WLD 39.

<sup>46</sup> In the *Cassere* case the court did not follow the *Panmure Club* decision, but instead followed the decisions in *The Committee of the Johannesburg Public Library v Spence* 5 OR 84 and *Khunou & Pettlele v Minister for Native Affairs and Mokhatle* 1908 TS 260. In the course of its judgment the court also referred to *Van der Byl v Trustees, Jewish Foreign Society* 20 CTR 774, *Reid v South African Party Club* 1922 TPD 36 and *Graham v Milnerton Turf Club* 1921 CPD 688.

<sup>47</sup> 1932 TPD 355.

<sup>48</sup> The only recent decision that could be traced in regard to the sequestration of clubs, is the Southern Rhodesia (as it was then known) decision in *Ex parte Matabeleland Club* 1962 2 SA 647 (SR). In this case it was found that a club could be sequestrated under the provisions of Rhodesian insolvency legislation.

A more recent example of the problems that arise where specific types of debtors cannot be categorised according to the more traditional definition of debtor, can be found in the case of *In re: Body Corporate of Caroline Court*.<sup>49</sup> Although the body corporate of a sectional title scheme is a “body corporate ... or other association of persons”,<sup>50</sup> it is not one that can be liquidated or wound up in terms of the Companies Act.<sup>51</sup> In the *Caroline Court* decision the Supreme Court of Appeal had to deal with an application for the winding-up of the affairs of a body corporate where the body corporate contended that the court was empowered to wind up its affairs due to its inability to pay its debts. In bringing the application the body corporate relied on section 48(6),<sup>52</sup> alternatively on section 48(1)(c) read with section 48(6), of the Sectional Titles Act. Although the Supreme Court of Appeal decided the issue on procedural law grounds and not on the substantive law, the court did raise some interesting questions regarding the unique nature of sectional title schemes.<sup>53</sup> This case serves as an example of how the definition of “debtor” in a unified Insolvency Act should be drafted if problems of this nature are to be avoided in the future. It is submitted that the proposed definition of “debtor” under a unified insolvency statute, more specifically paragraph (f), is wide enough to include the body corporate of a sectional title scheme. Under a unified insolvency statute it is doubtful whether the problems that were experienced in

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<sup>49</sup> [2002] 1 All SA 49 (SCA).

<sup>50</sup> Cf the definition of “debtor” in s 2 of the Insolvency Act.

<sup>51</sup> See s 36(5) of the Sectional Titles Act 95 of 1986 (hereinafter referred to as the Sectional Titles Act). S 36(5) states that the provisions of the Companies Act do not apply to bodies corporate established in terms of the Sectional Titles Act.

<sup>52</sup> S 48(6) provides that the affairs of a body corporate may be wound up when the building to which it is attached is damaged or destroyed. The court found that since this was not the case in the matter under consideration, the said provision could find no application.

<sup>53</sup> It is submitted that if the body corporate is not an entity that can be wound up in terms of the Companies Act, then it falls under the current definition of “debtor” in s 2 of the Insolvency Act. Consequently the body corporate should be capable of being sequestrated in terms of the provisions of the Insolvency Act. It is further submitted that, upon closer scrutiny of the legal nature of a body corporate, it shows characteristics akin to a partnership and could very well be seen as a type of statutory partnership. Since partnerships are capable of being sequestrated, a categorisation of this nature would also have brought the body corporate under the ambit of the provisions of the Insolvency Act.

the *Caroline Court* decision would have been experienced.<sup>54</sup> For ease of reference this type of debtor has been referred to as an “association debtor” in the proposed unified Insolvency Act.<sup>55</sup>

It is important to note that one of the main purposes of these proposals is to include all possible types of juristic and non-juristic entities in the definition of debtor.<sup>56</sup> Probably the most controversial debate which was held regarding these proposals<sup>57</sup> was whether or not to include certain types of institutions which have traditionally been dealt with in separate legislation, for example banks and insurance companies.<sup>58</sup>

## 7 CONCLUSION

A discussion of the many reported cases dealing with the sequestration or liquidation of certain types of entities, has illustrated the importance of including an all-encompassing definition of “debtor” in a unified insolvency statute. It is submitted that the above definition of “debtor”, although more cumbersome than the current one which excludes corporations with juristic

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<sup>54</sup> Provided of course s 36(5) of the Sectional Titles Act, which currently states that the Companies Act does not apply to bodies corporate, is not amended to provide that the unified Insolvency Act will not apply to bodies corporate created by the provisions of the Sectional Titles Act.

<sup>55</sup> The proposed unified Insolvency Act is contained in ann E below.

<sup>56</sup> By doing so this will also mean that the problem that was experienced in *Lawclaims (Pty) Ltd v Rea Shipping Co SA: Schiffcommerz Aussenhandelsbetrieb Der VVB Schiffsbau Intervening* 1979 4 SA 745 (N) will not be experienced again. In this case a company could not be liquidated under the provisions of the Companies Act because it was an external company. Consequently the court held that the company could be sequestrated in terms of the Insolvency Act (see the definition of “debtor” in s 2 of the Insolvency Act). With more and more cross-border insolvency cases coming to the fore of late, having a unified Insolvency Act will not only solve the problems experienced in the *Lawclaims* case, but will also prevent other potential problems from arising in cross-border insolvency matters - see Smith and Boraine “Crossing Borders Into South African Insolvency Law: From the Roman-Dutch Jurists to the Uncitral Model Law” 2002 10 *ABI Law Review* 135 (hereinafter referred to as Smith and Boraine).

<sup>57</sup> See eg the Workshop Transcriptions 18.

<sup>58</sup> Currently the provisions relating to these types of institutions are dealt with in s 68 of the Banks Act 94 of 1990, part VI of the Long Term Insurance Act 52 of 1998 and part VI of the Short Term Insurance Act 53 of 1998 respectively. This aspect is dealt with separately under ch 7 below.

personality, succeeds in being all-encompassing by including every conceivable form of debtor, be it corporate or otherwise.

The mere existence of a unified insolvency statute will obviate the need to try and determine, as is currently the case, whether a specific debtor should be sequestrated or liquidated under the provisions of different Acts. Under a unified Insolvency Act all debtors will be subject to liquidation in terms of the same statute, thereby creating certainty and uniformity, and will also negate the effect of the many reported cases in this regard.



**CHAPTER 7**

**SPECIALISED INSTITUTIONS UNDER A UNIFIED INSOLVENCY ACT**

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**SUMMARY**

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**1 INTRODUCTION<sup>1</sup>**

As in the case of most other countries,<sup>2</sup> there are certain types of specialised institutions which enjoy preferential treatment due to the nature of these business concerns. The main reason for their preferential treatment appears to be the protection of the public interest. The question that has to be decided within the framework of this study, is whether or not these institutions deserve their specialised status - not generally, but in the event of insolvency. This chapter seeks to answer this question and then proceeds to make proposals giving effect to the conclusions that have been reached.

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<sup>1</sup> In this chapter frequent reference will be made to the *Final Report Containing Proposals on a Unified Insolvency Act Jan 2000 Vol 1 to 5*. This report was drafted under the auspices of the Centre for Advanced Corporate and Insolvency Law at the University of Pretoria, and a copy thereof is available at the Merensky Library, University of Pretoria. This report is referred to in this chapter as the Final Report.

<sup>2</sup> See Giovanoli and Heinrich (eds) *International Bank Insolvencies: A Central Bank Perspective* (1999) where a useful summary of the handling of insolvent banks in various jurisdictions is provided.



Apart from the treatment of specialised institutions, there are also other (ancillary) matters that need to be discussed if a truly unified insolvency statute is to be introduced. These matters include alternatives to the liquidation (sequestration) of individuals,<sup>3</sup> the treatment of insolvent deceased estates,<sup>4</sup> business rescue provisions<sup>5</sup> and personal liability of directors and others,<sup>6</sup> to name but a few. While the treatment of specialised institutions will be dealt with in this chapter, the other ancillary matters mentioned above will be dealt with in Part 4C of this study. The treatment of solvent companies and close corporations will be dealt with in Part 4D below.

## 2 SPECIALISED INSTITUTIONS<sup>7</sup>

Since the key issue to be decided here is whether or not there should be one Act which deals with the liquidation of all legal entities, it is necessary to briefly look at the entities which receive specialised treatment under South African law. Besides the Companies Act 61 of 1973<sup>8</sup> and the Close Corporations Act 69 of 1984,<sup>9</sup> there are a number of other legislative provisions dealing with the liquidation of specific types of institutions, or the placing under curatorship of such

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<sup>3</sup> Eg the question arises as to whether s 74 of the Magistrates' Courts Act 32 of 1944 should be included in a unified insolvency statute.

<sup>4</sup> Currently regulated by s 34 of the Administration of Estates Act 66 of 1965.

<sup>5</sup> South Africa has a very limited array of business rescue provisions, namely s 311 of the Companies Act dealing with compromises, and judicial management which is dealt with in s 427 *et seq* of the Companies Act.

<sup>6</sup> Currently dealt with in s 424 of the Companies Act.

<sup>7</sup> In this chapter reference is made to the transcriptions of a symposium held on 23 Oct 1998, transcriptions of workshops held from 7 to 10 Dec 1998 and transcriptions of a conference held on 6 Oct 1999. The symposium, workshops and conference were used in order to obtain input from the insolvency profession as to the content and technical workings of a unified insolvency statute. In this study the transcriptions will be referred to as the Symposium Transcriptions (Final Report, Vol 2), Workshop Transcriptions (Final Report, Vol 2) and Conference Transcriptions (Final Report, Vol 4) respectively. A copy of these documents are available for perusal in the Merensky Library, University of Pretoria.

<sup>8</sup> Hereinafter referred to as the Companies Act. The provisions of the Companies Act do not have unlimited application - see s 3 of the Companies Act.

<sup>9</sup> Hereinafter referred to as the Close Corporations Act.

institutions. These are Part VI of the Long-Term Insurance Act 52 of 1988;<sup>10</sup> Part VI of the Short-Term Insurance Act 53 of 1988;<sup>11</sup> section 29 of the Pension Funds Act 24 of 1956; section 35 of the Friendly Societies Act 25 of 1956; section 18C of the Medical Schemes Act 72 of 1967; sections 27, 28 and 39 of the Unit Trusts Control Act 54 of 1981; Chapter X of the Co-Operatives Act 91 of 1981; section 33 of the Financial Markets Control Act 55 of 1989; section 68 of the Banks Act 94 of 1990;<sup>12</sup> and Chapter VIII of the Mutual Banks Act 124 of 1993.<sup>13</sup> For the sake of brevity only the liquidation of banks, and to a more limited extent insurance companies, will be referred to in this chapter. However, what is stated here in respect of banks and insurance companies will apply equally to the other institutions mentioned in this paragraph.

It seems illogical to speak of a unified Insolvency Act if such a unified Act is not going to be complete in every sense. The problem here is that these specialised institutions, such as banks and insurance companies,<sup>14</sup> are not directly governed by the provisions contained in the Insolvency Act, Companies Act or Close Corporations Act, even though such institution is, for example, a company. These specific types of institutions have provisions in their enabling legislation that regulate their winding-up or judicial management.<sup>15</sup>

While it is understandable that the authorities which are responsible for the administration of these institutions would prefer to retain control over the manner in which they are wound up or placed

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<sup>10</sup> Hereinafter referred to as the Long-Term Insurance Act.

<sup>11</sup> Hereinafter referred to as the Short-Term Insurance Act.

<sup>12</sup> Hereinafter referred to as the 1990 Banks Act.

<sup>13</sup> See par 5.1.2 of the Introduction and Summary of Recommended Changes, Discussion Paper 66, Project 63 by the South African Law Commission.

<sup>14</sup> See the Symposium Transcriptions 1-31 and the Workshop Transcriptions 1-74 for a discussion of these issues at the symposium and workshops respectively.

<sup>15</sup> Generally speaking the provisions of the Insolvency Act 24 of 1936 (hereinafter referred to as the Insolvency Act) are applied, but subject to special provisions applying in the case of the winding-up of such a specialised institution. One exception to this is the provisions of the Co-Operatives Act 91 of 1981. This Act comes close to reproducing all the provisions of the Insolvency Act.

under judicial management, it is submitted that there is no real reason why this can only be achieved by including such provisions in the enabling legislation. Stated differently, there appears to be no overwhelming reason why these provisions should not be included in a unified insolvency statute.<sup>16</sup>

In most cases the protection of the public interest is the basis for the current provisions in the Acts referred to.<sup>17</sup> To this end the authority governing such institutions has an important role to play. For example, when an application is brought in order to place a bank in liquidation, the Registrar of Banks has the right to oppose such application.<sup>18</sup> In the same vein the registrar has the right to apply to court to have a bank wound up.<sup>19</sup> The Master of the High Court may also not appoint any person as liquidator or judicial manager of a bank other than a person recommended by the Registrar of Banks.<sup>20</sup> These are laudable provisions that are aimed not only at protecting the interests of the bank's clients, the public, but also for the protection of financial markets and the national payments system. The principle of protecting the public interest also applies to the interests of policy holders in the case of insurance companies.<sup>21</sup>

Laudable as these provisions are, there is no reason why the same provisions, which currently protect the public interest, cannot be included in proposals for a unified insolvency statute. These provisions are aimed at preventing any person from simply bringing an application to wind up, for

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<sup>16</sup> It is evident that the Reserve Bank is opposed to this idea - see the Conference Transcriptions 16-67, and especially the comments made by Grobler (commencing at 28).

<sup>17</sup> In the case of banks there is an additional reason, namely the so-called "systemic risk" that is peculiar to the banking industry. Stated simply, systemic risk is the risk that a disturbance in financial markets may seriously harm the financial position of financial firms which could in turn disrupt the payments system of a country - see Patrikis "Role and Functions of Authorities: Supervision, Insolvency Prevention and Liquidation" in Giovanoli and Heinrich (eds) *International Bank Insolvencies, A Central Bank Perspective* (1999) 283. This aspect is dealt with in greater detail in par 4.1 below.

<sup>18</sup> S 68(1)(a) of the 1990 Banks Act.

<sup>19</sup> S 68(1)(a) of the 1990 Banks Act.

<sup>20</sup> S 68(1)(b) of the 1990 Banks Act.

<sup>21</sup> See eg part VI of the Long-Term Insurance Act.

example, a bank or insurance company that would, obviously, result in potential chaos. However, once the checks and balances have been complied with and the Registrar has been consulted and notified of the winding-up, it does not mean that the Registrar cannot still exercise his powers just because the provisions are contained in a unified piece of insolvency legislation.

The unification of insolvency legislation is not intended to take away the powers of any governing authority over its charge, but merely to provide for uniform procedures once the institution in question has in fact been placed in liquidation. After all, an insolvent bank is still insolvent and the provisions relating to insolvency must be applied to it.<sup>22</sup>

In brief, it can be stated that the powers that have currently been conferred on the governing authorities in respect of specialised institutions, will have to be retained in proposals for unified insolvency legislation. This is not only necessary in order to protect the public interest, but also for the purposes of good administration. However, the same objectives can be achieved by including these provisions in one consolidated piece of legislation.<sup>23</sup>

### **3 HISTORICAL DEVELOPMENT**

In order to determine whether or not the liquidation provisions relating to the banking and other specialised industries should be kept separate or included in a unified Act, it is necessary to briefly

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<sup>22</sup> It is conceded that the provisions relating to the appointment as co-liquidator of someone who is knowledgeable about the banking industry (s 68(1)(c) of the 1990 Banks Act) are important, and this has been addressed in the proposals contained in this report.

<sup>23</sup> The problem of amendment to the unified piece of insolvency legislation has also been addressed. Eg, unified insolvency legislation will probably fall under the control of the Ministry of Justice and Constitutional Development while the Banks Act, eg, falls under the auspices of the Ministry of Finance. The Finance Ministry would no doubt disapprove of the idea of the legislation being amended without first being consulted. This can effectively be addressed by building in a peremptory consultation clause before certain sections can be amended. This has been done very effectively in the new s 98A of the Insolvency Act, that makes provision for peremptory consultation in the case of amendment to provisions relating to preferences payable to employees in an insolvent estate.

set out the historical development of these specialised provisions. As stated above,<sup>24</sup> only the banking industry and, where necessary, insurance companies will be discussed in this chapter. In respect of banks a complete history has been provided. In the case of insurance companies only Union and current legislation will be discussed.

### **3 1 Pre-Union banking legislation**

#### *3 1 1 Cape Colony*

The earliest legislation dealing with banks in the Cape Colony that can be traced, is an ordinance in terms of which the Cape of Good Hope Savings Bank was established.<sup>25</sup> This ordinance did not contain any provisions as to the banks's liquidation or dissolution, and does not shed any light on the manner in which banks were wound up, if at all, during this period.

The first reference to banks in any legislation is to be found in the Joint-Stock Companies' Limited Liability Act 23 of 1861. Section I of this Act provided:

"I. The term 'joint-stock company' in this Act shall mean every partnership whereof the capital is divided, or agreed to be divided into shares, and so as to be transferable without the express consent of all the partners; and also every partnership which at its formation or by subsequent admission shall consist of more than twenty-five members: Provided, however, that nothing in this Act contained shall apply to any joint-stock company formed for the purpose of banking."

However, in the fourth proviso to section XIII, which dealt with proceedings against shareholders where the company had insufficient goods to satisfy an execution judgment, it was stated that this section did in fact apply to every joint-stock company established for the purpose of banking, notwithstanding anything to the contrary contained in the Act. From this it would appear that separate legislation did in fact regulate the incorporation of joint-stock companies for the purpose

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<sup>24</sup> See par 1 above.

<sup>25</sup> Ordinance 86 of 1831.

of banking, but that the rules regulating the liability of shareholders, also applied to shareholders of a joint-stock company established for banking.<sup>26</sup>

The Winding-up Act 12 of 1868 was the first legislation in the Cape Colony to make specific provision for the winding-up of joint-stock companies. Nowhere in this Act could any reference be found to a provision stating that it did not apply to joint-stock companies operating as a bank. In fact, in *The Wellington Bank, In Liquidation*<sup>27</sup> Smith J asked the question as to why the bank had not been placed “under the Winding-up Act at once” where the shareholders had first attempted a voluntary winding-up. The court immediately placed the bank under liquidation and appointed liquidators to deal with the administration.

The picture in regard to banks becomes even clearer in the Companies Act 25 of 1892. Section 222 of this Act provided as follows:

“222. In the case of any company subject to this Act and formed for the purpose of carrying on the business of banking or the business of life assurance, the provisions of this Act shall not apply in any case in which they would be inconsistent with the provisions of ‘The Banks Act, 1891,’ or ‘The Life Assurance Act, 1891,’ as the case may be.”

From this it is evident that the winding-up provisions contained in this Act applied also to banks, except in so far as they were inconsistent with the provisions of the enabling legislation.<sup>28</sup> However, the Banks Act 6 of 1891 did not contain any provisions pertaining to the liquidation

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<sup>26</sup> There was much litigation concerning this aspect at the time. See eg *Union Bank (in liquidation) v Watson’s Heirs* (1891) 1 CTR 72; *The Cape of Good Hope Bank (in liquidation) v East, Runciman and Others* (1891) 1 CTR 75 (also reported at (1891) 8 SC 157); *Liquidators Paarl Bank v Executrix and Heirs of GJ Roux* (1891) 1 CTR 136 (also reported under *The Liquidators of the Paarl Bank v Roux and Others* (1891) 8 SC 205); *The Union Bank, In Liquidation v Uys* (1891) 1 CTR 119; *The Cape of Good Hope Bank, In Liquidation v Belson* (1891) 1 CTR 183.

<sup>27</sup> (1891) 1 CTR 181. See also *Liquidators of Union Bank v King’s Trustee* (1893) 3 CTR 89 (also reported at (1893) 10 SC 101) where it is evident that the bank was being wound up in terms of the provisions of the Winding-up Act of 1868.

<sup>28</sup> See *The Cape of Good Hope Bank (in liquidation) v East, Runciman and Others* (1891) 1 CTR 75 (also reported at (1891) 8 SC 157) from which it is evident that the winding-up provisions of the Winding-up Act 23 of 1861 applied also to the winding-up of banks.

or winding-up of a bank. In fact, the Banks Act 6 of 1891 did not refer in any way to what would happen if a bank was to be wound up, which merely confirms the view that banks were wound up in the same way as any other company would be at that time. The Banks Act 6 of 1891 was later repealed by the Banking Act 38 of 1942.<sup>29</sup> However, the Life Assurance Act 13 of 1891 did contain provisions relating to the winding-up of a life assurance company. Section 24 of the Life Assurance Act 13 of 1891 provided as follows:

“24. The Court may order the winding-up of any company, in accordance with the “Winding-up Act, 1868,”<sup>30</sup> upon the petition of twenty or more policy-holders or shareholders, upon its being proved to the satisfaction of the Court that the company is insolvent; and in determining whether or not the company is insolvent, the Court shall take into account its contingent or prospective liability under policies or annuity, or other existing contracts.”

An interesting innovation, however, is to be found in section 25 of the same Act, granting the court a discretion to allow a procedure in lieu of winding-up:

“25 The Court may in the case of the company which has been proved to be insolvent, reduce the amount of the contracts of such company upon such terms and subject to such conditions as to the Court may seem fit, instead of granting a winding-up order.”

Section 26 also contained references to winding-up, but does not have any direct bearing on the present discussion.

### *3.1.2 Natal*

The Joint-Stock Companies' Limited Liability Law 10 of 1864 was the equivalent of the Cape Colony's Joint-Stock Companies' Limited Liability Act of 1861.<sup>31</sup> However, while the Natal statute contained the same provision stating that the Act did not apply to joint-stock companies established for the purpose of banking, it did not contain the fourth proviso that the Cape Colony

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<sup>29</sup> See par 3.2 below.

<sup>30</sup> This Act was repealed by Act 25 of 1892.

<sup>31</sup> See par 3.1.1 above.

statute contained in section XIII. Section 12 of the Natal statute was the equivalent of the Cape Colony's section XIII, and contained no provision referring to the liability of shareholders in a joint-stock company established for the purpose of banking. From this it is assumed that none of the provisions of the Natal statute applied to banks.

The Special Partnerships Limited Liability Act of 1864<sup>32</sup> specifically excluded "partnerships being Joint-Stock Companies, or being formed for the purpose of banking". From this one would assume that there was special legislation governing the winding-up of banks at the time, but no such legislation could be traced. In the Natal Winding-up Law 19 of 1866, no reference at all was made to banks or their exclusion from the ambit of the Act. From this must be deduced that the Act and all its provisions did in fact apply to banks and other specialised institutions, especially since the Natal Bank Act of 1888<sup>33</sup> contained no provision stating otherwise. The only provision that related to the winding-up of a bank in the 1888 statute was section 97, and provided as follows:

"97. If at any time during the continuance of this Law The Natal Bank (Limited) shall have sustained actual damages and incurred losses to such an amount that the whole amount of the Reserve Fund then accumulated, and one-fourth part of the subscribed Capital of the Bank (as by this Law defined, and from time to time increased), shall be exhausted in paying off and satisfying said damages and losses, then the Board of Directors for the time being shall forthwith call a special general meeting of the shareholders, in manner hereinbefore provided, and shall submit to such meeting a full and general statement of the affairs and concerns of the said Bank, and thereupon the affairs of the said Bank shall be wound up, and the Bank, as soon as may be, dissolved."

Unfortunately the Act did not state how, or in terms of which legislation, the bank was to be wound up. One can only assume that the winding-up laws at the time applied to the winding-up of the bank.

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<sup>32</sup> Law No 1 of 1865.

<sup>33</sup> Law No 43 of 1888.



### 3 1 3 Transvaal

In section 1 of *De Acte van Maatschappijen met Beperkte Verantwoordelijkheid*<sup>34</sup> it is evident that this legislation did not apply to banks. It is stated thus in the Act itself:

“ ..., met bepaling echter dat niets in deze wet vervat, betrekking zal hebben op eenige bankmaatschappij.”

The 1891 *Wet op het Liquideeren van Maatschappijen*<sup>35</sup> contained no reference to companies established for the purpose of banking. Also the *Wet met betrekking tot de Banken in de Zuid-Afrikaansche Republiek*<sup>36</sup> of 1892 contained no references to winding-up, and one must therefore assume that the *Wet op het Liquideeren van Maatschappijen* of 1891 did indeed apply to the liquidation of, *inter alia*, banks. The 1892 *Wet met betrekking tot de Banken in de Zuid-Afrikaansche Republiek* was replaced in 1893 by the *Wet met betrekking tot de Banken in de Zuid-Afrikaansche Republiek*<sup>37</sup> and likewise contained no reference to the winding-up of a bank. The latter Act was later repealed by the Banking Act 38 of 1942.<sup>38</sup> The 1894 *Wet op het Liquideeren van Maatschappijen*,<sup>39</sup> which replaced the winding-up statute of 1891, also contained no reference to the position of banks under this Act.

The Companies Act 31 of 1909 contained very precise provisions relating to not only the winding-up of banks and insurance companies,<sup>40</sup> but also co-operatives, building societies, friendly societies and trade unions.<sup>41</sup> Section 201 of this Act provided as follows:

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<sup>34</sup> *Wet No 5 van 1874.*

<sup>35</sup> *Wet No 8 van 1891.*

<sup>36</sup> *Wet No 22 van 1892.*

<sup>37</sup> *Wet No 2 van 1893.*

<sup>38</sup> See par 3.2 below.

<sup>39</sup> *Wet No 1 van 1894.*

<sup>40</sup> See s 201.

<sup>41</sup> See s 202.

“201. Where a company or a foreign company is subject to the provisions of-

- (a) Law No. 2 of 1893 or any law which for the time being is specially applicable to banking companies; or
- (b) Law No. 8 of 1898 or any law which for the time being is specially applicable to life, fire, or accident insurance companies or societies,

the provisions of this Act which would otherwise apply in respect of such company shall not apply wherever these provisions would be inconsistent with any such law.”

From this section it is evident that the provisions of the Companies Act would also apply to banks and insurance companies, but only in so far as the provisions were not inconsistent with the provisions of the banking legislation that applied at the time and the legislation dealing with insurance companies. As pointed out in the previous paragraph, Law 2 of 1893 contained no reference to winding-up, and it is to be assumed that the reference to this Act was to the provisions relating to the functioning of the bank as such. Likewise, Law No 8 of 1898<sup>42</sup> contained no references to winding-up.

### 3 1 4 Orange Free State

Section 13 of the *Wet over Beperkte Verantwoordelijkheid van Naamlooze Vennootschappen* contained in *Hoofdstuk C van Wetboek*, dealt with the liability of shareholders. In section 13(4) provision was made for the liability of shareholders of banking companies, despite any provisions to the contrary that may have been provided for elsewhere. Clearly there was other legislation at the time that regulated companies established for the banking industry.

Chapter CI of the Statute Law (*Wetboek*) of the Orange River Colony contained The Articles of Association of the National Bank. Part XVII of this Act made provision for the “Winding up of the National Bank of the Orange Free State, Limited” which were dealt with in sections 105 to 109. However, from the provisions themselves it would appear that the bank was not necessarily insolvent to the extent that it could not pay its debts. What happened if the bank was in fact hopelessly insolvent, is not certain from the provisions in question. Due to their importance, sections 106 and 107 are reproduced here in their entirety:

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<sup>42</sup> *Wet tot Regeling van de Besigheid van Assurantie-Maatschappijen in de Zuid-Afrikaansche Republiek, Wet No 8 van 1898.*



curatorship. Section 43 of the 1942 Banking Act made provision for a bank to be placed under curatorship by applying the provisions of sections 196 to 198 (inclusive) of the Companies Act 46 of 1926,<sup>44</sup> which provided for judicial management.

Section 44 of the 1942 Banking Act made provision for a bank to be wound up under the provisions of the 1926 Companies Act, subject to certain provisos. These provisos amounted to the following: The provisions did not apply if the bank was registered under the Co-operative Societies Act of 1939; the Registrar of Banks was added as one of the parties that needed to be informed and upon whom documents had to be served; the Registrar of Banks replaced the Master or was added as an additional party in some of the provisions; and the Registrar of Banks was given the power to oppose or bring winding-up applications in respect of banks. Section 45 of the 1942 Banking Act made provision for the cancellation of the bank's registration or provisional registration once the Master or court had confirmed the final account in regard to the winding-up of the financial institution.

### 3 2 2 *Banks Act 23 of 1965*<sup>45</sup>

The 1942 Banking Act was repealed by the 1965 Banks Act. Although very similar to the provisions contained in the 1942 Act, the provisions contained in sections 40, 41 and 42 of this new legislation were a little more refined than the provisions contained in the previous Act. However, the provisions did not really provide for anything new and were basically a re-enactment of the existing provisions dealing with the curatorship<sup>46</sup> and winding-up of a bank.

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<sup>44</sup> Hereinafter referred to as the 1926 Companies Act.

<sup>45</sup> Hereinafter referred to as the 1965 Banks Act. For a brief discussion of the winding-up provisions of this Act, see Willis *Banking in South African Law* (1981) 93-94 (hereinafter referred to as Willis). For an example of the difficulties experienced in applying the various provisions of both the 1965 Banks Act and the 1990 Banks Act, see *Alpha Bank Bpk v Registrateur van Banke* 1996 1 SA 330.

<sup>46</sup> For a brief discussion of the curatorship of a bank under these provisions, see Willis 94-96.

One major innovation, however, was section 41(6), which provided that only a person recommended by the Registrar of Banks could be appointed by the Master as a liquidator or judicial manager in the case where a bank was being wound up or had been placed under curatorship.<sup>47</sup>

### 3 3 Union legislation relating to the insurance industry<sup>48</sup>

#### 3 3 1 Insurance Act 37 of 1923<sup>49</sup>

Section 35 of the 1923 Insurance Act made provision for the petition by policy-holders for the winding-up of an insurance company.<sup>50</sup> Section 35(1) provided as follows:

“35. (1) On the petition of twenty or more policy-holders owning life policies for an aggregate sum of not less than ten thousand pounds and upon its being proved to the satisfaction of the court that the company is insolvent, the court may order the winding up of any company whose head office is in the Union and may apply, as far as may be deemed necessary, the provisions of the law governing the winding up of companies: Provided that such petition shall not be presented except with the leave of the court and leave shall not be granted until a *prima facie* case has been established to the satisfaction of the court and until security for costs such as an amount as the court may think reasonable has been given.”

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<sup>47</sup> See Willis 93-96.

<sup>48</sup> Although only Union legislation in regard to insurance companies will be discussed here, it is to be noted that there were several Acts and Ordinances that regulated the insurance industry in the various colonies prior to these Acts. Due to the fact that the historical development of winding-up provisions in respect of insurance companies is very much the same as that relating to banks, the detail of these statutes will not not be discussed here. However, for the sake of completeness the statutes in question are mentioned here: *Cape Colony*: Act for Incorporating the Union Fire and Marine Insurance and Trust Company, Act 32 of 1861; the Life Assurance Act, Act 13 of 1891. *Natal*: Assurance & Insurance Companies Act, Act 47 of 1904. *Transvaal*: *Wet tot Regeling van de Bezigheid van Assurantie-Maatschappijen in de Zuid-Afrikaanse Republiek, Wet No 12 van 1892*; *Wet tot Regeling van de Bezigheid van Assurantie-Maatschappijen in de Zuid-Afrikaanse Republiek, Wet No 8 van 1898*. *Orange Free State*: ch CIII of the Statute Law, Regulating the Admission of Insurance Companies; Law to Regulate Rights under Policies of Life Assurance, Law 12 of 1894.

<sup>49</sup> Hereinafter referred to as the 1923 Insurance Act.

<sup>50</sup> As to when a policy-holder had *locus standi* to bring such an application, see *L J Sheffield & Co Ltd v The United Provident and Assurance Association of South Africa, Limited*; *Barrow v Idem*; *Butterworth v Idem* 1932 WLD 200.

The following points are of interest here:

- (a) It had to be proved that the insurance company was insolvent;
- (b) The law applying to the winding-up of companies was applicable;<sup>51</sup>
- (c) The petition could not be presented to the court without its (the court's) permission; and
- (d) The court could not grant leave until such time as a *prima facie* case had been made.

The requirement that a *prima facie* case first had to be made before the court would grant leave to petition the court for winding-up was probably designed to prevent frivolous applications for the winding-up of insurance companies, thereby causing a panic amongst the public.

Section 35(2) conferred on the court the power to reduce the contracts of the insurance company instead of issuing a winding-up order. This would probably occur in cases where the court was of the opinion that the insurance company was still viable, and that it was not in the interests of the policy holders to place the insurance company in liquidation. Section 35(3) merely provided for the manner in which the value of policies had to be determined for the purposes of winding-up or the bringing of an application for the winding-up of an insurance company.

### 3 3 2 *Insurance Act 27 of 1943*<sup>52</sup>

The 1943 Insurance Act contained far more refined provisions in respect of winding-up than the provisions contained in the 1923 Insurance Act.<sup>53</sup> In addition to these extended provisions, the Act also made provision for the possibility of an insurance company being placed under judicial

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<sup>51</sup> In this regard see also the comments made in Davis *Gordon and Getz on the South African Law of Insurance* 4th ed (1993) 54 (hereinafter referred to as Davis).

<sup>52</sup> Hereinafter referred to as the 1943 Insurance Act. As regards the winding-up and judicial management of insurance companies under the 1943 Insurance Act generally, see Davis ch 3.

<sup>53</sup> See ss 30 and 32.

management.<sup>54</sup> It is also important to note that section 3(1) of the Companies Act expressly excludes the operation of the Companies Act in cases where its provisions are inconsistent with the provisions of the Insurance Act.<sup>55</sup>

In terms of section 30 of the 1943 Insurance Act the following persons or institutions could bring an application for the winding-up of an insurance company:<sup>56</sup>

- (a) The Registrar of Insurance Companies<sup>57</sup> (with the permission of the relevant Minister);<sup>58</sup>

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<sup>54</sup> See s 31. See also Davis 68-72.

<sup>55</sup> See also Davis 54. The reasons for the exclusion of the operation of the provisions of the Companies Act were explained by Vieyra J in *Ex parte Liquidators of Parity Insurance Co Ltd* 1966 1 SA 463 (W). According to Vieyra J (at 466) the reasons are that the liquidation of insurance companies introduce complexities of a nature not found in the liquidation of ordinary commercial companies. Vieyra J also criticised (at 476) the provisions in the 1943 Insurance Act as being inadequate, and the language as being obscure. However, see *Lindsay Keller & Partners v AA Mutual Insurance Association Ltd* 1988 2 SA 519 (W) where the court held that the winding-up provisions of the Companies Act were not inconsistent with the provisions of the Insurance Act of 1943. In this case the court distinguished between the winding-up of the “insurance business” of an insurance company and the winding-up of the company itself, holding that the provisions of the Insurance Act only applied to the winding-up of the “insurance business” (see also the discussion of the *Lindsay Keller* decision in Davis 57-58). However, see *Connolly v AA Mutual Insurance Association Ltd* 1991 1 SA 423 (W) where the plaintiff (the liquidators of an insurance company) contended that one part of an insurance business could be wound up, allowing the liquidators to sue the remaining part. Schabert J (at 428) regarded the contention as “utterly imaginable”. In *Ex parte Wells: In re African Horizon Insurance Co Ltd (in liquidation)* 1963 2 SA 419 (C) the court had already expressed its view that the provisions of s 32(4) of the 1943 Insurance Act did not allow the court to “issue legislation” superseding the provisions of the (1926) Companies Act.

<sup>56</sup> It is interesting to note that no grounds for the winding-up of an insurance company were provided for in the 1943 Insurance Act, save one instance where the Registrar was the applicant - see Davis 56. Since the provisions of the Companies Act applied *mutatis mutandis* (see ss 31(6) and 32(5)) except in so far as the provisions were inconsistent with the provisions of the 1943 Insurance Act, the grounds for liquidation set out in the Companies Act could be relied upon in appropriate circumstances - see Davis 56-57. In *Registrar of Insurance v Johannesburg Insurance Co Ltd (2)* 1962 4 SA 548 (W) at 551 Hiemstra J stated that the grounds for winding-up insurance companies are wider than in the case of other companies.

<sup>57</sup> For an example of this, see *Registrar of Insurance v Provident Assurance Corporation of Africa Ltd* 1963 4 SA 83 (W). See also Davis 54-55.

<sup>58</sup> S 30(1).

- (b) A registered insurer;<sup>59</sup>
- (c) A creditor of the insurance company “who was unable to obtain payment of his claim after recourse to the ordinary process of law”.<sup>60</sup>

However, none of the above could bring an application unless they had satisfied the court of the desirability of bringing such an application.<sup>61</sup> Section 30(3) made provision for the powers of the court where an application was brought. The court could:

- (a) Refuse the application;<sup>62</sup>
- (b) Order the Registrar to appoint an inspector to investigate the affairs of the insurance company;<sup>63</sup>
- (c) Order that the whole or part of the business of such an insurer be placed under judicial management;<sup>64</sup> or
- (d) Order that the whole or part of the business of such an insurer be wound up.<sup>65</sup>

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<sup>59</sup> S 30(1). See also Davis 55.

<sup>60</sup> S 30(2). See also Davis 55-56.

<sup>61</sup> Proviso to s 30(1) and proviso to s 30(2).

<sup>62</sup> S 30(3)(a); Davis 62.

<sup>63</sup> S 30(3)(b); Davis 62.

<sup>64</sup> S 30(3)(c); Davis 62. In terms of s 31(3) the court had to appoint the judicial manager and determine his or her remuneration. From the decision in *Ex parte Registrar of Insurance* 1963 3 SA 411 (W) it would appear that the court would only determine the remuneration after the judicial manager had reported to the court in terms of s 31(9).

<sup>65</sup> S 30(3)(d); Davis 63.



Section 30 of the Act also clearly stated that when exercising its discretion, the court had to act primarily in the interests of the policy owners.<sup>66</sup> Although the Registrar of Insurance played a critical role in the winding-up of an insurance company, he did not usurp the Master's powers in such a case.<sup>67</sup> In fact, the Master retained all his usual rights and powers in cases where insurance companies were being wound up.<sup>68</sup>

Section 31 made provision for the judicial management of an insurance company, and contained detailed provisions in respect of how the judicial management of the company was to be conducted.<sup>69</sup> The whole process was controlled by the court.<sup>70</sup> Section 32 made provision for winding-up and, interestingly enough, this whole process was also driven by the court. For example:

- (a) The court appointed a liquidator;<sup>71</sup>
- (b) The court could issue directions to the liquidator as it saw fit;<sup>72</sup>

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<sup>66</sup> It is for this reason that an alternative to the winding-up of an insurance company must be found, if at all possible - see in this regard the comments by Marais J in *Financial Mail (Pty) Ltd v Registrar of Insurance* 1966 2 SA 219 (W).

<sup>67</sup> See *Ex parte Liquidators of Parity Insurance Co Ltd* 1966 1 SA 463 (W).

<sup>68</sup> See *Registrar of Financial Institutions v Parity Insurance Co Ltd* 1965 2 SA 461 (W).

<sup>69</sup> For a more detailed discussion of the judicial management provisions, see Davis 68-72.

<sup>70</sup> See *Parity Insurance Co Ltd (in liquidation) v Hill* 1967 2 SA 551 (A); Davis 72-76.

<sup>71</sup> S 32(3). As regards the remuneration that the liquidator was entitled to, the court normally determined this on the return day of the rule *nisi* (see Davis 63). In cases where the remuneration determined by the court turned out to be insufficient, it was held that the liquidator was entitled to approach the court for a variation of the original order - see in this regard *Ex parte Wells: In re Auto Protection Insurance Co Ltd* 1968 2 SA 631(W).

<sup>72</sup> S 32(4). This subsection was amended in 1969 to state that the instructions given by the court would "prevail over the provisions of any law other than this Act". However, the word "law" as it was applied in this section did not mean the common law - see *Schuurman v Motor Insurers' Association of SA* 1960 4 SA 316 (T). For an example of the court issuing instructions to the liquidator, see *Foord v Lake* 1968 4 SA 395 (W) where the court gave the liquidator the power to accept or reject claims without proof before a magistrate, and to compromise claims without any directions from the creditors.

- (c) The liquidator acted under the control of the court at all times and could apply to the court for instruction.<sup>73</sup>

Although the law relating to the winding-up of companies applied *mutatis mutandis* to an insurance company being wound up, they only applied in so far as they were not inconsistent with the (detailed) provisions contained in the Insurance Act.<sup>74</sup>

### 3 4 Current position in regard to the banking industry

Before the current Banks Act 94 of 1990<sup>75</sup> could be promulgated, the current (1973) Companies Act had in the meantime been passed by Parliament. The 1990 Banks Act was therefore drafted with references to the 1973 Companies Act.<sup>76</sup> When it comes to the supervision of the banking industry in South Africa, there are basically three main role-players, namely the Registrar of Banks, the Reserve Bank and the Financial Services Board. The Financial Services Board, for example, plays an important role in the case of a bank or insurance company being placed under curatorship.

The provisions in the 1990 Banks Act dealing with winding-up and curatorship are far more refined than the previous provisions that appeared in the 1942 and 1965 banking legislation and, due to their relevance to the current discussion, will be dealt with here in detail. It is also interesting to note that these provisions (dealing with winding-up and curatorship) were recently

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<sup>73</sup> S 32(6).

<sup>74</sup> S 32(5) and (8). For examples of how this was applied in practice, see *Lindsay Keller & Partners v AA Mutual Insurance Association Ltd* 1988 2 SA 519 (W) and *Ex parte Wells: In re African Horizon Insurance Co Ltd (in liquidation)* 1963 2 SA 419 (C).

<sup>75</sup> Hereinafter referred to as the 1990 Banks Act.

<sup>76</sup> For an example of the difficulties involved in applying the various provisions of the 1965 Banks Act, the 1990 Banks Act and the Companies Act, see *Alpha Bank Bpk v Registrateur van Banke* 1996 1 SA 330.

amended,<sup>77</sup> providing the relevant authorities with even more say in the manner that banks are wound up.

Section 68 of the 1990 Banks Act deals with winding-up,<sup>78</sup> and basically provides for the following:

- (a) The Registrar (of Banks) has the right to apply for the winding-up of any bank;<sup>79</sup>
- (b) The Registrar has the right to oppose the application for the winding-up of any bank by any other person;<sup>80</sup>
- (c) No person other than a person recommended by the Registrar may be appointed by the Master as provisional or final liquidator of a bank;<sup>81</sup>
- (d) The Master must appoint a person designated by the Registrar to assist the provisional or final liquidator, and such person must be someone who, in the opinion of the Registrar, has experience and knowledge of the banking industry;<sup>82</sup>
- (e) The appointment of a person to assist the liquidator must be done by way of a letter in which is set out the name of the bank in respect of which the appointment has been made,

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<sup>77</sup> See ss 9 and 10 of the Banks Amendment Act 36 of 2000.

<sup>78</sup> In terms of s 3 of the Companies Act, its provisions do not apply to a bank.

<sup>79</sup> S 68(1)(a) of the 1990 Banks Act.

<sup>80</sup> S 68(1)(a) of the 1990 Banks Act.

<sup>81</sup> S 68(1)(b) of the 1990 Banks Act.

<sup>82</sup> S 68(1)(c) of the 1990 Banks Act.

any directions in regard to such person's remuneration and any other directions as the Master or Registrar may have seen fit to issue. The Master must send a copy of such a letter of appointment to the provisional or final liquidator concerned;<sup>83</sup>

- (f) If a bank is being wound up voluntarily, the liquidator has to furnish the Registrar with any returns or statements which the bank would have been obliged to furnish if it was not being wound up;<sup>84</sup>
- (g) In any application for the winding-up of a bank by the court,<sup>85</sup> the Registrar, in addition to the Master, must be served with the necessary application and of every affidavit submitted in support thereof;<sup>86</sup>
- (h) In any application for the winding-up of a bank by the court, the Registrar, in addition to the Master, may report to the court any facts ascertained by him which appear to him to justify the court in postponing the hearing or dismissing the application;<sup>87</sup>
- (i) In the case where a company which is a bank is being wound up voluntarily, a copy of the special resolution and of every order of court amending or setting aside any proceedings in relation to a winding-up, must be furnished to the Registrar;<sup>88</sup>

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<sup>83</sup> S 68(1A)(a)-(c) of the 1990 Banks Act.

<sup>84</sup> S 68(2) of the 1990 Banks Act.

<sup>85</sup> In terms of s 346 of the Companies Act.

<sup>86</sup> S 68(3)(a) of the 1990 Banks Act.

<sup>87</sup> S 68(3)(a) of the 1990 Banks Act.

<sup>88</sup> S 68(3)(b) of the 1990 Banks Act.

- (j) Provisions relating to the effect of the suspension, cancellation or termination of the registration of a bank as a result of an application brought by the Registrar.<sup>89</sup>

From these provisions it is quite evident that the liquidation or winding-up of a bank still takes place in terms of the rules relating to insolvency. All that the provisions in the Banks Act seek to achieve is the addition of the Registrar of Banks as a party to the proceedings, and the addition of a few administrative regulatory matters. In other words, the winding-up provisions contained in the Banks Act are merely procedural in nature, and do not detract from the substantive law that regulates winding-up generally. It is for this reason that I am of the opinion that these provisions should be included in a unified insolvency statute.<sup>90</sup>

However, a unified insolvency statute cannot, and should not, regulate any attempt at rescuing a bank or insurance company experiencing financial difficulties. For example, the section<sup>91</sup> dealing with the placing of a bank under curatorship should not be included in a unified insolvency statute, and it is submitted that these provisions should remain in the Banks Act.<sup>92</sup>

### **3 5 Current position in regard to the insurance industry**

Insurance legislation in South Africa was recently overhauled to the extent that two new pieces of insurance legislation, namely the Long-Term Insurance Act and the Short-Term Insurance Act, were promulgated in 1998.<sup>93</sup> These Acts contain identical provisions in regard to winding-up and

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<sup>89</sup> S 68(5) of the 1990 Banks Act.

<sup>90</sup> The aspects mentioned in paras (a) to (j) above can quite easily be addressed in a unified insolvency statute, as will be illustrated in par 4.4 below.

<sup>91</sup> Ss 69 and 69A of the 1990 Banks Act.

<sup>92</sup> Although a unified insolvency statute will also provide for business rescue, it is submitted that due to the specialised nature of banks and insurance companies, these provisions should remain in the enabling legislation. Another factor that influences such a submission, is that the Financial Services Board (FSB) has jurisdiction in the case of a bank being placed under curatorship. In order to effectively exercise its authority, the provisions will probably be better utilised in the Banks Act.

<sup>93</sup> Although promulgated in 1998, both these Acts only came into operation on 1 January 1999.

judicial management, and consequently only the provisions of the Long-Term Insurance Act will be referred to here.

After the gradual intensification of the winding-up provisions contained in first the 1923 Insurance Act,<sup>94</sup> and then the 1943 Insurance Act,<sup>95</sup> it is rather surprising to see how the provisions in the 1998 Act have been toned down to just a few basic principles that have to be applied in the case of an insurance company being wound up.

Part VI of the Long-Term Insurance Act provides for the “Judicial Management and Winding-up of Long-Term Insurers”. Section 41 deals with judicial management, section 42 with the winding-up of an insurer by the court and section 43 with voluntary winding-up. In regard to the winding-up of an insurance company by the court, the following principles apply:

- (a) The Registrar (of Insurance Companies) is deemed to be a person authorised by section 346 of the Companies Act to bring an application for the winding-up of an insurance company;<sup>96</sup>
- (b) The Registrar may bring such an application only with the permission of the relevant Minister, and then only when he is satisfied that it would be in the best interests of the policy-holders to do so;<sup>97</sup>

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<sup>94</sup> See par 3.3.1 above.

<sup>95</sup> See par 3.3.2 above.

<sup>96</sup> S 42(1) of the Long-Term Insurance Act.

<sup>97</sup> S 42(2) of the Long-Term Insurance Act.

- (c) When deciding whether it is just and equitable that an insurance company be wound up, the additional question that has to be asked by the court is whether it will be in the interests of the policy-holders to do so;<sup>98</sup>
- (d) Certain references to the provisions of the Companies Act dealing with winding-up must include a reference to the Registrar of Insurance Companies;<sup>99</sup>
- (e) Where application is made for the winding-up of a company by someone other than the Registrar,
  - (i) the application cannot be heard unless the application and all documents are also served on the Registrar at least 15 days before the application is set down for hearing;<sup>100</sup> and
  - (ii) the Registrar may oppose the application if he is convinced that the application is not in the interests of the policy-holders.<sup>101</sup>

Although this aspect falls beyond the scope of this study, it would appear that section 43, which provides for the voluntary winding-up of an insurance company, only makes provision for an insurance company to be wound up voluntarily as a voluntary winding-up by members.<sup>102</sup>

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<sup>98</sup> S 42(3)(b) of the Long-Term Insurance Act.

<sup>99</sup> S 42(3)(d) of the Long-Term Insurance Act.

<sup>100</sup> S 42(4)(a) of the Long-Term Insurance Act.

<sup>101</sup> S 42(4)(b) of the Long-Term Insurance Act.

<sup>102</sup> S 43(a) of the Long-Term Insurance Act states that the company must make satisfactory arrangements to meet all the liabilities of the long-term insurer under long-term policies entered into it prior to the winding-up. This is hardly likely to be possible in the case of a voluntary winding-up by creditors, which may be used where the company is insolvent.

## **4 PROPOSALS FOR THE INCLUSION OF SPECIALISED INSTITUTIONS UNDER A UNIFIED INSOLVENCY STATUTE**

### **4 1 Introduction**

As mentioned above,<sup>103</sup> the protection of specialised institutions is necessary for the protection of the public interest and, in some cases, for the protection and stability of financial markets. However, it is submitted that the same protection which is currently enjoyed by these institutions can be built into a unified insolvency statute. As pointed out above, there was one symposium and one conference which preceded a report on a unified Insolvency Act held at the University of Pretoria. Not only did the subject of including banks, insurance companies and the like in the unified proposals spark a heated debate at these events, but it was also one of the most problematic aspects of the report on a unified Insolvency Act.<sup>104</sup> Not only does this problem strike at the very core of the philosophy relating to the liquidation of these types of entities, but it is also a political issue that needs to be approached with the utmost caution and sensitivity.

At the heart of the debate lies the question as to whether certain institutions, the winding-up and judicial management of which currently take place under separate governing legislation, should be included under proposals for a unified Insolvency Act. The decision to exclude or include such provisions would appear to be one of policy. Many objections were made in respect of including the provisions currently contained in separate legislation, for example in the Banks Act or the Long-Term Insurance Act, in a unified statute.<sup>105</sup> It has been argued that the institutions which currently enjoy protection in terms of special legislation require this protection in the public interest and, in certain cases, for the protection and stability of the financial markets. From this one can only adduce that the protagonists for the retention of the special provisions in the

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<sup>103</sup> See par 2 above.

<sup>104</sup> See paras 3.1-3.18 Final Report Vol 1.

<sup>105</sup> This was the case at the conference held on 6 Oct 1999. See eg the submissions made by Grobler of the Reserve Bank, Conference Transcriptions 28-32.



governing legislation believe that this is the only way in which the public interest can be protected.

After having studied the provisions concerned in the relevant Acts, it is submitted that there can be no danger that the protection of the public interest will be compromised by including the liquidation of these institutions in a unified insolvency statute. Most of the provisions in question relate to preventing simply any person from bringing an application to liquidate a bank or insurance company which would, quite obviously, result in potential chaos. In addition, these provisions require a person with the requisite expertise to act as liquidator. However, the powers of the registrars concerned need not be compromised by including the (currently separate) provisions in a unified piece of legislation. In a nutshell, the unification process is not intended to take away the powers of any governing authority over its charge, but merely to provide for uniform procedures *once the institution in question has in fact been placed in liquidation*.

The powers that have currently been conferred on the governing authorities in respect of these specialised institutions will clearly have to be retained, in whatever form, in proposals for unified insolvency legislation. This would be necessary not only in order to protect the public interest, but also for the purpose of good administration. It is, however, submitted that the same objectives can be attained by including these provisions in unified insolvency legislation. Separate provisions create uncertainty and suspicion, especially at a time when transparency is of paramount importance. The inclusion of these provisions in the unified proposals would create legal certainty for all concerned, and would facilitate the effective administration of (all) insolvent estates. An additional advantage of including these provisions in a unified statute, would be the fact that the liquidation of banks and other institutions would be far less complicated to administer than they currently are.

As pointed out above, the intention here is only to include the provisions relating to liquidation and does not influence any other provisions contained in the governing legislation, for example

where an institution is placed under curatorship.<sup>106</sup> With this as background, it is submitted that an attempt should be made to include all types of institutions in a unified insolvency statute. An initial attempt at incorporating the separate provisions as they currently appear in the governing legislation, was a dismal failure.<sup>107</sup> The provisions are simply just too long, and drafting separate provisions for each type of institution based on the current legislation resulted in a clumsy and awkward chapter dealing with these special provisions. The proposals reflected below therefore reflect an attempt at drafting a blanket-clause which could apply in the case of all specialised institutions.

However, before this is attempted, the treatment of specialised institutions in other jurisdictions first needs to be examined. From an international<sup>108</sup> perspective Patrikis,<sup>109</sup> the First Vice President of the Federal Reserve Bank of New York, is of the opinion that the problem surrounding the liquidation of banks, is what he defines as “systemic risk”. He states it thus at 283:

“Banks are a pivotal part of the domestic and international payments system. Bank insolvencies entail systemic risks which are absent in the bankruptcy of most commercial concerns.”

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<sup>106</sup> See ss 69 and 69A of the 1990 Banks Act.

<sup>107</sup> See paras 3.1-3.18 Final Report Vol 1.

<sup>108</sup> For a more detailed exposition of international trends regarding the liquidation and regulation of banks, see Giovanoli and Heinrich (eds) *International Bank Insolvencies: A Central Bank Perspective* (1999) and Walker *International Banking Regulation: Law, Policy and Practice* (2001).

<sup>109</sup> Patrikis “Role and Functions of Authorities: Supervision, Insolvency Prevention and Liquidation” in Giovanoli and Heinrich (eds) *International Bank Insolvencies: A Central Bank Perspective* (1999) 283 (hereinafter referred to as Patrikis). This paper was delivered at a workshop on international bank insolvencies held in 1998.

“Systemic risk” is then defined as

“the risk that a disturbance in financial markets might seriously harm the financial position of financial firms, which could in turn threaten to disrupt the payments system and the capacity of the international financial system to allocate capital”.<sup>110</sup>

Patrikis therefore sees the function of the commercial law of banks as ensuring the integrity of the payments system.<sup>111</sup> He further points out that while non-bank insolvency is dominated by two main goals, namely the fair treatment of all creditors and the maximisation of the value of the estate, bank insolvency contains a third goal, namely the reduction of systemic risk.<sup>112</sup> Patrikis further points out that most countries treat the insolvency of banks differently than ordinary commercial insolvencies. As an example he points out that in the United States insolvency proceedings under the Bankruptcy Code differ from proceedings under the bank liquidation schemes in the following critical areas:<sup>113</sup>

- (a) Initiation of proceedings.
- (b) Administration of the estate.
- (c) Reorganisation.
- (d) Liquidity.

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<sup>110</sup> Patrikis 283.

<sup>111</sup> Patrikis 283.

<sup>112</sup> Patrikis 283-284.

<sup>113</sup> This is also the case under South African law. See par 3.4 above.

There are also important differences in the treatment of impeachable transactions where, in the case of banks, banking insolvency law would be less willing to reverse non-fraudulent transfers.<sup>114</sup>

While there is no doubt that the effect of the liquidation of a bank differs from the liquidation of other commercial concerns, Patrikis unfortunately does not state whether these institutions can *only* be protected by including the provisions in separate legislation. As pointed out above, it is *only* the liquidation process itself which is sought to be included in a unified insolvency statute, not other preceding proceedings such as the placing of a bank under curatorship in order to ensure its continued existence, or the protection of the financial markets. Patrikis himself recognises that there can be various stages in the gradual demise of a financial institution, ending in its possible liquidation:

“If insolvency authorities are morticians, supervisory authorities are the doctors. And often supervisory and insolvency authorities are one and the same. This suggests that bank insolvency is the end-stage of a continuous process, which begins with bank supervision, proceeds to workouts of distressed institutions, and terminates with insolvency.”<sup>115</sup>

By including banks and other institutions in a unified insolvency statute, it is the latter part of the process which one is seeking to address, not the initial or intermediate stages of supervision which would, in terms of the enabling legislation, be supervised by the governing body of the institution concerned.

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<sup>114</sup> Patrikis 285. The point is made that financial contracts are much more difficult to avoid than ordinary transfers. Under South African insolvency law special provision has been made for the avoidance of financial transactions: s 35A of the Insolvency Act deals with transactions on an exchange and s 35B deals with agreements on informal markets. The provisions in question basically provide that a trustee cannot avoid certain transactions, and may be bound to certain transactions that result in netting or set-off.

<sup>115</sup> At 285.

With this as background, it is interesting to note how banks (and other specialised institutions<sup>116</sup>) are treated in the United States and England.

#### **4 2 The liquidation of banks (and other specialised institutions) in the United States of America<sup>117</sup>**

The definition of “debtor” under the United States Bankruptcy Code<sup>118</sup> expressly excludes banks, savings banks, co-operative banks, savings and loan associations, building and loan associations, homestead associations, credit unions, industrial banks or similar institutions which are insured banks as defined in section 3(h) of the Federal Deposit Insurance Act.<sup>119</sup> Consequently, the insolvency law applicable to commercial banks in the United States is “an entirely different body of law from that applicable to other commercial enterprises”.<sup>120</sup> The reason for this is that domestic banks in the United States are subject to the liquidation provisions of the applicable federal and state banking laws.<sup>121</sup>

When it comes to the supervision of banks in the United States, there are various regulatory authorities which exercise control. These are: the Federal Reserve Board (FRB), the Treasury Department’s Office of the Comptroller of the Currency (OCC), the Federal Deposit Insurance

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<sup>116</sup> For a detailed discussion of the liquidation of insurance companies in other jurisdictions, see Moss (ed in chief) *et al Cross-Frontier Insolvency of Insurance Companies* (2001) especially par 1 (United Kingdom), par 2 (USA), par 4 (Australia) and par 14 (Germany).

<sup>117</sup> See generally Mattingly, Misback, Milenkovich, Hansen and Sommer “International Bank Insolvencies: A Central Bank Perspective” 1998 12 *International Banking, Finance and Economic Law* 259 (hereinafter referred to as Mattingly *ea*).

<sup>118</sup> 11 USC s 109(b)(2) and (d). See also Herbert *Understanding Bankruptcy* (1995) 78-79.

<sup>119</sup> 12 USC (1989).

<sup>120</sup> Mattingly *ea* 259. However, if the bank is a foreign bank that does not have a branch or agency in the United States, it may be liquidated in terms of the United States Bankruptcy Code - Mattingly *ea* 259.

<sup>121</sup> Mattingly *ea* 259.

Corporation (FDIC) and the Office of Thrift Supervision (OTS).<sup>122</sup> All the aforementioned are at federal level, and work in co-operation with state banking agencies at state level. The purpose of these federal and state supervisory and regulatory authorities is to ensure the continuous safety and soundness of banking institutions and stability in the financial markets.<sup>123</sup>

The reason that the liquidation of banks is treated separately from other commercial enterprises becomes clear when one looks at the framework for the liquidation of banks generally in the United States.<sup>124</sup> The liquidation of a bank depends largely on such bank's charter and license.<sup>125</sup> Where a bank has been licensed by a state, liquidation is subject to that state's law. However, where a bank has been licensed by the OCC, federal liquidation law is applicable to the liquidation of such a bank.<sup>126</sup>

In the case of a national bank, the OCC has the authority to determine whether such bank is insolvent.<sup>127</sup> The OCC also has the right to appoint a receiver to wind up the bank, and in the case of an insured national bank, the OCC must appoint the FDIC as receiver.<sup>128</sup> In the case of banks that have been licensed by a particular state, the state banking laws generally find application to the liquidation of such banks.<sup>129</sup> Examples are the New York banking law and the laws that find application in the state of California.<sup>130</sup>

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<sup>122</sup> Mattingly *ea* 260.

<sup>123</sup> Mattingly *ea* 260.

<sup>124</sup> Mattingly *ea* 262.

<sup>125</sup> Mattingly *ea* 262.

<sup>126</sup> Mattingly *ea* 262-263.

<sup>127</sup> Mattingly *ea* 262-263.

<sup>128</sup> Mattingly *ea* 262-263.

<sup>129</sup> Mattingly *ea* 264-265.

<sup>130</sup> Mattingly *ea* 264-265.

In South Africa, as opposed to the United States, banking law is governed centrally and not by provincial legislation. Consequently all legislation applicable to banks is governed by central government, allowing the provisions that apply to all banks to be the same throughout the Republic. By allowing states to govern their own (state) banking, the United States is unable to regulate the liquidation of all banks by means of central (federal) government laws. This inherent difference distinguishes the liquidation of banks in South Africa from the liquidation of banks in the United States.

#### **4 3 The liquidation of banks (and other specialised institutions) in England<sup>131</sup>**

Contrary to the position in the United States, under English law “banks are subject to insolvency and liquidation provisions that are essentially the same as for all other commercial companies”.<sup>132</sup> However, English law does contain special provisions<sup>133</sup> dealing with the liquidation of a bank which are very similar to the provisions that currently prevail in South Africa.<sup>134</sup>

The supervision of the banking industry in England recently passed from the Bank of England to the Financial Services Authority (FSA).<sup>135</sup> However, in terms of a Memorandum of Understanding (MOA) between the UK Treasury, the Bank of England<sup>136</sup> and the FSA entered into on 28 October 1997, a framework was created for co-operation between these bodies in

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<sup>131</sup> See generally Beaves “International Bank Insolvencies: A Central Bank Perspective” 1998 12 *International Banking, Finance and Economic Law* 237 (hereinafter referred to as Beaves).

<sup>132</sup> Beaves 237. However, while this is the case in respect of banks, the winding-up of an insurance company is effected by means of provisions contained in separate legislation - Beaves 237.

<sup>133</sup> Beaves 237-238.

<sup>134</sup> See par 3.4 above.

<sup>135</sup> Beaves 238.

<sup>136</sup> For an example of an application for the winding-up of a bank by the Bank of England, see *Re Bank of Credit and Commerce International SA* [1992] BCC 83.

order to ensure financial stability.<sup>137</sup> This is similar to the situation in South Africa where the Reserve Bank and the Financial Services Board function in tandem.

Where a bank is liquidated or wound up in terms of English law, it would appear that the FSA is limited to presenting a petition to the High Court for the winding-up of an “authorized institution” on the ground that it is unable to pay its debts within the meaning of section 123 of the English Insolvency Act 1986, or on the ground that it is just and equitable that the institution in question be wound up.<sup>138</sup> In addition to this, the FSA must also be notified of any petition for the winding-up of an authorised institution by any other person, or be provided with notice of any meeting at which a resolution for its winding-up will be considered.<sup>139</sup>

Subject to certain limitations regarding ongoing monitoring powers, the FSA has no authority over the liquidator once he or she has been appointed.<sup>140</sup> After the appointment of a liquidator, such a person is subject to the control of the court, and not the FSA.<sup>141</sup> It is not clear whether the FSA has the right to insist on a liquidator (or co-liquidator) with the requisite knowledge of the banking industry, but in light of the United Kingdom’s system of licensed practitioners, it is unlikely that this will ever be problematic in England.

To summarise, in England banks and other specialised institutions (except for insurance companies) are not dealt with any differently than other commercial entities. The only protection that is granted to the banking industry is certain procedural requirements similar to, but not as stringent as, those currently applicable in South Africa.

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<sup>137</sup> Beaves 238-239.

<sup>138</sup> Beaves 240. See s 92 of the Banking Act 1987.

<sup>139</sup> Beaves 237.

<sup>140</sup> Beaves 240.

<sup>141</sup> Beaves 240.



#### 4 4 Proposed new provisions dealing with specialised institutions in South Africa

In order to achieve an insolvency statute that is truly unified, it is proposed that a separate chapter dealing with the insolvency of these institutions can be built into a unified Insolvency Act. The proposed chapter and sections dealing with the insolvency of these institutions could be framed as follows:

##### “CHAPTER 3 - SPECIAL PROVISIONS APPLICABLE TO SPECIFIC DEBTORS

**9. Special provisions relating to the liquidation of certain debtors.** (1) If a debtor which has been, or is in the process of being liquidated in terms of the provisions of this Act is:

- (a) a long-term insurer as defined in section 1 of the Long-Term Insurance Act 52 of 1998, or a short-term insurer as defined in section 1 of the Short-Term Insurance Act 53 of 1998, or
- (b) a bank as defined in section 1 of the Banks Act 94 of 1990; or
- (c) a mutual bank as defined in section 1 of the Mutual Banks Act 124 of 1993; or
- (d) a pension fund as defined in section 1 of the Pension Funds Act 24 of 1956; or
- (e) a financial exchange as defined in section 1 of the Financial Markets Control Act 55 of 1989; or
- (f) a medical scheme as defined in section 1 of the Medical Schemes Act 72 of 1967; or
- (g) a management company as defined in section 1 of the Unit Trusts Control Act 54 of 1981; or
- (h) a co-operative as defined in section 1 of the Co-operatives Act 91 of 1981; or
- (i) a friendly society as defined in section 1 of the Friendly Societies Act 25 of 1956,

the provisions of this section must be applied when applying this Act to such a debtor.

(2) In the application for the liquidation of a debtor as referred to in paragraphs (a) to (i) of subsection (1), the registrar of such debtor shall be deemed to be a person authorised by section 4 to make an application to the court for the liquidation thereof.

(3) The registrar of any debtor as referred to in paragraphs (a) to (i) of subsection (1), may with the written consent of the Minister responsible for the administration of such debtor, make an application under section 4 for the liquidation of such a debtor if he or she is satisfied that it is in the interests of the beneficiaries or creditors of such debtor to do so.

(4) In any sections of this Act-

- (a) any reference to the Master in respect of notice being given, shall be construed as a reference also to the registrar of the debtor concerned;
- (b) any reference to the Registrar of Companies shall be construed as a reference also to the registrar of the debtor concerned.

(5) If an application to the court for or in respect of the liquidation of a debtor as referred to in paragraphs (a) to (i) of subsection (1) is made by any other person than the registrar of the debtor concerned-

- (a) it shall not be heard unless copies of the notice of motion and of all accompanying affidavits and other documents filed in support of the application are lodged with the registrar of such debtor at least 15 days, or such shorter period as the court may allow on good cause shown, before the application is set down for hearing; and
- (b) the applicant concerned shall not, at any time before the application is set down for hearing, make public or cause to be made known to any person other than the registrar concerned, his or her intention to bring such an application, failing which the applicant shall be guilty of an offence and, on conviction, shall be sentenced to imprisonment for a period not exceeding X years, or a fine; and
- (c) if, for any reason, the registrar of the debtor concerned is satisfied that the application is contrary to the interests of such debtor or its beneficiaries, such registrar may join the application as a party and file affidavits and other documents in opposition to the application; and
- (d) in addition to any question whether it is just and equitable that the debtor should be wound up, there shall be considered also the question whether it is in the interest of the beneficiaries or other stakeholders of that debtor that it should be wound up.

(6) No liquidation resolution relating to the liquidation of a debtor referred to in paragraphs (a) to (i) of subsection (1), as contemplated in section 8<sup>142</sup> or paragraph (d) of subsection (1) of section 4<sup>143</sup> of this Act, shall be registered by the Registrar of Companies in terms of section 200 of the Companies Act 61 of 1973, and no liquidation resolution to that effect in terms of the constitution of such a debtor which is not a company shall have legal force

- (a) unless a copy of the notice referred to in paragraph (b) in subsection (2) of section 8 has been lodged also with the registrar of the debtor concerned; or
  - (b) if the registrar of such debtor, by notice to the debtor, declares that the resolution is contrary to an appropriate legislative provision which prohibits the adoption of such resolution.
- (7) (a) Notwithstanding the provisions of the Companies Act 61 of 1973 or any other law under which a debtor as referred to in paragraphs (a) to (i) of subsection (1) has been incorporated, Chapter 24 of this Act shall, subject to this subsection and with the necessary changes, apply in relation to the judicial management of such a debtor, whether or not it is a company, and in such application the registrar of the debtor concerned shall be deemed to be a person authorised by section 4 of this Act to make an application to court for the liquidation thereof.
- (b) The registrar of the debtor concerned may make an application under Chapter 24 of this Act for a judicial management order, in respect of such a debtor if he or she is satisfied that it is in the interests of the debtor or the beneficiaries of such debtor to do so.
  - (c) If an application to the court for the judicial management of a debtor as referred to in paragraphs (a) to (i) of subsection (1), is made by any other person than the registrar of the debtor concerned-
    - (i) it shall not be heard unless copies of the notice of motion and of all accompanying affidavits and other documents

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<sup>142</sup> Cl 8 refers to voluntary liquidations by resolution.

<sup>143</sup> Cl 4 refers to applications for liquidation by corporate debtors.

- filed in support of the application are lodged with the registrar of the debtor concerned at least 15 days, or such shorter period as the court may allow on good cause shown, before the application is set down for hearing; and
- (ii) the registrar of the debtor concerned may, if satisfied that the application is contrary to the interests of the debtor or its beneficiaries, join the application as a party and file affidavits and other documents in opposition to the application.
- (d) As from the date on which a provisional or final judicial management order is granted in respect of a debtor as referred to in paragraphs (a) to (i) of subsection (1), any reference to such debtor shall, unless clearly inappropriate, be construed as a reference to the provisional or final judicial manager, as the case may be;
- (8) (a) Notwithstanding the provisions of this Act,
- (i) no person other than a person recommended by the registrar of a debtor as referred to in paragraphs (a) to (i) of subsection (1), shall be appointed by the Master as provisional liquidator, liquidator, provisional judicial manager or judicial manager, as the case may be, of any such institution; and
  - (ii) the Master shall appoint a person designated by the registrar of the debtor concerned, who shall be a person who in the opinion of the registrar concerned has wide experience of, and is knowledgeable about the latest developments in, the industry concerned, to assist a provisional liquidator, liquidator, provisional judicial manager or judicial manager referred to in paragraph (a) in the performance of his or her functions in respect of the institution in question.
- (b) The appointment by the Master of a person in terms of subsection (a)(ii) shall be by means of a letter of appointment addressed by the Master to the person appointed and in which is set out-
- (i) the name of the institution in respect of which such person is appointed;
  - (ii) directions in regard to the remuneration of the person appointed; and
  - (iii) such other directions incidental to the matter as the Master or the registrar of such debtor may deem necessary,
- and a copy of such letter of appointment shall be furnished by the Master to the provisional liquidator, liquidator, provisional judicial manager or judicial manager concerned.
- (9) During the voluntary liquidation by resolution in terms of section 8 of any debtor as referred to in paragraphs (a) to (i) of subsection (1) of this section, the liquidator shall furnish, if applicable, the registrar of the debtor concerned with such return or statement which the debtor concerned would have been obliged to furnish to such registrar in terms of any Act, were such debtor not being wound up, as such registrar may require.
- (10) The provisions of this section may not in any way be amended or changed without prior consultation with, and written approval of such changes by, the Minister responsible for the administration of a debtor as referred to in paragraphs (a) to (i) of subsection (1).”

## **4 5 Explanation of provisions**

### *4 5 1 To whom do the provisions apply?*

Clause 9(1) merely identifies the institutions which are affected by the provisions contained in this chapter, with reference to the relevant governing legislation.<sup>144</sup>

### *4 5 2 Registrar may bring application*

Clause 9(2) includes the registrar of the institution concerned as one of the persons who may bring an application for the liquidation of a debtor in terms of clause 4, which is basically a retention of the *status quo*.

### *4 5 3 Registrar may only bring application if authorised to do so*

Clause 9(3) is linked to clause 9(2), in that the relevant registrar may only bring such an application (in terms of clause 4) if he or she has been authorised to do so by the Minister responsible for the administration of the relevant institution.

### *4 5 4 Notice to registrar*

Clause 9(4) has been included to ensure that the registrar of the relevant institution also receives notice of information which has to be supplied to the Master. This is necessary to ensure that the registrar concerned can also exercise other important powers which have been conferred upon him or her elsewhere in the clause.

### *4 5 5 Protection of the public interest*

Clause 9(5) is of paramount importance in the protection of the public interest. One of the greatest fears of the governing bodies of the institutions already referred to, is that someone other than the registrar would be able to bring an application for the liquidation of the debtor, without the registrar being aware of the application, or being powerless to do anything about preventing the application from being made, and subsequently granted.

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<sup>144</sup> These are the same as those that currently enjoy special treatment - see par 2 above.

Paragraph (a) ensures that the registrar concerned has in fact been notified, without which prior notification the court may not grant the order. Paragraph (b) is intended to prevent an applicant who is bringing an application from making public the fact that an application is to be brought. Failure to comply with this requirement results in the commission of an offence. Paragraph (c) allows the registrar to join the application as a party and to file opposing affidavits in respect of the application. The governing bodies therefore retain control over the process leading up to the application being heard by the court. Paragraph (d) ensures that the court will also consider the interests of the various stakeholders<sup>145</sup> of the debtor before granting a liquidation order.

#### *4 5 6 Voluntary liquidation*

Clause 9(6) prevents a relevant institution from entering into a voluntary liquidation by resolution without the prior knowledge of the registrar concerned. This is achieved by preventing the registration of the resolution unless notice of the resolution has also been given to the registrar, or if the registrar has informed such institution that the adoption of the resolution is prohibited.

#### *4 5 7 Judicial management*

Clause 9(7) makes judicial management applicable also to the institutions listed in clause 9(1). Paragraph (b) entitles the registrar of the relevant institution to make an application for the judicial management of the relevant institution.

Paragraph (c) provides for sufficient notice to be given to the relevant registrar in cases where the application for judicial management is brought by someone other than the registrar concerned. In this case also the registrar is entitled to join the application as a party and to file opposing affidavits.

#### *4 5 8 Appointment of specialist as liquidator or judicial manager*

Clause 9(8) has been inserted to ensure that a person with the necessary expertise will be appointed to liquidate or judicially manage the relevant specialised institution. This subsection

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<sup>145</sup> Eg the policy-holders of an insurance company.

also provides for the appointment of a person to assist the liquidator or judicial manager with the liquidation of a specialised institution.<sup>146</sup> The Master must therefore appoint as liquidator or judicial manager a person recommended by the relevant registrar.<sup>147</sup> In addition, the Master must also appoint someone designated or nominated by the registrar of the debtor concerned, to assist the liquidator in the performance of his or her functions.

#### *4 5 9 Submission of returns and information*

Clause 9(9) has been inserted to ensure that the relevant returns and statements which may be required to be furnished by law,<sup>148</sup> are still furnished to the relevant registrar at a time when the debtor concerned is being wound up voluntarily.

#### *4 5 10 Amendment*

Clause 9(10) is intended to address the problem of amendment to the provisions contained in a unified Insolvency Act. The unified insolvency legislation will probably fall under the control of the Ministry of Justice and Constitutional Development, while the administration of the specialised institutions will probably fall under the auspices of a different ministry.<sup>149</sup> By inserting a peremptory consultation clause, the Ministry of Justice and Constitutional Development is prevented from amending the legislation without prior consultation with other ministries. Of course this provision only applies to the amendment of section 9, and does not effect amendment to the remainder of the legislation.

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<sup>146</sup> This is in accordance with s 68(1A) of the 1990 Banks Act.

<sup>147</sup> At the conference held on 6 Oct 1999, Calitz of the Master of the High Court (Pretoria) requested that this sub-clause be extensively formulated to exclude the possibility of misinterpretation in the appointment of liquidators (see the Conference Transcriptions 20). The clause has been drafted accordingly.

<sup>148</sup> Eg in terms of the 1990 Banks Act.

<sup>149</sup> Eg banks fall under the Ministry of Finance and not under the Ministry of Justice and Constitutional Development.

## 5 CONCLUSION

From the above discussion and the subsequent proposed insertion of a clause dealing with the liquidation of specialised institutions, it is evident that specialised institutions can quite effectively be accommodated within the framework of a unified insolvency statute. Instead of duplicating an excessive number of clauses in each specialised Act which provide for essentially the same circumstances, it appears far more sensible to provide for the relatively few key aspects that provide for the protection of the public interest.<sup>150</sup>

As suggested, however, it is submitted that in order to achieve effective supervision over distressed banks and other specialised institutions, it is necessary to retain, in the enabling legislation, provisions that provide for the possible recovery of such institutions under the auspices of the necessary authorities.

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<sup>150</sup> Stated differently, all legislation that requires the participation of the Master of the High Court as supervisor of the administration process, should be included under one Act.