

**Moving towards a unified approach for the winding-up  
of companies in view of the "Repealed" chapter 14 of  
the Companies Act 61 of 1973**

Submitted in partial fulfillment of the requirement for the  
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**Ashika Hasmukhlal Nichha**

**10123084**

Prepared under the supervision of

**Prof. A Boraine**

At the University of Pretoria

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## Summary

The new Companies Act 71 of 2008 came into effect on 1 May 2011 repealing the Companies Act of 1973. The 2008 Companies Act retained provisions relating to the winding-up of insolvent companies, in particular Chapter 14. It is submitted that even though the 1973 Companies Act has been repealed and only Chapter 14 has been retained for the winding-up of insolvent companies, Chapter 14 cannot be applied in isolation without considering the provisions relating to the winding-up of insolvent companies that fall outside the ambit of Chapter 14 of the 1973 Companies Act. This research proposes a unification of provisions relating the winding-up of both solvent and insolvent companies in a single piece of legislation.

Chapter 1 introduces the dissertation. Chapter 2 consists of a brief overview of the development of corporate law in South Africa. Chapter 3 will focus on a descriptive and comparative approach illustrating between single and dual systems, specifically those in between the USA and England, as well as discuss the advantages and disadvantages of the systems. Chapter 4 contains a discussion on the relationship between the 1973 and 2008 Companies Acts in view of their respective liquidation proceedings of insolvent companies. Chapter 5 consists of an analysis of the Draft Bill Proposals in context of a unified bill and corporate legislation. Lastly, Chapter 6 will draw conclusions.

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I am grateful to my parents for encouraging me and having faith in me.

## Declaration of Originality

Full name of student: Ashika Hasmukhlal Nichha

Student number: 10123084

### Declaration

I understand what plagiarism is and am aware of the University's policy in this regard.

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## Abbreviations

Companies Act 61 of 1973; Companies Act 1973; old Companies Act or 1973 Companies Act

The Companies Act 71 of 2008; the new Companies Act 2008; the new Companies Act; 2008 Companies Act

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## Chapter 1: Introduction

### **1. General background**

South African insolvency law, to some extent is based on Roman-Dutch law origins<sup>1</sup> but English bankruptcy law played a significant role in shaping South African insolvency law.

South Africa does not have a single unified insolvency legislation which means that the sources of insolvency law are to be found in various pieces of legislation, common law principles and precedent. The main sources for South African insolvency include the Insolvency Act 24 of 1936, which deals specifically with insolvency for individuals; the Companies Act 71 of 2008, together with parts of the Companies Act 1973, and the Close Corporations Act of 1984 which deal with corporate insolvency. Furthermore, there is other legislation applicable relating to the winding-up of other legal entities, such as banks and insurance companies.<sup>2</sup> Also applicable are statutory enactments, judgments of the High Courts and the Constitutional Court.

Corporate insolvency in South Africa is covered by separate legislation. The main reason is that companies are separate juristic persons having their own legal personalities and characteristics distinct from individuals. The development of company law in South Africa can be traced back to the 19<sup>th</sup> Century: <sup>3</sup> company law in South Africa originates in English law.<sup>4</sup> Until 2011, the Companies Act 1973 provided for the winding-up of insolvent companies and solvent companies.

The new Companies Act 71 of 2008 came into effect on 1 May 2011 repealing the Companies Act, 1973.<sup>5</sup> The 2008 Companies Act retained provisions relating to the

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<sup>1</sup> Amsterdam Ordinance of 1777.

<sup>2</sup> These include section 68 of the Banks Act 94 of 1990 and part VI of the Long Term Insurance Act of 1998 respectively.

<sup>3</sup> See Burdette "Framework for Corporate Insolvency Law Reform in South Africa" (2002) LLD Thesis, University of Pretoria at 21: "Prior to this, South African common law only made provision for individuals and the only form of business enterprise at the time, namely the partnership."

<sup>4</sup> See Cilliers and Benade *Corporate Law* (2000) 21 "The Cape Joint Stock Companies Limited Liabilities Act 1861 was the first company legislation in South Africa and an almost verbatim adoption of the English Joint Stock Companies Act of 1844 and the Limited Liability Act of 1855..."

<sup>5</sup> General Notice 421 Government Gazette 32121(9 April 2009).



winding-up of insolvent companies, in particular Chapter 14.<sup>6</sup> It is submitted, though the 1973 Companies Act has been repealed and only Chapter 14 has been retained for the winding-up of insolvent companies, Chapter 14 cannot be applied in isolation without considering the provisions relating to the winding-up of insolvent companies that fall outside the ambit of Chapter 14 of the 1973 Companies Act due to its wording.<sup>7</sup> It is a point of departure that the fragmentation of South African insolvency law calls for research with a view to consider the best approach to deal with this aspect in future. The fragmentation and related problems that existed prior to the enactment of the 2008 Companies Act, have been exacerbated by the still more fragmented approach since its enactment, since winding-up provisions relating to solvent and insolvent companies are now spread across different pieces of legislation. The 2008 Companies Act largely regulates the position relating to solvent companies and the 1973 Companies Act largely that of insolvent companies. It is submitted that this division has caused even greater fragmentation.

Other approaches will be considered: English insolvency law<sup>8</sup> and US bankruptcy law,<sup>9</sup> systems which have a single piece of legislation covering both personal and corporate insolvency. Both countries have successfully incorporated their respective insolvency laws in a distinctive manner, there are advantages and disadvantages to adopting a single statute.<sup>10</sup>

In the South African context the broader unification of legislation may not be an easy task considering our history of having various pieces of legislation. The unification of legislation may lead to easy accessibility of legislation, as well as convenience, but may also pose a challenge to insolvency practitioners overtime, who have adopted the traditional approach to insolvency law. The ultimate unification of personal and corporate insolvency may be a bold step in the South African insolvency context.

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<sup>6</sup> Cassim et al *Contemporary Company Law* 2012 at 913.

<sup>7</sup> Boraine and Van Wyk “ The application of “repealed” sections of the Companies Act 61 of 1973 to liquidation proceedings of insolvent companies” 2013 De Jure 647.

<sup>8</sup> Insolvency Act 24 of 1986.

<sup>9</sup> Bankruptcy Reform Act of 1987, also referred to as the Bankruptcy Code.

<sup>10</sup> Key “To unify or not to unify insolvency legislation: International Experience” 1999 De Jure 71.

Over a number of years there have been significant developments in insolvency law, not only in South Africa but globally. In 2000 the South African Law Reform Commission (SALRC) published a report which had drafted a Draft Insolvency Bill<sup>11</sup> and recommended that South Africa's individual and corporate insolvency should be contained in a single piece of legislation. The report and a Draft Insolvency Bill were completed by the Law Reform Commission but their efforts never came to fruition. As such, they did not contain the provisions dealing with corporate insolvency law. The Department of Justice later made available informal versions of a draft bill available following the 2000 Draft Bill with Commentary but its status is that of a working document, and it is not clear when legislation will be enacted.

## **2. Research Statement**

The research statement: the current fragmentation of South African insolvency law, especially as it relates to companies and to a lesser extent close corporations, gives rise to difficulties in applying the law and interpreting the law since there are now two sets of winding-up provisions in two pieces of legislation to work with. It is important to conduct research to consider various approaches to deal with this dual aspect.

The aims of the dissertation are: first, to consider whether it is advantageous to enact a single insolvency statute in view of the United States and English Insolvency systems. Second, to consider corporate insolvency in view of the fact that Chapter 14 of the 1973 Companies Act is applied, though the Act has been repealed by the 2008 Companies Act. Last, to consider and comment on the proposals contained in the Draft Insolvency Bill of 2015. Insolvency law reform, especially in South Africa, is not an easy task due to a history of differing legislation and, if unified legislation is to be enacted, these laws need to be well thought out and harmonized fully.

## **3. Limitation of Research**

The dissertation does not attempt to deal with the unification of personal and corporate insolvency law extensively, but rather proposes the unification of corporate insolvency legislation relating the winding-up of solvent and insolvent companies as such. It is

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<sup>11</sup> South African Law Reform Commission Report on the review of the law of insolvency (Project 63) Volume 1 (Explanatory Memorandum) and Volume 2 (Draft Bill) (Feb 2000).

conceded that such unification ultimately should take place within the broader context of a single insolvency act.

This initial aspect of unification might not be as drastic in effect as compared to the unification of the entire insolvency legislation, but may be a convenient means to provide more certainty and efficiency without the duplication and complication of legislation. In view of other jurisdictions there is a need for reform in South African insolvency to reflect not only the needs of society and the socio-economic values in South Africa, but also various trends, such as globalization, as a whole.

#### **4. Methodology**

Chapter 1 sets the scene for the research. Chapter 2 provides a brief overview of the development of corporate insolvency law in South Africa. The purpose of this chapter is to provide an understanding of how insolvency law, particularly corporate insolvency, developed in South Africa.

Chapter 3 gives an exposition of single and dual systems of enacting legislation and considers the advantages and disadvantages of a unified system of law. The systems in England and the USA will be considered.

In chapter 4, the duality of statutes that exists in South Africa in respect of companies will be discussed. In particular, some difficulties arising from the fragmented approach, exacerbated by the application of the Companies Act 61 of 1973 to the Companies Act 71 of 2008, will be discussed. In this regard, examples will be relied on to demonstrate the need for a new structure.

Chapter 5, will deal with the Draft Insolvency Bill of 2015, which proposes a unified and harmonized Insolvency Act. The main focus of this chapter will be to take cognizance of this unification effort in relation to the winding-up of companies, but, at the same time, to pose the question of what to do since this proposal is not ready to become law soon.

Finally Chapter 6 will draw conclusions and make proposals in view of the various approaches discussed in the dissertation.

## **Chapter 2: Historical Overview of the Development of Corporate Law in South Africa**

### **1. Introduction**

This chapter presents a historical overview of insolvency law and the development of corporate insolvency law in South Africa: it is important to understand the development of general insolvency law in South Africa. Previously, provision was made for consumer insolvency but: corporate insolvency developed much later, in 1926, as companies began to be viewed as separate legal persons distinct from natural persons. For purposes of this chapter it is sufficient to provide a brief overview of the historical roots of the South African legal system: it falls beyond the scope of this dissertation to give a detailed discussion of each aspect of the historical development of insolvency law.

### **2. Pre-Union Legislation**

The Pre-Union, in South Africa consisted of four entities, namely, the Republic Transvaal, the Cape Colony, Natal and the Orange Free State. Each was regulated by respective legislation which was applicable only to it.

The Cape Colony was the first to adopt company legislation in South Africa. The Cape Joint Companies Limited Liability Act, 1861<sup>12</sup> was an almost verbatim adoption of the English Joint Stock Companies Act, 1844 and the Limited Liability Act of 1855, both of which had been repealed by that stage.<sup>13</sup> Natal, the Transvaal and the Orange Free State followed the Cape Colony in enacting company law based on the English Acts.

### **3. Union Legislation**

The Parliament of the Union of South Africa in 1916 repealed the existing statute law of insolvency in the various provinces and substituted a uniform law of insolvency

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<sup>12</sup> Act 23 of 1861

<sup>13</sup> See Cilliers and Benade *et al Corporate Law* 21 and 23(hereafter referred to as Cilliers and Benade):"The Joint Stock Companies Act of 1844 was the first Act to allow incorporation in terms of a general enabling Act. Provision was only made for unlimited companies and personal liability was imposed on members for the debts of the company. This Act was repealed in 1856 and replaced by the Limited Liability Act of 1855, which accepted the unlimited liability of members as a given fact but created the machinery for the limitation of such liability to the amount due by members on their shares."

assignment throughout the Union.<sup>14</sup> The first part of Union company legislation was the Companies Act 46 of 1926, which was based on the Transvaal Companies Act 31 of 1909 which, and as indicated above, was based on English law. South African company law is based on English law: though various Acts have been passed after 1909 in England, overtime the South African Companies Act of 1926 was merely supplemented accordingly through various Amendment Acts. After the promulgation of the Companies Act of 1929 in England,<sup>15</sup> and in light of the amendments made to English legislation, the Lansdown Commission was appointed in South Africa to consider changes to the South African Companies Act of 1926.<sup>16</sup> As a result of the recommendations made by the Lansdown Commission, the Companies Act 23 of 1939 was promulgated. Numerous, less general amendments to the Companies Act of 1926 were introduced by other Companies Amendment Acts, Finance Acts and General Law Amendments. The Companies Amendment Act 46 of 1952 was promulgated based on the recommendations of the Millin Commission;<sup>17</sup> it was appointed following a report by the Cohen Commission in England, which resulted in the English Companies Act of 1948.<sup>18</sup>

The Jenkins Committee<sup>19</sup> was appointed in England in 1962 to report on company law. South Africa followed suit, and appointed a Commission of Enquiry into the Companies Act under the Chairmanship of Van Wyk de Vries J.<sup>20</sup>

#### **4. Companies Act 61 of 1973**

The Companies Act 61 of 1973 stems directly from the report of the Van Wyk de Vries Commission and not only incorporates amendments to the old Act but, in itself, is a completely new, restructured Companies Act. The framework of the Companies Act of

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<sup>14</sup> Mars *The Law of Insolvency* 12(hereafter referred to as Mars).

<sup>15</sup> Companies Acts 1929 and 1948. See also Cilliers and Benade 22 “Although the Companies Act 1948 implements some of the European Economic Community’s directives, it does not amount to a fundamental reform of English company legislation. It is essentially a consolidation in a more logical form and an endeavor to express the provisions in language as simple and uncomplicated as possible.”

<sup>16</sup> Burdette *Framework for Corporate Insolvency Law Reform in South Africa* (2002) LLD Thesis University of Pretoria 39(hereafter referred to as Burdette Thesis).

<sup>17</sup> Report of the Commission of Enquiry on the Amendments of the Companies Act (UG 69 of 1948).

<sup>18</sup> Burdette Thesis 39.

<sup>19</sup> Report of the Company Law Committee.

<sup>20</sup> Main Report (RP of 1970) and the Supplementary Report and Draft Bill (RP 31 of 1972).

1962 simply did not lend itself to further extension and amendment.<sup>21</sup> English precedent played an important role in South African company law, and the Commission did not recommend major amendments or new additions except if there were compelling reasons to do so. However, the Companies Act of 1973 marks a divergence between English and South African company law.<sup>22</sup> The 1973 Companies Act has been amended on various occasions in order to deal with various subjects.

Chapter XIX of the van Wyk de Vries Commission's main report dealt with the recommendations for winding-up and related mainly to the submission of a statement of affairs by its directors, reports by the Master, various provisions relating to liquidations, provisions relating to the administration process and provisions relating to the examination of directors and others.<sup>23</sup> In the 1973 Companies Act the winding-up of companies is dealt with in Chapter XIV: companies could be wound up voluntarily or by order of the court.

It is interesting to note that the 1973 Companies Act created a duality of statutes in dealing with insolvent companies. Section 339<sup>24</sup> provided that the law of insolvency also applies to the administration of companies. This duality created some interpretational problems in the administration of insolvent companies.<sup>25</sup>

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<sup>21</sup> Cilliers and Benade 24.

<sup>22</sup> See also Cilliers and Benade 24: "Major departures from the traditional English approach to be found in the Companies Act of 1973 include: (a) the establishment of the "company having share capital" as the basic company form in place of the unlimited company; (b) the virtual abrogation of the ultra vires doctrine; (c) the institution of a system of no par value shares; (d) the introduction of the statutory derivative action; and (e) the institution of a standing advisory committee on company law."

<sup>23</sup> Burdette Thesis 71.

<sup>24</sup> Companies Act 61 of 1973

<sup>25</sup> Burdette Thesis 71 and 72: "Section 339 of the 1973 Companies Act brings about the following problem: before one can decide whether or not section 339 applies, one first has to determine whether the provision is capable of being applied to winding-up. The next step would be to determine whether the matter is specifically provided for in the Companies Act. If the matter is not provided for in the Companies Act the solution is simple, in that the law relating to insolvency will be applied (whether that provision is contained in the Insolvency Act or in the common law). However, problems do arise where provisions are partially provided for in the Companies Act and partially provided for in the Insolvency Act. The question then is to what extent the provisions relating to insolvency will apply if at all."

## 5. Companies Act 71 of 2008

The new Companies Act of 2008<sup>26</sup> came into operation on the 1<sup>st</sup> of April 2011,<sup>27</sup> with extensive implications relating to corporate finance.<sup>28</sup> The 2008 Companies Act repealed the 1973 Companies Act bar Chapter 14.<sup>29</sup>

The Companies Act of 2008 is the consequence of a comprehensive corporate review which resulted in a draft policy framework. In essence corporate reform was needed for the following reasons: the weakness in current company law and the changes to the nature of the global and domestic economy together with the constitutionally-mandated process of transformation of South African society, compel a comprehensive review of South African company law.<sup>30</sup> The aim of the reform was to address the growing recognition by companies and governments that there was a need for higher standards of corporate governance and ethics and a greater interdependence between enterprises and the societies in which they operate.<sup>31</sup> In the context of changes to the law of corporate insolvency the review pointed out that particular attention should be given to the role and responsibilities of liquidators, the process of winding-up and the powers of inquiry.<sup>32</sup>

The provisions pertaining to corporate insolvency procedures in the 1973 Companies Act were retained. Item 9(1) of Schedule 5 provides, despite the repeal of the 1973 Act and until a date determined by the Minister by notice in the Government Gazette, Chapter 14 of the 1973 Companies Act continues to apply with regard to the winding-up

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<sup>26</sup> Companies Act 71 of 2008.

<sup>27</sup> General Notice 421 Government Gazette 32121 (9 April 2009).

<sup>28</sup> The previous Companies Act provided for two types of companies, namely a company having par value and a company having no par value shares. Over time, legal practitioners and others involved in corporate finance realized that the par value of a share was insignificant and a misleading indicator. It was only some forty years later that legislature rectified the confusion and complexity in South African corporate law by abolishing par value shares by introducing the New Companies Act 2008.

<sup>29</sup> See Schedule 5 Item 9 of the Companies Act of 2008.

<sup>30</sup> The following six categories were isolated as the focus of the reform: "Corporate formation; corporate finance; corporate governance; business rescue and mergers and take overs; not-for-profit companies; and administration and enforcement". See Boraine and Van Wyk "The application of "repealed" sections of the Companies Act 61 of 1973 to the liquidation proceedings of insolvent companies" *De Jure*(2013) 645( hereafter referred to as Boraine and Van Wyk).

<sup>31</sup> Department of Trade and Industry South African Company Law for the 21st Century: Guidelines for Corporate Law Reform May 2004 (2004) 15 (hereafter referred to as DTI: Guidelines).

<sup>32</sup> DTI: Guidelines 44.

and liquidation of companies under the Act as if the 1973 Act has not been repealed.<sup>33</sup> One of the main reasons for retaining Chapter 14 of the 1973 Companies Act was that these provisions would be incorporated into comprehensive legislation regulating insolvency and business rescue.<sup>34</sup> Therefore, the winding-up of companies is governed by two distinct pieces of legislation. If there is a conflict between the winding-up provisions of the 1973 Companies Act and Chapter 3 of the Companies Act of 2008, the latter will prevail. The Companies 71 of 2008 regulates the winding-up and liquidation of solvent companies, as well it introduces processes for the business rescue of companies.

## 6. Conclusion

It is evident from the chapter that English law has had a major influence on South African insolvency law. However, South African insolvency law is a hybrid system, consisting of some Roman-Dutch principles and English law. South Africa has steadily created its own insolvency law to an extent, distinct from other insolvency regimes around the world. The Insolvency Act 24 of 1936 has been the primary source of insolvency law for almost eighty years in South Africa. The insolvency law has been subject to a number of amendments over this period; however its review as a whole only started in the 1980's.

There are differences between individual and corporate insolvency and, the interpretational difficulties between these two aspects of insolvency remain and continues to grow; even more so as a result of the introduction of the 2008 Companies Act. Consumer insolvency is governed by the Insolvency Act 24 of 1936, whereas corporate insolvency was governed by the Companies Act 61 of 1973 (insolvent Companies) and, now, by the new Companies Act 71 of 2008(solvent companies).

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<sup>33</sup> Cassim et al *Contemporary Company Law* (2012)913.

<sup>34</sup> See Boraine and Van Wyk 646-647:“Nevertheless, the provisions relating to business rescue were not excluded from the ambit of the 2008 Act and Chapter 6 of the 2008 Act deals with these proceedings. No substantive provisions relating to the grounds and procedure for the liquidation of insolvent companies were developed and incorporated into the 2008 Act.”



## **Chapter 3: Assessment of Single versus Dual Insolvency Systems in the context of the USA and England**

### **1. Introduction**

The dissertation deals with the question of whether a unified approach to the winding-up of companies will be appropriate in the South African context. Before one considers the advantages and disadvantages of unified legislation one needs first to consider the different methods harmonizing and unifying insolvency legislation. The advantages and disadvantages of single or dual systems will be discussed and assessed, especially in view of South Africa's unique history.

This part of the study contains a brief comparative outline of the basic features of insolvency laws in jurisdictions such as England and USA. England has maintained separate legislation for consumer and corporate insolvency, whereas the United States of America has largely accomplished unified legislation. This comparative study will enable us to evaluate and understand the reform process adopted by these countries, as well as the rationale behind these reforms.

The purpose of the chapter is to give a brief overview of the historical development and reform process of insolvency law in these jurisdictions and, thus, will not provide a detailed exposition of the history; rather, it will highlight the key developments over time.

### **2. Single and Dual Systems: Advantages and Disadvantages**

Before evaluating draft legislation which deals with both consumer and corporate insolvency the various drafting options need to be assessed. The assessment of single or dual statutes can be made by analyzing the different methods, considering their respective advantages and disadvantages, and adapting them to the needs of a particular state. Keay identifies the various methods in which legislation can be enacted.<sup>35</sup> The first way to enact legislation is by having separate pieces of legislation for individual and corporate insolvency.<sup>36</sup> Second, there can be separate legislation for

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<sup>35</sup> Keay "To unify or not to unify insolvency legislation: International experience and the latest South African proposals" 1999 *De Jure* 64 (hereafter referred to as Keay).

<sup>36</sup> *Ibid.*

individual and corporate insolvency and the latter can be incorporated by reference to parts of the legislation dealing with individuals.<sup>37</sup> Third, there can be a single statute enacted, which deals with both individual and corporate insolvency but which provides for separate procedures for dealing with both types of insolvencies.<sup>38</sup> The final method is by drafting a single statute that deals with both individual and corporate insolvency equally.<sup>39</sup>

There are several advantages to a single statute.<sup>40</sup> The first advantage is that both consumer and corporate insolvency have the same objective, which is to form a *concursum creditorium*, which allows creditors to act as a group and allows for a just and equitable administration and distribution of the insolvent's assets; as well as to rescue and rehabilitate the insolvent.<sup>41</sup> Second, a unified system would decrease the costs of the process and would result in greater efficiency.<sup>42</sup> Keay mentions that an advantage of not duplicating provisions is the reduction in the size of statutes, which would be a refreshing change given the propensity of government's today to produce massive

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<sup>37</sup> *Ibid.*

<sup>38</sup> *Ibid* at b 65.

<sup>39</sup> *Ibid.*

<sup>40</sup> See also Havenga "Simplification and Unification in Corporate and Insolvency Law-Are We Making Any Progress?" 2001 *SA Merc LJ* 411 and 412(hereafter referred to as Havenga): "A unified Act would be more user friendly for foreign investors; that corporate insolvencies far exceed individual insolvencies in terms of value; that unnecessary differences are mostly inexplicable and complicate matters; that the opportunity to enact a unified Act may be lost if not taken away; that is easier to amend a single Act than separate Acts administered by different Ministers and considered by different portfolio's; that there will be a confusion if the insolvency law relating to individuals is reformed and nothing is done in connection with corporate insolvencies."

<sup>41</sup> See Keay 71: "First, many aspects of insolvency affecting both individuals and companies are, or should be, the same, as the aims of both personal and corporate insolvency are essentially identical: the provision of a procedure which provides an orderly, fair and equitable administration of an insolvent's estate, including an equal distribution of the assets of the insolvent; the provision of an impartial, efficient and expeditious administration process where the debts of creditors are satisfied with as little delay and expense as possible; the provision of mechanisms which allow for the treatment of insolvents' affairs before their position becomes hopeless, that is, early efforts to consider rescue proposals; the investigation of the affairs of the insolvent both to discover the reason(s) for the insolvency and to see if action needs to be taken because of the conduct of the insolvent, and in relation to corporate insolvents, their officers; the provision of a process which protects the community in that those who are insolvent are rendered unable to trade and to continue, without restriction, to obtain credit."

<sup>42</sup> See *Ibid* at 71 and 72: "Insolvency practitioners would be able to rationalize the administration of estates, and they should become, in due course, more efficient and more competent. In a dual system practitioners have to complete so many different forms and have to follow different procedures as well as having to be subject to different rules of court and different regulations." See *Wood Principles of International Insolvency Law* (2007) 6 (hereafter referred to as Wood).

pieces of legislation and then expect everyone to follow them.<sup>43</sup> Third, a unified approach would allow for harmony and unity among legislation and would reduce divergence. The fourth advantage is that the unified approach would allow insolvency legislation to be accessible, not only to legal practitioners, but also students and the greater public access.<sup>44</sup> Another advantage is that insolvency law would be recognized as an independent area of law.<sup>45</sup> Lastly, a unified approach allows unified control over both areas of law instead of having separate government departments to control consumer and corporate insolvency separately.

The disadvantages of a unified system include the following: that there are differences between natural and corporate persons.<sup>46</sup> Second, there are different philosophies behind consumer and corporate insolvency.<sup>47</sup> Third, the distinction between consumer and corporate insolvency is so great that it would be difficult to unify them without divergence. Fourth, it is necessary, if one wishes to introduce a unified system and if a dual system has operated previously for many years, to overcome the traditional thinking which is to separate the branches of insolvency; it can be an onerous task.<sup>48</sup> Last, drafting unified legislation incorporating consumer and corporate insolvency is a difficult task.<sup>49</sup>

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<sup>43</sup> Keay 72.

<sup>44</sup> *Ibid*: “A unified legislative scheme would provide a more regulated and comprehensive way of laying down the law.” See also Havenga 418.

<sup>45</sup> See Keay 72 “It is submitted that a unified scheme would emphasize this fact and permit the further development of insolvency law.”

<sup>46</sup> The main objectives of insolvency for individuals is to protect a debtor from harassment by creditors; to enable him to make a fresh start-especially in less blameworthy cases; to reduce indebtedness by making a contribution from present and future income, while at the same time, considering his personal circumstances. On the other hand, the main aim in corporate insolvency is to preserve the business, or viable parts thereof, where possible- not necessarily the company; where personal liability has been abused, to impose personal liability on responsible persons. See also Havenga 418.

<sup>47</sup> See Keay 73: “While there is a tendency in modern insolvency law around the world to emphasize the need to rehabilitate the debtor, whether the debtor is a person or a company, there is a particular emphasis on the fact that individuals should receive relief and release from their debts and be restored to the community as soon as possible.

<sup>48</sup> Keay 73.

<sup>49</sup> See *Ibid*: “To frame sections which apply to both persons and companies can be rather exacting and exceptions may have to be made for one form of insolvency when it comes to provisions which are applicable to both personal and corporate insolvency. If one wishes to frame truly unified legislation there may be a need to make compromises in order to have clarity and retain consistency.”

The advantages and disadvantages of a unified system or a dual system have to be considered before enacting any legislation. Dual systems are effective in legal systems in which they are drafted carefully and have been implemented correctly. Single legislative systems require a lot of time and effort in drafting, together with comprehensive research and space to allow for amendments over time. Most jurisdictions are adopting a unified approach; South Africa should follow suit by embracing modern trends for purposes of convenience and clarity.<sup>50</sup>

### 3. English Insolvency System

The English insolvency system developed later, when compared to continental Europe. The first bankruptcy legislation to be enacted was the Bankruptcy Act of 1542, introduced by Henry VIII.<sup>51</sup> Other Bankruptcy Acts followed and reflected changes over time. The Elizabethan Act of 1571 followed: the main aim being to prevent fraud and create a system of administration. The insolvency set-off was codified and discharge was introduced by the Bankruptcy Acts of 1705 and 1725.<sup>52</sup> The 1800's saw various changes being made to the previous Bankruptcy Act's; mainly the abolition of the trader and non-trader distinction and the introduction of preferential debts, as is evident in the Bankruptcy Acts of 1824, 1844, 1849, 1861 and 1883.<sup>53</sup> The Bankruptcy Act of 1914 was a direct result of the impact of the various developments arising through industrialization. This Act remained in force for seventy one years until 1985.

The law relating to corporate bodies was introduced by the Joint Stock Companies Act, 1844 although corporate insolvency itself only made a proper appearance in the

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<sup>50</sup> See Wood 6 "The law should be reasonably predicable, not arbitrary, capricious or discretionary....The law should aim at as much simplicity as is commensurate with the complexity of modern economies."

<sup>51</sup> Wood 17.

<sup>52</sup> *Ibid.*

<sup>53</sup> See Calitz "System of Regulation of South African Insolvency Law: Lessons from the UK" (2008) *Obiter* 357 and 358(hereafter referred to as Calitz 2008 *Obiter*):"The foundation of the modern English system of regulation of bankruptcy law was established when Joseph Chamberlain became the president of the Board of Trade. Chamberlain advocated a vision that the law had both to provide for the administration of the estate of the bankrupt but there was also a requirement for thorough and independent investigation into causes of insolvency in the public interest rather than leaving matters in the hands of creditors. Chamberlain was convinced that there was a public role to be played in the administration of bankruptcy and went ahead to develop the proposals for the Bill that would later become the landmark Act of 1883."

inclusion of the institution of “winding-up” in the Joint Stock Companies Act of 1848.<sup>54</sup> This Act was followed by the Limited Liability Act of 1855, the Joint Stock Companies Act of 1856, the Companies Act of 1948, the Companies Act of 1985 and the Companies Act of 1989.<sup>55</sup>

By the late nineteenth century insolvency law had evolved into specialized branches of individual and corporate insolvency. Both branches were contained in separate collections of statutes, namely the Bankruptcy Acts and the Companies Acts, and were administered judicially by different courts under different sets of procedural rules. Although many points of resemblance existed on both branches, and in some cases entire doctrines or legislative provisions were directly duplicated from the one branch of law to the other, the divergences between the two types of insolvencies became and remain substantial.<sup>56</sup> Over the years, various committees were established whose main task was to review certain aspects of English insolvency law.<sup>57</sup>

It was not until the Cork Report was commissioned that serious thought was given to the idea of unified legislation.<sup>58</sup> The first comprehensive review was undertaken in 1977 under the chairmanship of Sir Kenneth Cork.<sup>59</sup> One of the main recommendations in the

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<sup>54</sup> Omar *Insolvency Law in England and Wales* 2.

<sup>55</sup> See Cilliers and Benade *Corporate Law* (2000) 21 and 22 “The Limited Liability Act of 1855 accepted the unlimited liability of members as a given fact but created the machinery for the limitation of such liability to the amount due by members on their shares. The Joint Stock Companies Act of 1856 consolidated the two former Acts and thus made provision for two kinds of companies: the unlimited company and the limited company...The Companies Act of 1948, as amended by the Companies Acts of 1967, 1976, 1980 and 1983, was consolidated by the Companies Acts of 1985...It is essentially a consolidation and rearrangement of the previous legislation in a more logical form and an endeavor to express the provisions in language as simple and uncomplicated as possible...The Companies Act of 1989 introduced into English law the rules on consolidated accounts and the regulation of auditors contained in the European Economic Community’s Seventh and Eighth Directives.”

<sup>56</sup> See Fletcher *The Law of Insolvency* (1990) 13(hereafter referred to as Fletcher): “A failure to appreciate the full extent of the divergence between corporate and individual insolvency has at times led even the Legislature itself to formulate potentially unworkable procedures as hereby the unmodified provisions of the bankruptcy law were incorporated by reference into company winding-up, without proper regard to the practical consequences resulting from the two bodies of legal rules.”

<sup>57</sup> Calitz 2008 *Obiter* 358.

<sup>58</sup> Keay 67.

<sup>59</sup> The Cork Committee was given a very wide brief:

- (a) To undertake a total review of the law of insolvency, bankruptcy, liquidation and receiverships, and to consider reforms that are necessary or desirable;
- (b) To examine the possibility of formulating a comprehensive insolvency system, including the possibility of harmonizing and integrating procedures;

Cork Report was the unification of individual and corporate insolvency into a single piece of legislation which would unify insolvency courts.<sup>60</sup> Unfortunately not all the recommendations made in the Cork Report were implemented, a fact which has a negative impact on the development of insolvency law in England.<sup>61</sup> Although the laws relating to individual and corporate insolvency were merged into one Act, namely the Insolvency Act of 1986, the Act itself did not bring about a genuine unification of the law relating to these separate branches of the law.<sup>62</sup>

Various defects are evident in the Insolvency Act of 1986. Prior to unification, the Companies Act was amended so that it could be integrated into the Insolvency Act of 1986. The provisions dealing with bankruptcy and corporate insolvency were substantially amended with the result that each of the systems had been somewhat streamlined.<sup>63</sup> However, only a relatively small part of the Insolvency Act is common to both personal and corporate insolvency. Even though the development of both consumer and corporate law took place at the same time, the legislation did not clearly reflect this because many of the recommendations made in the Cork Report were not implemented resulting in a lack of integration. Incorporating individual and corporate insolvency into one statute does not necessarily bring about a unification of the insolvency laws, especially if the Act still makes a distinction between individual and corporate insolvency.<sup>64</sup> Despite a high degree of harmonization being achieved between parallel provisions belonging to different branches of insolvency law, the traditional

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(c) To investigate the possibility of formulating less formal procedures as alternatives to bankruptcy and winding-up; and

(d) To make recommendations.

<sup>60</sup> See Fletcher 17 : “ The central recommendations were that a unified Insolvency Code should be enacted in place of the diversity of statutes governing two distinct, if cognate branches of the law, and that a unified system of insolvency courts should be created to administer the law. “

<sup>61</sup> Burdette Thesis 86. Some of the main reasons for not implementing all the recommendations made by the Cork Report include the fact that there was a change in government between the time the commission of the Cork Report and the implementation of the recommendations. The recommendations that were implemented were done hurriedly without any consultation and debates. As a result, the Insolvency Act of 1985 was not unified and it had failed to incorporate individual and corporate insolvency. The evident defects were amended by the Insolvency Act of 1986.

<sup>62</sup> See Fletcher 20.

<sup>63</sup> Keay 68. Keay further states: “As a result there are, for example, separate provisions dealing with pre-liquidation transactions that are voidable on the one hand and pre-bankruptcy transactions which are voidable on the other.”

<sup>64</sup> Burdette Thesis 88.

distinction survives between consumer and corporate insolvency, and the pre-existing procedures have retained their respective and separate features.<sup>65</sup>

The Insolvency Act of 1986 has had two amendments, the Insolvency Amendment Act of 1994 and an Insolvency Amendment Act (number 2), 1994. Although not directly relevant to this research, the Insolvency Act of 2000 and the Enterprise Act of 2002 have resulted in a restriction on the use of the institution of “administrative receivership”: both Acts are a direct result of provisions absent from in the Insolvency Act of 1986.

#### **4. The Insolvency System in the United States of America**

The United States insolvency system can be described as a completely unified system of insolvency law. It was one of the first to introduce unified insolvency legislation together with reform, and has been followed by countries. Bankruptcy legislation in the United States is a federal issue.

Prior to 1800 English law and legal culture were predominant in the American colonies and early attempts to secure a Federal Bankruptcy Act leant heavily on the experience in England:<sup>66</sup> in the early insolvency laws, reference is made to the first bankruptcy law passed in England, namely the 1542 Act in the reign of Henry VIII.<sup>67</sup> The first permanent Federal bankruptcy law was passed in 1800. The Bankruptcy Act of 1800 closely followed the model of the 1732 English statute of George II: most notably, in allowing for complete creditor control of the bankrupt’s estate. As a result of the 1837 Panic, the Bankruptcy Act of 1841 was passed. The Bankruptcy Act of 1841 was an attempt to introduce bankruptcy legislation for both voluntary and involuntary bankruptcy.<sup>68</sup> The Panic of 1857 and the financial cataclysm caused by the American Civil War enacted overwhelming pressure for another federal bankruptcy law and led to the enactment of the Bankruptcy Act of 1867.<sup>69</sup>

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<sup>65</sup> Fletcher 20.

<sup>66</sup> See Tabb “The History of Bankruptcy Laws in the United States” (1995) *American Bankruptcy Institute Law Review* 12. (Hereafter referred to as Tabb): The first United States bankruptcy law, passed in 1800, virtually copied the existing English law.

<sup>67</sup> *Ibid* 12.

<sup>68</sup> *Ibid* 16.

<sup>69</sup> *Ibid* 28.

The Bankruptcy Act of 1867 was later repealed in 1878, despite it being used by the United States to shape the judicial mechanisms for dealing with bankruptcy cases. The next important phase in American bankruptcy history was the enactment of the Bankruptcy Act of 1898 and its subsequent amendments.<sup>70</sup> The Act remained in force for eighty years after being repealed by America's current bankruptcy legislation, namely the Bankruptcy Reform Act of 1978.

Although there were many amendments to the Bankruptcy Act of 1898, the core remained intact until 1979.<sup>71</sup> In 1970 Congress created the Burdick Commission on the Bankruptcy Laws of the United States as a result of growing dissatisfaction with the 1898 Bankruptcy Act.<sup>72</sup> The purpose of the Burdick Commission was to study and report on the existing bankruptcy laws. It did lodge its report in 1973, the Bankruptcy Reform Act followed in 1978, replacing the 1898 Act with the current Bankruptcy Code of 1978.<sup>73</sup> The Bankruptcy Code is a clear attempt to improve and streamline the process of administering bankruptcy cases. The Bankruptcy Code has also been amended on numerous occasions.<sup>74</sup> In 2005, the Bankruptcy Abuse Prevention and Consumer Protection Act (BAPCPA) of 2005 was introduced. The main aims of the BAPCPA include preventing abuse, disallowing debts obtained through fraud or crime and disallowing loopholes that previously existed.<sup>75</sup> The US Bankruptcy Code contains different chapters relating to various aspects of insolvency; BAPCPA has tightened its regulations through the introduction of the means testing and a compulsory education programme.

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<sup>70</sup> *Ibid* 30: "Notwithstanding its origins with the credit industry, the 1898 Act ushered in the modern era of liberal debtor treatment in the United States bankruptcy laws."

<sup>71</sup> Ferriell and Janger *Understanding Bankruptcy* (2007) 137.

<sup>72</sup> *Ibid* 137.

<sup>73</sup> See Tabb 32.

<sup>74</sup> See also Ferriell and Janger *Understanding Bankruptcy* (2007) 141: "The 1994 Amendments provided for one potentially significant change it created a new Bankruptcy Commission to study the Code and make recommendations."

<sup>75</sup> See Calitz "Developments in the United States' Consumer Bankruptcy Law: A South African Perspective" 2007 *Obiter* 401 "BAPCPA has fundamentally changed the mood of the US consumer bankruptcy law and the sweeping and controversial changes to the Bankruptcy Code have been widely criticized by inter alia the Bench, academic scholars and other role-players."



United States' bankruptcy law is seen to be "uniform", especially when reference is made to the federal system of government in the United States.<sup>76</sup> The Bankruptcy Code consists of nine chapters.<sup>77</sup> The United States' system has a single statute enacted which deals with both individual and corporate insolvency, but provides for separate procedures for dealing with both types of insolvencies. The Bankruptcy Code is truly unified in that most of its provisions deal with all forms of debtors, even if some of provisions appear under different chapter headings.<sup>78</sup>

## 5. Conclusion

South Africa currently has separate legislation governing consumer and corporate insolvency. After reviewing the advantages and disadvantages of a unified system, it is concluded that the advantages of a unified system outweigh the disadvantages. In implementing a unified system many challenges will be faced, mainly because consumer and corporate insolvency, for instance, are distinct areas of insolvency in South Africa, with different philosophies and aims. South Africa has a history of a dual system and overcoming traditional thinking, as well as drafting unified legislation, may be difficult tasks but a Draft Insolvency Bill exists and could serve as a template, as will be discussed in chapter 5.

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<sup>76</sup> Burdette 122.

<sup>77</sup> The Bankruptcy Code is divided into nine chapters:

- (a) Chapter 1 contains general provisions such as definitions;
- (b) Chapter 3 is entitled "Case Administrations" and deals with the commencement of a bankruptcy case under the code;
- (c) Chapter 5 is entitled "Creditors, the Debtor and the Estate" and deals with creditors, their claims, duties and benefits of the debtor and what the estate consists of;
- (d) Chapter 7 is entitled "Liquidation" and deals with liquidation cases under the Bankruptcy Code. In the main this chapter deals with the administration of chapter 7 cases, the collection of assets and the liquidation and distribution of the estate;
- (e) Chapter 9 is entitled "Adjustment of Debts of a Municipality";
- (f) Chapter 11 is entitled "Reorganisation" and deals with business rescue measures" and is a unified set for all kinds of "Reorganization", usually for debtors engaged in business, including individuals, partnerships and corporations and for both public and closely held companies. Its goal is to rehabilitate a business as a going concern rather than to liquidate it.;
- (g) Chapter 12 deals with the adjustment of debts of a family farmer with regular income;
- (h) Chapter 13 is entitled "Adjustment of Debts of an Individual With Regular Income."
- (i) Chapter 15 incorporates the Model Law on Cross Border Insolvency drafted by the United Nations Commission on International Trade Law.

<sup>78</sup> Burdette 247.

The most desirable method would be to have unified legislation incorporating both, individual and corporate insolvency. Despite the major transformation of the practices of legal practitioners, uniform insolvency laws create uniformity and certainty. It is submitted, since the Companies Acts 1973 and 2008 govern corporate insolvency, that it will be a difficult task to harmonize and unify both these Acts. It would be desirable for purposes of certainty and public accessibility to unify Companies Act 1973 and 2008, in order to have a single Companies Act to govern corporate insolvency.

Insolvency law in England developed over time and was altered and re-enacted to reflect the continuous changes experienced. Corporate insolvency developed to accommodate the growing need to protect companies, their directors and shareholders. Even though the comprehensive review by the Cork Committee recommended unification of laws, recommendations were not implemented by the government. As a result, even though England has a “unified” system, individual and corporate insolvency continue to exist and develop independently. England has not been successful in implementing unified legislation because it has merely incorporated individual and corporate insolvency without proper integration and harmonization.

The legal system in the United States of America, on the other hand, has departed from its origins in English statutes in some respects and for instance developed unique bankruptcy laws to reflect unique socio-economic needs by enacting unified legislation. The bankruptcy Code of 1978 has separate procedures for dealing with both types of insolvencies, creating different chapters dealing with different issues. The key lesson that South Africa can learn is that drafting unified insolvency legislation requires thorough research and drafting techniques to integrate consumer and corporate insolvency, as well as a proper consideration for the socio-economic and political environment of a developing economy.

The major problem in South African corporate insolvency law remains the fragmentation of corporate insolvency laws as a result of the two Companies Acts. The Insolvency Act of 1936 and parts of the Close Corporations Act, both of which regulate corporate insolvency. Unifying and harmonizing these laws into a single piece of legislation will eradicate fragmentation and create uniformity. A single statute will prevent duplication of

laws and overcome difficulties experienced in practice. It is submitted that the incorporation of Chapter 14 of the 1973 Companies Act into the 2008 Companies Act can be done in two ways. The first is by absorbing Chapter 14 verbatim into a new Act; the second method is by having both provisions in one chapter but having separate procedures dealing with solvent and insolvent companies.

## **Chapter 4: The Winding-Up of Insolvent Companies: Application of Repealed Sections**

### **1. Introduction**

The winding-up of solvent companies is regulated by the Companies Act 71 of 2008 and of insolvent companies by the Companies Act 61 of 1973. Despite the Companies Act of 1973 being repealed, Item 9 of schedule 5 of the 2008 Companies Act provides that chapter 14 of the 1973 Companies Act will continue to apply in respect to the winding-up and liquidation of companies as if it has not been repealed.

This chapter investigates the interpretation of Item 9 of schedule 5 in view of the application of the Companies Act 61 of 1973. The duality of statutes for the winding-up of companies has created various problems. The dissertation discusses two issues that demonstrate the need for reform. First, the meaning of “solvent” is not provided in the Companies Act of 2008; the sole definition is found in the previous Companies Act of 1973. Second, the provision of security for costs which was contained in the 1973 Companies Act is not in the 2008 Companies Act. The key question to arise: How do legal practitioners deal with provisions falling within the “repealed” Companies Act 61 of 1973 that have been excluded from the Companies Act 71 of 2008?

These issues serve as examples of the exacerbation of the problems in application and interpretation following the further fragmentation by the 2008 Companies Act and the interim solution by which chapter 14 of the 1973 repealed Companies Act is kept alive. Without this provision corporate insolvency will not be possible, but the current situation remains unsatisfactory.

### **2. The transition from the Companies Act 61 of 1973 to the Companies Act 71 of 2008**

The Companies Act 71 of 2008 came into effect on 1 May 2011, and repealed the Companies Act 61 of 1973. However item 9(1) of Schedule 5 provides, despite the repeal of the 1973 Companies Act, and until a date determined by the Minister through

notice in the Government Gazette, that Chapter 14 of the 1973 Act continues to apply with respect to the winding-up and liquidation of companies under this Act. Therefore, the winding-up of companies is governed by two distinct pieces of legislation, the Companies Act 61 of 1973 which deals with the winding-up of insolvent companies, and the Companies Act 71 of 2008, which deals with the winding-up of solvent companies.

The guidelines for corporate reform were drafted as part of the reform process in 2004.<sup>79</sup> The key aim in developing company law was that the Companies Act 61 of 1973 was thirty years old and had not been subjected to a comprehensive review to reflect the fundamental developments that were taking place in South Africa and elsewhere.<sup>80</sup> The liquidation provisions previously were found in Chapter 14 of the 1973 Act and read together with the Insolvency Act 24 of 1936. There were both overlaps and inconsistencies in the provisions of the previous Companies Act.<sup>81</sup> However, the motivation, as can be ascertained from the 2004 policy framework, was that these provisions would be incorporated into a comprehensive regulatory process for insolvency and business rescue.<sup>82</sup> No substantive provisions relating to the grounds and procedure for the liquidation of insolvent companies were incorporated in the new Companies Act.<sup>83</sup>

Even though section 224 of the new Companies Act states that the Companies Act of 1973 has been repealed, Schedule 5 of the 2008 Companies Act contains transitional provisions in respect of the 1973 Companies Act. The winding-up of insolvent companies, as previously mentioned, continues to be regulated by the provisions of the

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<sup>79</sup> See Department of Trade and Industry South African Company Law for the 21<sup>st</sup> Century: Guidelines for Corporate Law Reform May 2004 (2004) 3(hereafter referred to as DTI: Guidelines):"This review of company law in South Africa is now a priority. South Africa has fundamentally changed since the law review of its company law. A new constitutional framework and political, social and economic environment have been established post -1994. Corporate governance and other legislative developments since the 1990s have further underscored the need for reform. In addition the South African and global economies are significantly altered in their functioning."

<sup>80</sup> See *Ibid* 16 "New company law should therefore be consistent not only with the Constitution of South Africa and the principles of equality and fairness that it enshrines, but also with other laws that have been enacted, including the BEE Act, competition law, environmental law and access to information legislation."

<sup>81</sup> *Ibid* 43.

<sup>82</sup> Boraine and Van Wyk "The application of "repealed"\* sections of the Companies Act 61 of 1973 to liquidation proceedings of insolvent companies "2012 *De Jure* 646( hereafter referred to as Boraine and Van Wyk).

<sup>83</sup> *Ibid*.

Companies Act 61 of 1973 until such time as it has been replaced by other appropriate legislation. At first glance, the wording of this section subject to certain transitional provisions, indicates that this is a complete and comprehensive repeal.<sup>84</sup> Boraine and Van Wyk, point out, on a textual interpretation, that the transitional provisions set out in Schedule 5, specifically item 9, and segregate the application of the provisions to Chapter 14 of the Companies Act of 1973.<sup>85</sup>

### **3. The scope of Companies Act 61 of 1973 applicable to the new Companies Act 71 of 2008**

The scope of the application of the Companies Act 61 of 1973 in respect to the winding-up of insolvent companies is contained in Schedule 5 item 9 in the new Companies Act 71 of 2008. Schedule 5 item 9 provides for the following:

9. Continued application of previous Act to winding-up and liquidation.—

(1) Despite the repeal of the previous Act, until the date determined in terms of sub item (4), Chapter 14 of that Act continues to apply with respect to the winding-up and liquidation of companies under this Act, as if that Act had not been repealed subject to sub items (2) and (3).

(2) Despite sub item (1), sections 343, 344, 346, and 348 to 353 do not apply to the winding-up of a solvent company, except to the extent necessary to give full effect to the provisions of Part G of Chapter 2.

(3) If there is a conflict between a provision of the previous Act that continues to apply in terms of sub item (1), and a provision of Part G of Chapter 2 of this Act with respect to a solvent company, the provision of this Act prevails.

(4) The Minister, by notice in the *Gazette*, may—

(a) determine a date on which this item ceases to have effect, but no such notice may be given until the Minister is satisfied that alternative legislation has been brought into force adequately providing for the winding-up and liquidation of insolvent companies; and

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<sup>84</sup> *Ibid* at 651.

<sup>85</sup> *Ibid*.

(b) prescribe ancillary rules as may be necessary to provide for the efficient transition from the provisions of the repealed Act, to the provisions of the alternative legislation contemplated in paragraph (a).

The Companies Act 71 of 2008 repealed most of the Companies Act 61 of 1973: the notable exception is Chapter 14 which continues to apply in respect of the winding-up and liquidation of insolvent companies.<sup>86</sup> Sections 343, 344, 346 and 348-353 do not apply to the winding-up of solvent companies, except to the extent necessary to give full effect to the provisions of the new Act dealing with the winding-up and de-registration of solvent companies. (Part G of Chapter 2 of Act 71 of 2008).<sup>87</sup> The old Companies Act makes extensive provision for administrative and subsequent protective legislative functions to deal with an insolvent company.<sup>88</sup> The 2008 Companies Act provides a link (“bridge”) to the provisions of the 1973 Act, yet it does not make sense to pick and choose processes “piecemeal”; choosing between the 2008 Companies Act and 1973 Companies Act as and when needed, especially if a proper, comprehensive, tested and coherent procedure is available within the legal framework of the Companies Act of 1973.<sup>89</sup>

Item 9(1) of Schedule 5 provides that Chapter 14 of the Companies Act 61 of 1973 continues to apply in respect to the winding-up and liquidation of companies under this Act. It can be inferred from the wording of this provision that Chapter 14 applies to the winding-up of “companies” broadly, whether solvent or insolvent.<sup>90</sup>

How exactly is the term “repeal” to be interpreted? If section 11 of the Interpretation Act is followed, then the Companies Act of 1973 shall remain in force until the new Companies Act’s provision comes into force.<sup>91</sup> The effect of the repeal is that reference

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<sup>86</sup> See Item 9(1) of Schedule 5 of Act 71 of 2008.

<sup>87</sup> See Item 9(2) of Schedule 5 of Act 71 of 2008.

<sup>88</sup> Boraine and Van Wyk 651.

<sup>89</sup> *Ibid* at 653.

<sup>90</sup> See Boraine and Van Wyk 654: “The whole chapter 14 applies in a broad fashion to the liquidation of insolvent (or not solvent) companies although the procedure set out in chapter 14, subject to provisions such as section 79 of the 2008 Act, is also applicable to the winding-up of solvent companies.”

<sup>91</sup> See Botha *Statutory Interpretation* (2012) 70: “Section 11 of the Interpretation Act was enacted to deal with those unfortunate gaps in law if the one enactment is repealed, but the replacement has not yet become operational: ‘When a law repeals wholly or partially any former law and substitutes provisions for the law so repealed, the repealed law shall remain in force until the substituted provisions come into operation.’ This means that if an enactment has been repealed and is replaced by another, but the

made to the old Companies Act shall be construed as reference to the provision as re-enacted in terms of the 2008 Companies Act.<sup>92</sup> Therefore, item 9 is intended to serve only as a stop gap until new legislation is passed.<sup>93</sup> Item 9(4)(a) provides that Chapter 14 of the Companies Act 61 of 1973 will continue to apply and be in force until new or alternative legislation has been brought adequately providing for the winding-up and liquidation of insolvent companies. Section 12 of the Interpretation Act is not relevant in all respects since the new Companies Act did not keep Chapter 14 of the 1973 Companies Act “alive”- in effect, it can be argued that the 2008 Act, in practice, did not constitute a complete repeal of the 1973 Companies Act by virtue of the phrasing of section 224 and schedule 5 to the 2008 Companies Act.<sup>94</sup> Item 9(4) (b) prescribes ancillary rules to be applied where necessary to provide for the efficient transition from the provisions of the old Companies Act to the provisions of alternative legislation when contemplated.

From the above discussion, Schedule 5 should be interpreted not in a narrow, but rather in a liberal manner as it would result in the abolition of important measures in place to address matters relating to corporate insolvency in the absence of comprehensive legislation that can be viewed as an improvement on the present situation.

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replacement is not yet operational (for whatever reason), the repealed provision will remain in force- although repealed- until the replacement is in force.”

<sup>92</sup> Section 12(1) of the Interpretation Act provides that: “Where a law repeals and re-enacts, with or without modifications, any provision of a former law, references in any other law to the provisions so repealed shall, unless the contrary intention appears, be construed as references to the provisions so re-enacted.”

<sup>93</sup> See *Standard Bank Of South Africa Ltd v R -Bay Logistics CC* 2013 (2) SA 295 (KZD) C 2013 (2) SA 295 at par 21 and 22: “To answer, I think it is first necessary to consider the apparent intention behind the transitional provisions encapsulated in item 9. It seems clear that the legislature’s ultimate objective is to replace the provisions of chapter 14 of the old Companies Act, dealing with the winding-up of companies, with new legislation which would deal, separately, with ‘solvent’ companies and ‘insolvent’ companies. However, at the time that the new Act came into force, it made provision (in part G) only for the winding-up procedure for ‘solvent’ companies. For reasons which are not apparent, the legislature had not got round to creating any new legislation to deal with the winding-up of ‘insolvent’ companies. It is therefore clear that item 9 is intended to serve only as a stopgap, until such new legislation is passed. Item 9(4)(a) specifies that chapter 14 of the old Companies Act must continue in force until such new legislation, dealing with ‘insolvent’ companies, is actually in place.”

<sup>94</sup> Boraine and Van Wyk 661.



## 4. Miscellaneous issues arising from the application of the Companies Act 61 of 1973

### 4.1 The meaning of “solvent” companies

A chief difficulty is whether a state of actual or commercial insolvency is necessary to initiate the process set out in Chapter 14 of the 1973 Companies Act. Though some of the cases discussed below apply to close corporations, the processes are the same.<sup>95</sup> Section 345 of the Companies Act 61 of 1973 has been excluded from the new Companies Act. Section 345 of the 1973 Companies Act applies only to the winding-up of companies, and sets out the circumstances in which a company is deemed to be unable to pay its debts. The courts have since grappled with the meaning of “solvent” and whether there is implied inclusion into the new Companies Act.<sup>96</sup> A key reason for this confusion is that the term “solvent” is not defined in the 2008 Companies Act and this has led to various divergent decisions by the courts as to its meaning.

In *Standard Bank v R-Bay Logistics CC*<sup>97</sup> the court, in the matter in which the applicant, Standard Bank, failed to allege the insolvency of the respondent, R-Bay, had to decide what the legislature intended with “solvency” in Part G of Chapter 2 and in item 9 of schedule 5. The court set out the position in South African law and acknowledged that there was a difference, duly acknowledged by the legislator, between “actual or liberal insolvency” and “commercial insolvency”.<sup>98</sup> The 1973 Companies Act allowed for

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<sup>95</sup> See Locke “The meaning of ‘solvent’ for purposes of liquidation in terms of the Companies Act 71 of 2008: *Boschpoort Ondernemings (Pty) Ltd v Absa Bank Ltd*” 2015 *De Jure* 153( hereafter referred to as Locke): “A similar situation applies to the winding-up of close corporations. The new Act has made provisions applicable to the winding-up of insolvent companies in chapter 14 of the previous Act equally applicable to the insolvent winding-up of close corporations (item 9 Schedule 5, read with ss66 of the Close Corporations Act 69 of 1984, as amended by the new Act in Schedule 3.”

<sup>96</sup> See also <http://www.financialinstitutionslegalsnapshot.com/2014/05/solvent-and-insolvent-winding-up-of-companies-what-is-solvent-2/>.

<sup>97</sup> 2013 (2) SA 295 (KZD) C 2013 (2) SA 295. (hereafter referred to as *Standard Bank* judgement).

<sup>98</sup> *Boraine and Van Wyk* 655. See also See *Standard Bank* judgement par 14-15 :“Central to the issue raised by the respondent is what is meant by 'solvent' and 'insolvent' where those terms are used in item 9 and part G. It has long been accepted that, in our law, a state of 'insolvency' has two different meanings. Actual or literal insolvency involves a comparative measurement of the value of a company's assets and its liabilities. If the total value of those liabilities exceeds the total value of the assets, the company is actually insolvent. However, 'commercial insolvency' recognizes that, whether a company is actually insolvent or not, if it does not have sufficient cash resources to make payment of its ongoing obligations, as and when they fall due, the company is commercially insolvent. The two concepts (i.e.

commercial insolvency as contemplated in the provisions of sections 344(f) and 345, which provided that a company could be wound up if it was unable to pay its debts.<sup>99</sup> The court found that it is clear that item 9 of schedule 5 is intended to serve as a stop gap as item 9(4)(a) specifies that Chapter XIV of the 1973 Companies Act must continue to apply in force until such new legislation dealing with “insolvent” companies is actually in place.<sup>100</sup> Thus, for purposes of winding-up of an “insolvent” company, section 344 must still regulate the basis upon which it can be wound up. Commercial insolvency will be sufficient for the Companies Act 61 of 1973 to apply in respect of insolvent companies and, consequently, the new Companies Act will not apply.<sup>101</sup> The court consequently decided that a company need only establish commercial insolvency for the provisions of the Companies Act 71 of 2008 relating to the winding-up of solvent companies to be applicable.<sup>102</sup> Delport and Vorster point out that to argue that section 345(1) (a) of the 1973 Act will apply only once it is proved that the company is not solvent would have the effect that it would be ineffective and it would never find application; a result that could not have been intended by the legislature.<sup>103</sup>

In *HBT Construction and Plant Hire CC v Uniplant Hire CC*,<sup>104</sup> the court interpreted the inclusion of section 345 into the new Companies Act as implying that an applicant had to prove the insolvency of the company before the provisions of Chapter 14 of the previous Companies Act regulated the winding-up.<sup>105</sup> Although, not expressly stated, it may be gathered from the context that the court had factual insolvency in mind, meaning that an applicant had to show that the liabilities of the company exceeded its assets.<sup>106</sup> Locke submits that this interpretation had the effect that the deeming provisions in section 345 (as well as the deeming provision in section 69 of the Close

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actual insolvency vs. commercial insolvency) are quite different. The former involves the mere assessment of the value of a company's assets and liabilities. The latter involves an assessment of the company's cash flow, to determine whether it has the immediate wherewithal to pay its current expenses as they fall due.”

<sup>99</sup> *Standard Bank* judgement par 25.

<sup>100</sup> *Ibid* at par 22.

<sup>101</sup> *Ibid* at par 36.

<sup>102</sup> Boraine and Van Wyk 656.

<sup>103</sup> Delport & Vorster *Henochnsberg on the Companies Act, 71 of 2008* (2014) 320(hereafter referred to as Henochnsberg).

<sup>104</sup> 2012 (5) SA 197 (hereafter referred to as *HBT Construction* judgement).

<sup>105</sup> *HBT Construction* judgement par 6 and 7.

<sup>106</sup> Locke 154.

Corporation's Act), no longer on their own constituted a ground for insolvent winding-up in terms of Chapter 14.<sup>107</sup>

In *First Rand Bank Ltd v Lodhi 5 Properties Investment CC and Another*,<sup>108</sup> it was decided, in the absence of an express provision, that there is no indication in the new Companies Act that the legislature intended, particularly in so far as it left section 345 of the 1973 Companies Act intact, to do away with the principle that a company (or close corporation) may be liquidated on the grounds of its "commercial insolvency".<sup>109</sup> The expression "solvent company" in item 9(2) of schedule 5 of the new Companies Act relates to solvent companies being companies that are either not "actually (or factually) insolvent" or "commercially insolvent", envisaged in Part G of Chapter 2 of the new Companies Act. By contrast, to companies that are insolvent, companies that are either "commercially insolvent" or "actually (or factually) insolvent", are to be dealt with in terms of Chapter 14 of the 1973 Companies Act.<sup>110</sup>

In *Boschpoort Ondernemings (Pty) Ltd v Absa Bank Ltd*,<sup>111</sup> Absa Bank applied for Boschpoort Ondernemings to be wound up in terms of section 344(f) read with section 345 of the Companies Act 61 of 1973, or alternatively in terms of section 81(1) (c) (ii) of the Companies Act 71 of 2008. The fact that the company was commercially insolvent was not disputed. In the *court a quo*, it was accepted, because the company was factually *insolvent*, it could be wound up only in terms of solvent winding-up provisions in the new Companies Act. However, a liquidation order was granted because it was just and equitable to do so. The Supreme Court of Appeal stated that the new Companies Act does not refer to "insolvency" and the fact that the legislature refrained from defining "solvency" was apparently deliberate in order to retain the existing interpretations.<sup>112</sup> The court stated various reasons for this conclusion.<sup>113</sup> The court held

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<sup>107</sup> *Ibid.*

<sup>108</sup> 2013 (3) SA 212 (GNP)(hereafter referred to as *First Rand Bank* judgement).

<sup>109</sup> *First Rand Bank* judgement par 30.

<sup>110</sup> *Ibid.*

<sup>111</sup> 2014 (2) SA 518 (SCA) ([2014] JOL 31202 (hereafter referred to as *Boschpoort Ondernemings* judgement).

<sup>112</sup> *Boschpoort Ondernemings* judgement par 19.

<sup>113</sup> *Ibid* at par 17 "It is difficult to determine the value of assets objectively and creditors have insufficient knowledge of their assets. The test whether a company is able to pay its debts is more readily determinable and objective, which makes it preferable for the adjudication of liquidation applications."

that the legislature is presumed to be acquainted with the interpretation of earlier legislation by the court which applies where there has been settled judicial interpretation before legislation was passed.<sup>114</sup> This belief confirms the presumption that the legislature did not intend to alter the law more than necessary.<sup>115</sup> The position is that in order for the provisions of Chapter 14 of the Companies Act 61 of 1973 to come into operation, the company must not be solvent. The position was confirmed in paragraph 21 and 22, that the retention by the legislature in the context of the winding-up of a solvent company in the new Companies Act of the deeming provisions as to when a company is unable to pay its debts as contained in section 345 of the old Companies Act, is a clear indication of what is meant by an insolvent company in the new Companies Act.<sup>116</sup> Delport and Vorster submit that an application for the winding-up of a company that is not solvent, and thus the application of Chapter 14 of the 1973 Companies Act, must, at least, allege factual or commercial insolvency, whether based on clear evidence to the effect or on *prima facie* evidence, such as that provided for in section 345(1) (a) of the 1973 Companies Act.<sup>117</sup> It can be concluded that “insolvent” for purposes of the new Companies Act means commercial insolvency (and the same “commercial solvency” applies to solvent companies).<sup>118</sup>

#### **4.2 Security for costs**

Section 13 of the Companies Act 61 of 1973 provided that where a limited company was the plaintiff or applicant in any legal proceedings a court, at any stage, could order it to furnish security for costs if there was reason to believe that the company or, if the company was being wound up, its liquidator would be unable to pay the costs of the defendant or respondent if successful in his defense and could stay all proceedings until security was given. The new Companies Act of 2008 does not contain a similar

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<sup>114</sup> *Ibid* at par 18.

<sup>115</sup> *Ibid* at par 18.

<sup>116</sup> Henochsberg 315.

<sup>117</sup> *Ibid* at 319. See also Henochsberg 319 : “Although s345(1)(a) of the 1973 Act will only become operative if it is proved that the company is not solvent, it is suggested that it could nevertheless be used to make a *prima facie* case that the company is solvent.”

<sup>118</sup> See Locke 161: “Winding-up in terms of ss 80 or 81 of the new Act is only available to commercially solvent companies. It is not necessary to prove additionally that such a company is factually solvent, as this would lead to ‘an unbusinesslike result’(par 23). Commercially insolvent companies must still be wound up in terms of chapter 14 of the previous Act(par 22).The Supreme Court of Appeal effectively held that the grounds for winding-up of insolvent companies remain unchanged.”

provision in respect of the requirement of security of costs by companies in civil proceedings.<sup>119</sup> The question now is, in the absence of the statutory provision for security of costs by companies, whether a local company can be compelled to give security for costs wither as plaintiff or defendant.

In *Haitas v Port Wild Props 12 (Pty) Ltd*,<sup>120</sup> it was common cause that the applicant was insolvent as he had neither realizable assets nor cash.<sup>121</sup> For a period of three years the applicant made no attempt to enroll the matter.<sup>122</sup> (When the dispute arose the Companies Act 61 of 1973 was in effect and when the matter was enrolled in the court the new Companies Act 71 of 2008 had come into effect.) A question arose whether the interests of justice would be served by requiring the applicant to file security for costs.<sup>123</sup> The court held that it is inimical to the interests of justice to expect the applicant to proceed with the matter to its finality, well knowing that in the event that the respondents succeeded and an adverse costs order is made against the applicant, such costs order would not be satisfied.<sup>124</sup> In these circumstances it would be unfair, unjust and inequitable that an impecunious and insolvent applicant would be allowed to proceed with the trial while not at risk.<sup>125</sup> It is not in the interest of justice to embark on vexatious litigation whereby only the defendants would be at risk with regard to costs.<sup>126</sup> The plaintiff was ordered to file security for costs in terms of rule 47, as directed by the registrar.<sup>127</sup> This case serves as authority that the judiciary considers section 13( which falls outside the scope of chapter 14) to have been repealed, security for costs can still be demanded from an insolvent company in terms of rule 47 of the Uniform Rules of Court and based on the criteria created through the development of common law principles.<sup>128</sup>

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<sup>119</sup> See also <https://www.cliffedekkerhofmeyr.com/en/news/publications/2014/dispute/dispute-resolution-matters-september-security-for-costs-a-new-dispensation.html>.

<sup>120</sup> 2011 5 SA 562 (GSJ). (hereafter referred to as *Haitas* judgement).

<sup>121</sup> *Haitas* judgement par 9.

<sup>122</sup> *Ibid* at par 10.

<sup>123</sup> *Ibid* at par 13.

<sup>124</sup> *Ibid* at par 13.

<sup>125</sup> *Ibid* at par 13.

<sup>126</sup> *Ibid* at par 13.

<sup>127</sup> *Ibid* at par 17.

<sup>128</sup> Boraine and Van Wyk 652.

In *Ngwenda Gold v Precious Prospect Trading*,<sup>129</sup> the respondents attempted to seek an order directing the applicants to provide security for costs, while the respondents opposed the application.<sup>130</sup> The court was critical of the *Haitas* judgement:<sup>131</sup> in the absence of a provision similar to section 13 of the Companies Act as a result of an oversight on the part of the legislature,<sup>132</sup> the court found that an applicant, in an application for security for costs must base its entitlement to security for costs on the principles of the common law.<sup>133</sup> The application for security for costs accordingly was dismissed. The court in *Ngwenda Gold v Precious Prospect Trading* indicated, as a result of the repeal of section 13 and the fact that the 2008 Act did not contain an equivalent provision that reference has to be made to the common law provisions when deciding on whether a company should be obliged to provide security for costs.<sup>134</sup> Van der Merwe AJ duly noted that rule 47 of the Uniform Rules of Court regulated the procedural aspects of security for costs but that the principles of the common law governed the specific instances when security could be sought in the absence of legislative stipulations.<sup>135</sup>

In the recent case of *Boost Sports Africa (Pty) Ltd v the South Africa Breweries (Pty) Ltd*,<sup>136</sup> a dispute arose between the applicant and the respondent, whereby the

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<sup>129</sup> Unreported case 2011/31664 (GSJ) 14 December 2011.(hereafter referred to as *Ngwenda* judgement).

<sup>130</sup> *Ngwenda* judgement at par 1.

<sup>131</sup> See *ibid* at par 9 and 16: "This judgment is not authority for the proposition that the approach reflected in section 13 of the previous Companies Act should still find application, notwithstanding the fact that the legislature has seen fit not to retain the equivalent of section 13 of the previous Companies Act in the new Companies Act. The judgment is also not authority for the proposition that an insolvent company or even a company in liquidation is in general obliged to provide security for costs. Contrary to the contentions advanced on behalf of the respondents, the judgment is even less authority for the proposition that a company whose assets exceed its liabilities by a large margin, but whose assets are not readily realizable, is obliged to provide security for costs... The *Haitas*-judgment accordingly did not simply reintroduce the approach to security for costs as reflected in section 13 of the previous Companies Act, but specifically took into account special circumstances which indicated that the plaintiff was indeed proceeding with vexatious, reckless or unmeritorious litigation."

<sup>132</sup> *Ngwenda* par 22. See further at par 12 "The fact that the new Companies Act was promulgated after the inception of the Constitution of the Republic of South Africa, 1996, suggests that the legislature, in not retaining an equivalent provision to the previous section 13, was mindful of the provisions of section 34 of the Constitution of the Republic of South Africa, 1996, in terms whereof access to the courts is enshrined."

<sup>133</sup> *Ibid* at 10.

<sup>134</sup> Boraine and Van Wyk 652.

<sup>135</sup> *Ibid*.

<sup>136</sup> (20156/204) [2015] ZASCA 93.(hereafter referred to as the "*Boost judgement*".)

applicant refused to furnish evidence of its ability to pay the respondent's costs in the event of its claim being dismissed, which led to the respondent launching an application of security for costs.<sup>137</sup> In the *court a quo*, the judgment was given in favour of South African Breweries and Boost Sports Africa was ordered to furnish security for the costs of the legal action.<sup>138</sup> On appeal the SCA dismissed the case and the applicant was ordered to provide security for costs. The bench gave various reasons for its decision. First, the court derives its power from the Constitution in terms of section 173 to protect and regulate its own processes and to develop the common law, taking into account the interests of justice.<sup>139</sup> Second, the omission of a similar provision to section 13 from the 2008 Companies Act, therefore, must be taken (*prima facie*, at least) to import a change of intention on the part of the legislature.<sup>140</sup> Third, it has been suggested that such a provision has been excluded because its inclusion would limit the fundamental right of access to the courts as enshrined in section 34 of the Constitution and would thereby be unconstitutional.<sup>141</sup> Fourth, section 39(2) of the Constitution makes plain that, when a court embarks upon a course of developing the common law, it is obliged to "promote the spirit, purport and objects of the Bill of Rights".<sup>142</sup> Last, the omission of a provision similar to section 13 in the new Companies Act is strange since section 8 of the Close Corporation's Act 69 of 1984, which has been interpreted in accordance with the principles that have evolved in relation to the corresponding provisions in the previous Companies Act, has been retained.<sup>143</sup> The onus is on the party seeking security to persuade a court that security should be ordered.<sup>144</sup> Though there may be a poor prospect of recovering costs, a court, in its discretion, should order the furnishing of security for such costs by an *incola* company only if it is satisfied that the

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<sup>137</sup> *Ibid* at par 2.

<sup>138</sup> *Ibid* at par 4.

<sup>139</sup> *Ibid* par 13.

<sup>140</sup> *Ibid* at par 13.

<sup>141</sup> *Ibid* at par 13. See also at par 13 "But that may be to ignore the fact that a court was vested with discretion in terms of s 13 and that in exercising its discretion a court performs a balancing act. On the one hand it must weigh the injustice to the plaintiff if prevented from pursuing a proper claim by an order for security and against that it must weigh the injustice to the defendant if no security is ordered and the plaintiff's claim fails and the defendant finds himself unable to recover costs."

<sup>142</sup> *Ibid*.

<sup>143</sup> *Ibid*.

<sup>144</sup> *Ibid* at par 14.

contemplated main action (or application) is vexatious or reckless or otherwise amounts to an abuse.<sup>145</sup>

In view of the abovementioned cases Van Loggerenberg and Malan submit that section 13 of the Companies Act 61 of 1973 is capable of existing alongside section 34 of the Constitution.<sup>146</sup> They further contend that in the absence of a corresponding section in the Companies Act 71 of 2008 to section 13 of the 1973 Companies Act is a pure oversight by the legislature and that legislative intervention is the most appropriate remedy to rectify this situation by introducing a provision similar to section 13 of the Companies Act of 1973 into the Companies Act of 2008.<sup>147</sup> Boraïne and Van Wyk, on the other hand, argue that section 13, as a “procedural matter incidental to civil proceedings”, should still find application within a spectrum clearly delineated by the insolvent state of a company, especially as the 2008 Act was not intended to regulate proceedings relating to insolvent companies.<sup>148</sup> They further contend that the lack of a provision, such as section 13, was not an oversight on the part of the legislator in relation to insolvent companies, as the former was not called upon to consider security for costs within this ambit.<sup>149</sup> The case of Boost Sports Africa has confirmed the liberal approach followed in the *Haitas* case. The Supreme Court of Appeal, finally, has clarified the uncertainty with regards to security for costs: the courts will require an impecunious plaintiff company to furnish security for costs if there is reason to believe that the plaintiff will not be able to pay an adverse costs order.

## 5. Conclusion

The above discussion sets out the scope of the application of the Companies Act 61 of 1973, with some examples of its current application. It is clear from the wording of item 9 of schedule 5 of the 2008 Companies Act that the 1973 Companies Act continues to apply, “as if it had not been repealed”, in respect of insolvent companies. Uncertainty

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<sup>145</sup> *Ibid* par 16.

<sup>146</sup> Van Loggerenberg and Malan “Security for costs by local companies: Back to 1909 in the Transvaal, or not?” 2012 *THRHR* 619(hereafter referred to as Van Loggerenberg and Malan).

<sup>147</sup> Van Loggerenberg and Malan 621.

<sup>148</sup> Boraïne and Van Wyk 672.

<sup>149</sup> *Ibid*. See further at 672: “At present, the provision relating to the provision of security for costs in the unofficial 2010 working draft of the Insolvency and Business Recovery Bill is a hybrid version of section 13 and the developed version of the common law by the courts in *Haitas* judgement etcetera.”



arises because item 9 states that Chapter 14 of the 1973 Companies Act, continues to apply, and it is unclear whether the provisions relating to the winding-up and liquidation of companies falling outside of this chapter remain in effect.

The meaning of “solvent” was for instance not provided in the Companies Act of 2008, which has created a number of different opinions. The Supreme Court of Appeal in the *Boschpoort* judgement has brought about clarity in the interpretation of item 9(1) of schedule 5 with regard to the meaning of “solvent” and “insolvent”. This case confirmed that the test for solvency (and insolvency) is commercial solvency and, if a company is commercially insolvent, it will be governed by the Companies Act 61 of 1973. It can be concluded, if an insolvent company is being wound up and liquidated, it will be wound up in terms of section 345 of the 1973 Companies Act, relying on the term “insolvent” as envisaged in the 1973 Companies Act.

Prior to the 2008 Companies Act, a defendant company could rely on the provisions of section 13 of the 1973 Companies Act and bring an application requesting the court to order security for costs against a company of dubious financial standing. However, the new Companies Act 2008 does not contain a similar provision. In the *Haitas* judgement the court adopted a liberal approach and stated that security for costs can still be demanded, though the provision of security for costs is not contained in the Companies Act 71 of 2008, this lacuna cannot defeat a court's inherent power to regulate its own process by guarding against unnecessary or vexatious litigation by impecunious plaintiffs. Therefore the courts can insist on the furnishing of security where the interests of justice demand it. On the other hand, in the *Ngwenda Gold* judgement, the court followed a conservative approach and concluded that section 13 of the previous Companies Act 1973 did not apply and, therefore, common law principles must be relied upon. Finally, the Supreme Court of Appeal in the *Boost* judgement confirmed the liberal approach in the *Haitas* judgement, that security for costs must be furnished by *incola* companies.

It is clear from this chapter that the scope of the Companies Act 71 of 2008 is not aimed at regulating the winding-up and liquidation proceedings of insolvent companies. The Companies Act 61 of 1973 continues to regulate the winding-up and liquidation of

companies through the application of Chapter 14, even if they do not fall within the ambit of Chapter 14. Our courts have been reluctant to apply sections falling beyond the scope of Chapter 14, and instead, have relied on developing the common law to fill the gap. The failure of the legislature to replace provisions of the 1973 Companies Act in the new Companies Act cannot be regarded as a legislative oversight, but rather as a way of maintaining the provisions of the previous Companies Act. It can be inferred from the discussion above that our courts have grappled with connecting the provisions of these two Companies Acts' and that this duality has created interpretational and practical problems.

Despite the current system of winding-up of companies being workable it has shortcomings which create problems. First, the application of Chapter 14 of the Companies Act 61 of 1973 creates interpretational problems because it cannot be viewed in isolation. Also, item 9(1) of schedule 5, which states that chapter 14 of the 1973 continues to apply in respect of the winding-up and liquidation of companies as if the 1973 Act had not been repealed, is problematic. The issues discussed in this dissertation by way of examples to highlight the interpretational difficulties are: firstly, the definition of "solvent" is not defined in the new Companies Act of 2008 and, secondly there is no provision for security for costs. Thirdly, both the 1973 Companies Act and the 2008 Companies Act contain provisions relating to the winding-up of companies that must now be read together. The complications in respect of these dual companies Acts' has resulted in interpretational problems and has led to expensive litigation costs and remains a time-consuming process.

The aforesaid problems can be addressed in unified legislation by incorporating the provisions relating to the winding-up and liquidation of companies. It is submitted that if the provisions relating to the winding-up of companies is contained in one section (or chapter), which regulates both solvent and insolvent companies, it would avoid the interpretational problems, resulting in more certainty within this area of the law. The current dispensation regulating the winding-up and liquidation of companies is not viable because it is complicated and results in differing interpretations. Harmonizing the liquidation provisions of the Companies Act 61 of 1973 and the Companies Act 71 of

2008, and creating a single companies Act would remove the duplication of statutes and create transparency in our insolvency regime. If a unified Act is not adopted soon, an alternative, and arguably better interim measure than the current situation would be to, at least unify the winding-up provisions for both solvent and insolvent companies in the 2008 Companies Act.

This chapter thus illustrates that the current state of affairs complicates an already complex system due to further fragmentation of our insolvency laws and that matter should be addressed by legislative intervention.

## **Chapter 5: Analysis of and Comments on the Draft Insolvency Bill**

### **1. Introduction**

The current Insolvency Act 24 of 1936 has served as the primary source of insolvency law for almost eighty years. Other sources of South African insolvency law are contained in various pieces of legislation. Though the system has worked fairly well in the past, there is a need for transformation in this branch of law.

In the international context insolvency law has been reviewed and brought in line with modern developments. A review of South African insolvency law was commenced in 1988, by the South African Law Commission. The first Draft Insolvency Bill and Explanatory memorandum can be viewed as a tangible step towards implementing law reform in South African insolvency law but it did not contain provisions relating to the liquidation of companies yet.<sup>150</sup> Subsequent to these initiatives, Cabinet adopted a resolution to work towards a single unified insolvency Act but, the Department of Trade and Industry instead, proceeded with new company legislation, which resulted in the 2008 Companies Act. This Act however did not cater for the liquidation of insolvent companies and related matters; hence the incorporation of Chapter 14 of the 1973 Companies Act, as discussed in Chapter 4 of this dissertation, as a transitional arrangement pending the introduction of new, comprehensive insolvency legislation. The Department of Justice and Constitutional Development, however, continued to develop new insolvency legislation which resulted in a working document in the format of a draft bill. The 2015 version of the Draft Bill is the current version used and was made available to the public. It attempts to unify both consumer and corporate insolvency law principles. For purposes of this discussion, it will be referred to as the Draft Insolvency Bill of 2015. The relevant Project Committee has considered the

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<sup>150</sup> See South African Law Commission *Draft Insolvency Bill and Explanatory Memorandum Working Paper 66 Project 63(1996)* and its *Review of the Law of Insolvency Discussion Paper 86*. See also, South African Law Reform Commission report *on the review of the law of insolvency (Project 63)* vol 1 (Explanatory Memorandum) and vol 2 (Draft Bill) (Feb 2000).

comments and has amended the Draft Bill a number of times in view of recent changes.<sup>151</sup>

This chapter is thus based on the unofficial 2015 working draft of the Insolvency and Business Recovery Bill.<sup>152</sup> The chapter analyzes the Draft Insolvency Bill of 2015 proposals in the context of the regulation, as well as the unification of liquidation proceedings in view of the winding-up and liquidation of companies (including solvent and insolvent companies). The scope of the chapter is limited to the unification of company legislation relating to the winding-up of companies.

## **2. Structure and unification of the winding-up provisions in respect of companies**

The preamble states that the Draft Insolvency Bill aims to consolidate, unify and amend the law relating to the insolvency of consumers and companies as well as other legal entities.<sup>153</sup> The Draft Insolvency Bill of 2015 contains twenty-four chapters relating to different aspects of the law.<sup>154</sup> In view of the unification of insolvency law, the Draft Insolvency Bill of 2015 is a single statute to deal with both individual and corporate insolvency, but provides for separate procedures for dealing with the two types of insolvency. In circumstances in which insolvency law applies to both insolvency regimes common procedures are provided. South Africa has adopted a similar approach to the United States of America by enacting a single piece of legislation and providing separate procedures for dealing with the two types of insolvencies. This approach can be viewed as being completely unified: it takes cognizance of the different philosophies behind consumer and corporate insolvencies by enacting separate procedures relating to each area and makes provision for procedures which are common to both consumer

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<sup>151</sup> See Evans, Loubser & Van der Linde “Aspects of the Draft Insolvency Bill” 1999 *SA Merc LJ* 211; and Boraine and Van der Linde “The draft Insolvency Bill- An exploration” Part 1 1998 *TSAR* 621.

<sup>152</sup> Hereafter referred to as the Draft Insolvency Bill of 2015.

<sup>153</sup> The preamble contained in the Draft Insolvency Bill of 2015 is as follows:

“To consolidate, unify and amend the law relating to the insolvency of natural persons, companies, close corporations, trusts, partnerships and other legal entities, with or without legal personality, so as to balance the needs of the different stakeholders.”

<sup>154</sup> The Draft Insolvency Bill, for example contains chapters such as Chapter 1: Definitions; Chapter 2: Manners In Which Debtor May Be Liquidated; Chapter 3: Special Provisions Applicable To Specific Debtors; Chapter 4: Liquidation Orders And Commencement Of Liquidation; Chapter 5: Effect Of Liquidation; Chapter 6: Rights And Obligations Of Debtor During Insolvency; Chapter 7: Impeachable Dispositions; etcetera.

and corporate insolvency. For example, under chapter 2, section 3 stipulates the provision relating to the application by a debtor for the liquidation of an estate of a natural person or partnership; section 4 relates to the application by a debtor for the liquidation of a trust, company, co-operative, close corporation or another debtor, other than a natural person or partnership. These separate sections retain the distinct philosophies behind both types of insolvency, for example, companies are regarded as separate legal entities as opposed to natural persons.<sup>155</sup> Chapter 11 contains the stipulations relating to meetings and the questioning of debtors and other persons, which reflects that this chapter makes provision for both consumer and corporate insolvency and is a common factor between them.

The definitions are contained in Chapter 1, section 1 of the Draft Insolvency Bill of 2015. The Draft Insolvency Bill of 2015 does not differentiate between winding-up solvent and insolvent companies, as is evident from the omission of these terms from the definitions section. Section 4 regulates the liquidation applications with reference to who brings the liquidation application. The Draft Insolvency Bill of 2015 makes specific cross-reference to the Companies Act 71 of 2008 where a specific provision falls within the ambit of the Companies Act of 2008. For example, section 4(d) states: “the Commission or Panel defined in section 1 of the Companies Act has applied to the court for an order to wind up the company”.

As mentioned above, the Draft Insolvency Bill of 2015 removes the distinction between the winding-up of insolvent and solvent companies. It is submitted that this distinction was removed as a result of the uncertainty and complications that resulted from the duality of statutes, namely, the Companies Act 61 of 1973 and the Companies Act 71 of 2008, which regulated these areas separately. Chapter 4 regulates the liquidation order and the commencement of liquidation. Since the Draft Insolvency Bill of 2015 refers to

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<sup>155</sup> See Keay “To unify or not to unify insolvency legislation: International experience and the latest South African proposals” 1999 *De Jure* 71.

“liquidation” broadly, it can be deduced that the Draft Insolvency Bill of 2015 has done away with this distinction.<sup>156</sup>

It is interesting to note that the legislature views the liquidation and winding-up of companies as an extraordinary and extreme measure. This view is reflected in sections 10 and 11 which stipulate the provisions relating to the granting of provisional and final liquidation orders. Both sections state that the orders may be granted, amongst other requirements, if any of the following, where applicable, are not more appropriate than winding-up:

- 1) Business rescue proceedings in terms of Chapter 6 of the Companies Act 71 of 2008;
- 2) Compromise in terms of section 155 of the Companies Act 71 of 2008;
- 3) Post or pre-liquidation composition in terms of section 118 or 119;
- 4) Administration order in terms of section 74 of the Magistrates’ Courts Act 32 of 1944.

From the above provisions, it can be inferred that the legislature views the winding-up of companies as a last resort, and other methods of dealing with companies must be considered and/ or exhausted before liquidation and winding-up are considered.

Security for costs has been a contentious issue, as discussed in Chapter 4 of the dissertation: section 12 of the old Companies Act alone made provision for security for costs, the new Companies Act 2008 does not contain a similar provision. The Draft Insolvency Bill of 2015 does not expressly make provision for security for costs as did the 1973 Companies Act. However, section 7 relates to the abuse of a court’s procedure or malicious or vexatious applications for liquidations. Section 7 provides as follows:

Whenever the court is satisfied that an application for the liquidation of a debtor's estate is an abuse of the court's procedures or is malicious or vexatious, the

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<sup>156</sup> The Draft Insolvency Bill of 2015 does not define “liquidation” in section 1, the definitions section. Furthermore, there are no separate definitions for “solvent” and “insolvent” companies under this section.

court may allow the debtor forthwith to prove any damages which he or she may have sustained by reason of the application and award him or her such compensation as it considers appropriate.

Furthermore, section 174(6) provides that a liquidator or administrator need not give security for costs for such proceedings unless the court on application of the defendant or respondent is satisfied that the proceedings are frivolous or vexatious. From these two sections, it can be concluded, where there is an abuse of the court's procedures or malicious or vexatious application for liquidation, there are two alternatives available to the aggrieved party. First, they can claim damages in terms of section 7, by proving that they sustained damages by reason of the application and, second, in terms of section 174(6), the defendant or respondent applies to the court and satisfies the court that the proceedings are frivolous or vexatious. If the court is satisfied, the liquidator or administrator needs to provide security for costs for such a proceeding. Both of these sections are subject to satisfying the court that proceedings result in an abuse or are malicious or vexatious applications. It can be deduced from these provisions that the court has wide powers in granting such orders, and this is greater protection and relief for the parties that will be aggrieved as a result such vexatious proceedings.

### **3. Application of the Companies Act 61 of 1973 and Companies Act 71 of 2008**

The Draft Insolvency Bill of 2015 regulates the winding-up of consumer and corporate insolvency and has combined the provisions relating to the winding-up of solvent and insolvent companies. The Draft Insolvency Bill of 2015 does not contain any proviso with regard to the repeal of the 1973 Companies Act and the 2008 Companies Act in respect to the winding-up and liquidation of companies. In the absence of such a clause the winding-up and liquidation of companies is regulated by three pieces of legislation, namely, the 1973 Companies Act, the 2008 Companies Act and the new Insolvency Act (based on the Draft Insolvency Bill of 2015).

It is unclear whether the Draft Insolvency Bill of 2015 can be viewed as alternative legislation that has been brought into force to adequately provide for the winding-up and liquidation of insolvent companies as is contained in Schedule 5, item 9(4) of the new



Companies Act. Item 9(4) of schedule 5 to the 2008 Companies Act specifies that Chapter 14 of the old Companies Act must continue in force until such new legislation, dealing with insolvent companies, is in place. The Draft Insolvency Bill of 2015 does not contain a provision on whether a new Insolvency Act, based on the Draft Insolvency Bill of 2015, replaces the 1973 Companies Act relating to the winding-up and liquidation of insolvent companies.

The definition section in the Draft Insolvency Bill of 2015 refers only to the Companies Act 71 of 2008 under the definition of “Companies Act”. Therefore, there is uncertainty whether Chapter 14 of the 1973 Companies Act will continue to apply once the Draft Insolvency Bill is promulgated in a formal Insolvency Act. The Draft Insolvency Bill of 2015 is silent on the application of the 1973 Companies Act and it is uncertain whether Chapter 14 will have continued application or would be repealed once the Draft Insolvency Bill is formalized.

Lastly, the Draft Insolvency Bill of 2015 makes no provision for conflicts which may arise from the Companies Acts of 1973 and 2008 and the Draft Insolvency Bill of 2015, in respect to the winding-up of companies. It is not clear which Act will prevail if there is a conflict: this situation would lead to unnecessary litigation for the courts to resolve. Furthermore, there is no specific provision in cases where the Draft Insolvency Bill of 2015 is silent on certain issues, or the matter is excluded with regard to the winding-up of companies, if the issue previously has been regulated either by the Companies Act of 1973 or of 2008. It is unclear on whether or not the provisions of the 2008 Companies Act can be relied on to fill in any gaps that may arise from the Draft Insolvency Bill of 2015.

#### **4. Conclusion**

The Draft Insolvency Bill of 2015, although not an official draft bill, can be seen as the first tangible step by South African legislative structures to undertake proper insolvency reform in South Africa. The Draft Insolvency Bill of 2015 has been in the process of drafting and its preceding versions have been under scrutiny for a number of years and is yet to be promulgated as a formal Draft Bill before it enters the formal legislative

process. This delay possibly could be the result of a number of unresolved issues in the unification of insolvency laws which have been detected in our insolvency regime.

The Draft Insolvency Bill of 2015 can be seen as a step towards implementing a unified insolvency legislation and law reform in South Africa. It is submitted that even in its current format the Draft Insolvency Bill of 2015 will resolve many of the uncertainties that have arisen due to the duality of the 1973 Companies Act and the 2008 Companies Act. The new system seems to create more certainty in winding-up provisions and harmonizes the provisions relating to the winding-up of companies. It will also be a better fit with the other insolvency provisions provided for in the Draft Insolvency Bill of 2015.

## **Chapter 6: Conclusion**

The aim of the dissertation is to suggest a unified approach, at least, in respect of the winding-up of companies and ultimately the adoption of a single piece of legislation to reflect it. Currently, the winding-up of companies is governed by two companies Acts. The Companies Act 61 of 1973 regulates the winding-up and liquidation of insolvent companies; while the Companies Act 71 of 2008 regulates the winding-up of solvent companies. The insolvency law, including the Insolvency Act of 1936, also applies in part to the winding-up of a company unable to pay its debt. In view of the dual statutes, the dissertation proposes a single Act, combining both Acts into one Act.

Chapter 2 purports to show that consumer and corporate insolvency historically has developed at a different pace over time, in South Africa. Although consumer insolvency developed much earlier than corporate insolvency, towards the latter part of the 20<sup>th</sup> Century, it has evolved into a separate and identifiable area of law.<sup>157</sup> From this chapter, it is evident that South African insolvency law is based on a hybrid system of Roman Dutch and English law principles.

In South Africa there are different sources administering different areas of insolvency in South Africa. Many countries have recently adopted a unified approach to their insolvency regimes. In considering the advantages and disadvantages of a unified system it can be observed that a unified system would be beneficial in the South African context as it would create simplicity.<sup>158</sup> Unified insolvency statutes in other jurisdictions serve as a benchmark through understanding their respective reform processes and philosophies. In the English system, on which South African insolvency law is based, unification process that was not perfected because the English legislature did not implement all the recommendations made by the Cork Committee.<sup>159</sup> The study of the US Bankruptcy Code shows how the United States of America, one of the first to implement unified insolvency laws, has been successful insolvency laws, which was

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<sup>157</sup> See par 3, Chapter 2.

<sup>158</sup> See par 2, Chapter 3.

<sup>159</sup> See par 3, Chapter 3.

achieved through successful integration.<sup>160</sup> In adopting bankruptcy laws which suite the unique environment of the US it has achieved harmonization. South Africa can learn from these jurisdictions in implementing unified insolvency laws.<sup>161</sup>

The current situation in South Africa, marked by a duality of company law statutes in relation to winding-up and liquidation gives rise to various and, in some instances, unresolved interpretational issues. As discussed in chapter 4 of the dissertation, Chapter 14 of the previous Companies Act continues to apply, as is provided for in Item 9 of Schedule 5 contained in the new Companies Act.<sup>162</sup> As a result many aspects which have been left out of Chapter 14, but are linked to the winding-up of companies, create a gap in law. As discussed, an example is the exclusion of the definition of “solvent” and “insolvent”: after a number of cases the Supreme Court in *Boschpoort* confirmed that “solvency” refers to commercial (in) solvency.<sup>163</sup> Similarly, there is no provision for security for costs, which was previously contained in the 1973 Companies Act. The *Boost* judgement has brought about certainty in that security for costs must be furnished by *incola* companies.<sup>164</sup> Chapter 4, thus demonstrates that the duality of laws creates a number of uncertainties and problems which could have been avoided and results in unnecessary litigation. It is now left to the courts to resolve such issues by interpreting the sometimes conflicting provisions of the various pieces of legislation causing unnecessary delays and costs.

It is submitted in view of South Africa’s unique history, that it would be more advantageous to adopt unified insolvency legislation, especially in the context of harmonizing the winding-up of solvent and insolvent companies.<sup>165</sup> As observed from other jurisdictions who have successfully implemented unified insolvency laws it is important for South Africa to take cognizance of the distinct characteristics of consumer and corporate insolvency, and to incorporate common provisions where they are

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<sup>160</sup> See par 4, Chapter 3.

<sup>161</sup> See par 5, Chapter 3.

<sup>162</sup> See par 2 and 3, Chapter 4.

<sup>163</sup> See par 4.1, Chapter 4.

<sup>164</sup> See par 4.2, Chapter 4.

<sup>165</sup> See par 2, Chapter 2.

applicable.<sup>166</sup> If existing legislation works well, this legislation can be duplicated in a unified legislation. The Draft Insolvency Bill attempts to incorporate the winding-up provisions of 2008 Companies Act together with the provisions of the 1973 Companies Act by providing for the winding-up of solvent and insolvent companies, and by creating common provisions for both processes.<sup>167</sup> It also incorporates the corporate insolvency provisions into the general principles of insolvency, hence providing a unified model.

In relation to the winding-up and liquidation in which solvent and insolvent liquidation provisions have been combined, the Draft Insolvency Bill of 2015 can be viewed as an important step forward in improving our insolvency regime.<sup>168</sup> Not only will the Draft Insolvency Bill of 2015 resolve past and present issues and conflicts that have arisen from the duality of statutes in company legislation, but it is submitted that it will also make legislation more accessible and easier to understand. Nevertheless, the effect of the winding-up provisions in the Companies Acts 1973 and 2008 remains somewhat unsatisfactory at present.<sup>169</sup>

In conclusion, the Draft Insolvency Bill of 2015 will bring certainty to some contentious issues relating to the winding-up and liquidation of companies:<sup>170</sup> the Draft Insolvency Bill of 2015 will bring about an improvement in South African insolvency law as a whole.

It must however be noted that the Draft Bill of 2015 is not even a formal bill yet and given the time span since the advent of insolvency law reform in the 1980's, a new insolvency Act may still be years away. Hence, as an interim measure, and if the broad insolvency law reform project remains stagnant, it is submitted that the liquidation provisions of the 2008 Companies Act and Chapter 14 of the 1973 Companies Act, be revisited with the view of providing harmonized provisions for both solvent and insolvent

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<sup>166</sup> See par 5, Chapter 3.

<sup>167</sup> See par 2, Chapter 5.

<sup>168</sup> *Ibid.*

<sup>169</sup> See par 5, Chapter 4 and par 3, Chapter 5.

<sup>170</sup> For example, Chapter 4 of the dissertation discusses the distinction between solvent and insolvent companies and the provisions that apply. The Draft Insolvency Bill of 2015 has abolished this distinction and has made the sections applying to the liquidation and winding-up of companies equally applicable to both types of companies. Provision for security for costs was excluded in the Companies Act 71 of 2008 which led to uncertainty and unnecessary litigation. The Draft Insolvency Bill of 2015 clearly provides relief for parties that have suffered damage or are being inconvenienced by vexatious and malicious proceedings.

corporate insolvencies in the 2008 Companies Act. The reason for this is that the current state of affairs causes interpretational difficulties as indicated and it's not conducive for current insolvency practice.<sup>171</sup>

Lastly, it remains vital to embrace the attempts by the South African Law Reform Commission and the Department of Justice and Constitutional Development as the preferred option to do away with scattered pieces of legislation, particularly in company law, and by eliminating the distinction between solvent and insolvent companies, and to bring the law on par with best international practices.

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<sup>171</sup> See par 4 and 5, Chapter 4.

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