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THE ADVANTAGE TO CREDITORS UNDER THE INSOLVENCY ACT 24 OF 1936

BY

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CHAPTER 1:

INTRODUCTION

SUMMARY

1. Introduction
 - 1.1 Background Information
 - 1.2 Problem statement and research objectives
 - 1.3 Methodology
 - 1.4 Delineation and limitations
 - 1.5 Proposed Structure
-

1.1 Background information

Insolvency law in South Africa is codified in three main statutory instruments, the most significant of which is the Insolvency Act.¹ There are also alternative insolvency procedures which are provided for by the Magistrates' Courts Act(MCA)² which introduces the administration order procedure.³ Alternatively, there is also the National Credit Act(NCA)⁴ which introduces debt review⁵ as an alternative to sequestration.

This study will focus on one of the requirements of the sequestration process namely the advantage to creditors requirement, which is established under the Insolvency Act. The Insolvency Act is one of the oldest pieces of insolvency legislation in South Africa having been introduced in 1936 and has therefore been law for over one hundred years.

¹ Act 24 of 1936.

² Act 32 of 1944.

³ See ss 74 and 74A to 74W of the Magistrates' Court Act 32 of 1944.

⁴ Act 34 of 2005.

⁵ See s 86 of the NCA.



The sequestration process provides for a procedure which is used to sequester a debtor's estate. Under South African insolvency law, a debtor's estate may be sequestered by voluntary surrender where a debtor applies for sequestration of his own estate⁶ or by way of compulsory sequestration,⁷ where creditors apply for the sequestration of the debtor's estate. Of late, an interesting phenomenon called a friendly sequestration has emerged as a result of insolvent debtor's quest to get a fresh start, that is, to obtain a discharge of all pre-sequestration debt.⁸ This procedure will also be discussed in this dissertation.

At the heart of the sequestration process is the requirement for advantage to creditors.⁹ Although the phrase 'advantage to creditors' is not defined in the Insolvency Act, the courts have, in the past, constantly alluded to the dictum in *Meskin & Co v Friedman* (1948 2 SA 555 (W) 559) that there must be a 'reasonable prospect that some pecuniary benefit will result to creditors'.¹⁰ Accordingly, in order for a debtor to succeed with an application for voluntary surrender, the Insolvency Act requires the debtor to show that sequestration will be to the advantage of his creditors.¹¹ Likewise in compulsory sequestration,¹² the courts require the debtor to show that the sequestration of the debtors' estate will be to the advantage of creditors.¹³

With respect to voluntary surrender, the Insolvency Act stipulates that the insolvent debtor proves to the court that there is reason to believe that the sequestration of his estate will be to the advantage of his creditors.¹⁴ Judge Bertlesmann echoed the same sentiments in *Ex parte Ogunlaja and Others*:¹⁵

⁶ Ss 3-7 of the Insolvency Act 24 of 1936.

⁷ Ss 9-12 of the Insolvency Act.

⁸ S 129 (1)(b) of the Insolvency Act.

⁹ Roestoff & Boraine "Body Corporate Palm Lane v Masinge: Discretion and powers of the court in applications for sequestration" 2013 *De Jure* 208.

¹⁰ Roestoff & Boraine 2013 *De Jure* 211.

¹¹ S 10(c) of the Insolvency Act.

¹² S 3(1) of the Insolvency Act.

¹³ See s 6(1) of the Insolvency Act. See also *Ex Parte Collins* (1927) WLD 172.

¹⁴ Ss 6(1), 10(c) and 12(1).

¹⁵ 2011 JOL 27029 (JNP) para 36.



“Unless and until the Insolvency Act is amended, the South African Insolvency law requires an advantage to creditors before the estate of an individual can be sequestrated. Much as the troubled economic times might engender sympathy for debtors whose financial burden has become too much to bear, the insolvency law seeks to protect the interests of creditors at least to the extent that a minimum advantage must be ensured for the concurrent creditor when the hand of the law is laid on the insolvent.”

The advantage to creditors requirement has also been emphasised in several court judgments as the key requirement in obtaining a sequestration order and these cases will be discussed at a later stage in this dissertation. This dissertation will also explore the alternatives to sequestration such as debt review as provided in the NCA and administration as provided for in the MCA. Lastly the research will compare the advantage to creditors requirement as an access requirement to formal sequestration in South Africa, with the requirements for access to formal sequestration in other jurisdictions such as the Australia, and the United States of America and suggest proposals for reform.

1.2 Problem statement and research objectives

The advantage for creditors requirement is the point of departure for a debtor who is desirous of benefiting from debt relief provided by the sequestration procedure.¹⁶ An over indebted debtor will not meet the threshold to access formal sequestration processes unless they can prove that it will be to the advantage of creditors.¹⁷ In *Ex Parte Matthysen et uxor (First Rand Bank Ltd intervening)*,¹⁸ the court held that there must be enough assets in the estate to cover all costs of the sequestration and yield not negligible dividend to creditors.

The MCA¹⁹ also provides for administration as another legislative tool to assist the over-indebted consumer. The administration has been described as a modified form of

¹⁶ See Par 2.2.

¹⁷ See Par 2.3.

¹⁸ 2003 (2) SA 308 (T) 311J 312G.

¹⁹ S 74 of the MCA.



insolvency proceedings and it is intended to deal with relatively small estates where the costs of sequestration would exhaust the estate.²⁰ However, this statutory instrument also places significant importance on the debtor's earnings and without constant income, a debtor will not qualify for administration as it aims to reduce the debtor's monthly repayments to an amount that the debtor can afford. It is submitted, therefore, that administration does not provide an over-indebted debtor with immediate relief as the debtor will have to repay the debt over a longer period to obtain relief.

Although sequestration may offer some relief with regards to pre sequestration debt, it is not the aim of the sequestration procedure to provide relief to debtors.²¹ For this reason, debt relief occurs when sequestration is automatically terminated after a period of ten years from the date of sequestration or when the insolvent applies to court to be rehabilitated.²²

The advantage to creditors requirement is the reason why the South African insolvency legislation being regarded as pro-creditor.²³ Despite having been law for almost one hundred years, the South African Law Reform Commission has recommended the retention of the advantage to creditors requirement.²⁴

In summary the objectives of the study are therefore:

- a) To evaluate the natural person insolvency system as a whole, with particular attention to sequestration, debt review and administration;
- b) To specifically evaluate the advantage to creditors' requirement and whether it should be retained;

²⁰ Kelly-Louw, Nehf & Rott *The Future of Consumer Credit Regulation: Creative Approaches to Emerging Problems* (2008) 194.

²¹ See chapter 2 para 2.2 for a detailed discussion on sequestration.

²² S 127A (1).

²³ See Ss 6(1), 10(c) and 12(1) of the Insolvency Act. See also Boraine *et al* "The Pro-Creditor Approach in South African Insolvency law and the Possible impact of the Constitution" 2015 *NIBLeJ* 61.

²⁴ Roestoff & Coetzee "Debt relief for South African NINA debtors and what can be learned from the European Approach" 2017 *CILSA* 251.



- c) To compare the advantage to creditors requirement in South Africa with international trends as regards access requirements in Europe and the United States of America; and
- d) To look at international guidelines specifically on access to formal sequestration or debt relief measures;

1.3 Methodology

The method which will be followed in this research will entail a literary study of legislation, case law, books, journals, reports and thesis. The research will investigate the South African insolvency legislation, particularly the advantage requirement for sequestration, debt review and administration and how the requirement has affected the development of insolvency law in South Africa.

1.4 Delineation and limitations

This research will focus on the South African natural persons' insolvency legislation, in particular, the advantage to creditors' requirement as an access requirement to formal insolvency procedures. In as much as there are other access requirements to sequestration, they will not be the focal point of this dissertation.

1.5 Proposed structure

- a) Chapter one provides a general introduction to the subject of advantage to creditors as well as a historical background. The research objectives and problem statement are also discussed. The chapter also discusses the methodology as well as delineation and limitations.
- b) Chapter two discusses the debt relief measures that are available to natural person debtors in South African insolvency law. Sequestration is discussed as well as debt review and administration with a view to ascertain whether the debt relief measures provide discharge from debt.
- c) Chapter three deals with the advantage to creditors requirement, the requirement is critically evaluated especially with regards to its effect on debt relief, impact on



law reform and how the courts have applied the advantage requirement in various decisions.

- d) In Chapter four, International trends in consumer insolvency are discussed. Australia and the United States of America are juxtaposed with the South Africa system and comparisons are drawn especially with regards to access requirements to formal insolvency.
- e) Chapter five is the conclusion. It summarizes the whole discussion on advantage to creditors and recommendations are made concerning the advantage to creditors requirement and how it affects natural person debt relief and law reform.



CHAPTER 2:

DEBT RELIEF MEASURES IN TERMS OF SOUTH AFRICAN INSOLVENCY LAW

SUMMARY

- 2.1 Introduction
 - 2.2 Sequestration
 - 2.3 Debt Review
 - 2.4 Administration Order
 - 2.5 Proposed pre-liquidation composition
 - 2.6 National Credit Amendment Act
 - 2.7 Conclusion
-

2.1 Introduction

Debt relief has been at the centre of recent law reform initiatives in natural person insolvency law.²⁵ The most recent development being the National Credit Amendment Act.²⁶ This comes as a result of the lawmakers realising that the existing debt relief measures are inadequate in addressing debt relief. This chapter will discuss the existing debt relief measures which are sequestration, debt review, administration, the proposed pre- liquidation composition²⁷ and debt intervention.²⁸

2.2 Sequestration

²⁵ The South African Law Reform Commission made several propositions aimed at reforming natural person insolvency law such as, the Draft Insolvency Bill of 1996, The Draft Insolvency Bill of 2003, The proposed Unified Insolvency Act of 2003 and finally the Insolvency Bill of 2015.

²⁶ Act 7 of 2019.

²⁷ The South African Law Reform Commission proposed an Insolvency Bill which proposes a debt relief measure known as pre- liquidation composition.

²⁸ S 86A of the NCA. Debt intervention is introduced in the Debt Relief Act as an amendment to the NCA.



A sequestration order is defined in section 2 of the Insolvency Act as any order of Court whereby an estate is sequestrated, including a provisional order when it has not been set aside.²⁹ Sequestration brings about debt relief in that it results in the discharge of pre-sequestration debts.³⁰ The discharge takes place as a result of automatic rehabilitation after ten years from the date of sequestration,³¹ or after an application to court for rehabilitation.³² As indicated,³³ in terms of the Insolvency Act, there are three ways in which a debtor's estate may be sequestrated, namely; voluntary surrender, compulsory sequestration or a so-called friendly sequestration, which is in actual fact a compulsory sequestration. These procedures will be discussed hereunder.

2.2.1 Voluntary surrender

A debtor who wishes to surrender his estate has to publish a notice of surrender in the government gazette and in the newspaper circulating in the district in which he resides, or in which his principle place of business is located.³⁴ An application for surrender may be brought by the insolvent debtor himself or his agent or any person interested with the administration of the estate of a deceased insolvent debtor, or an insolvent debtor who is incapable of managing his affairs.³⁵

The court will accept the surrender of the debtor's estate only if it is satisfied of three aspects, namely:³⁶

a) *Actual insolvency*

The debtor has to show that they are actually insolvent and that their liabilities exceed their assets.³⁷ In the decided case of *Ex Parte Harmse*,³⁸ the court explained the meaning of insolvency with reference to section 6(1) of the Insolvency Act to mean that it must be

²⁹ S 2 of the Insolvency Act.

³⁰ S 129(1)(b) of the Insolvency Act.

³¹ S 128A of the Insolvency Act.

³² S 124(1) of the Insolvency Act.

³³ Chapter 1, para 1.1.

³⁴ S 4(1) of the Insolvency Act.

³⁵ S 3(1) of the Insolvency Act.

³⁶ S6(1) of the Insolvency Act.

³⁷ Davis "Step-by-Step Voluntary Surrender: Application for the voluntary surrender of a debtor's estate" 2000 *De Rebus* 34.

³⁸ 2005 (1) SA 323 (N) 362.



established that the debtor is without funds to pay his debts in full and that it is improbable that the assets will realize enough for this purpose.

b) *Sufficient free residue to pay the costs of sequestration*

The debtor must also show that there are sufficient assets in the free residue to defray the costs of the sequestration.³⁹ The phrase “free residue” is defined in section 2 of the Insolvency Act as that portion of the estate which is not subject to any right of preferences by reason of any special mortgage, legal hypothec, pledge or right of retention.⁴⁰

c) *Sequestration must be to the advantage of creditors*

As indicated,⁴¹ the Insolvency Act does not define advantage for creditors, however, the courts have helped in shedding light on the intention of the legislature. In *Trust Wholesalers and Woolens (Pty) Ltd v Mackan*⁴² the Court defined advantage to creditors to mean, “a substantial portion of the creditors, determined according to the value of the claims, will derive advantage from the sequestration”. In *London Estates (Pty) Ltd v Nair*,⁴³ the court reiterated further that there will be advantage for creditors if a reasonable prospect that there will a pecuniary benefit to creditors is established. Again in *Ex Parte Matthysen et Uxo (First Rand Bank intervening)*,⁴⁴ it was submitted that for the sequestration of an estate to be to the advantage of creditors, the applicant for surrender must show that a not negligible dividend will be paid to creditors.

2.2.2 Compulsory sequestration

³⁹ Davis 2000 *De Rebus* 34.

⁴⁰ See S 2 of the Insolvency Act.

⁴¹ Chapter 1, para 1.1.

⁴² 1954 (2) SA 109 (N).

⁴³ 1957 (3) SA 591 (N).

⁴⁴ 2003 (2) SA. 308 (T) 316B-C.



Compulsory sequestration is another way in which a debtor's estate may be sequestrated. An application for compulsory sequestration is initiated by the debtors' creditors.⁴⁵ The Court may grant an application for the sequestration of the debtor's estate if it is satisfied that a creditor or his agent who has a liquidated claim for not less than R100, or two or more creditors (or their agents) claims for not less than R200 against a debtor who has committed an act of insolvency or is insolvent,⁴⁶ and finally if there is reason to believe that it will be to the advantage of the debtor if his estate is sequestrated,⁴⁷ a provisional sequestration order will be granted. If t the return date of the *rule nisi* the court establishes that there is reason to believe that sequestration will be to the advantage of creditors,⁴⁸ a final sequestration order will be granted.

The most notable difference between a voluntary surrender and a compulsory sequestration is that in compulsory sequestration the onus of satisfying the court rests on the sequestrating creditor.⁴⁹ Furthermore, with respect to the advantage to creditors' requirement, in compulsory sequestration the creditor is required to show that there is a reason to believe that sequestration will be to the advantage of the creditors,⁵⁰ while in voluntary surrender the debtor is required to show that sequestration will be to the advantage of creditors.⁵¹

In explaining the concept of advantage to creditors, the Court in *Gardee v Dharmanta Holdings and Others*,⁵² held that sequestration will only be to the advantage of the creditors if it will result in a greater dividend to them than would otherwise be the case, for example, through the setting aside of impeccable transactions, or the exposure of concealed assets, or if it will prevent an unfair division of the proceeds of the assets or some creditors being preferred to others.

⁴⁵ S 9(1) of the Insolvency Act.

⁴⁶ *Ibid.*

⁴⁷ S 10 of the Insolvency Act.

⁴⁸ S 12 of the Insolvency Act.

⁴⁹ *Braithwaite v Gilbert* 1984 SA 717 (W) 718.

⁵⁰ S 12(1) of the Insolvency Act.

⁵¹ S 6(1).

⁵² 1978 (1) SA 1066 (N) 1068-7.



2.2.3 Friendly Sequestration

The Insolvency Act does not explicitly provide for a friendly sequestration. However, this concept has been developed in practice. In a friendly sequestration a debtor's estate is sequestrated by an amicable creditor.⁵³ However, the courts have submitted that "the mere fact that an application for compulsory sequestration is brought by a creditor who is prepared to cooperate with the debtor, or who is motivated by a desire to assist the debtor, does not preclude the granting of a sequestration order.⁵⁴ In fact, the court has a discretion to either grant or refuse an order of sequestration.⁵⁵ Accordingly, where it is clear that there is an abuse of the process of the court, this discretion is exercised against the granting of such an order.⁵⁶

2.2.4 Rehabilitation

According to Bertelsmann,⁵⁷ insolvency of a natural person debtor comes to an end when he is rehabilitated.⁵⁸ Rehabilitation enables the insolvent to make a fresh start, free from his pre sequestration debts.⁵⁹ An insolvent who is not rehabilitated by the court within a period of ten years from the date of sequestration of his estate would be deemed to be rehabilitated after the expiry the ten years from date of sequestration.⁶⁰

Bertelsmann⁶¹ stipulates that the principle of rehabilitation and the concomitant release of pre sequestration debts was introduced in South African insolvency law via the Roman Dutch law under the Amsterdam Ordinance of 1771. It is therefore interesting to note that although it has been argued that discharge from pre-sequestration debt was not the intention of legislature in implementing the sequestration procedure, a procedure for

⁵³ Chitimira & Mabina "The meaning of advantage to creditors under voluntary, compulsory and friendly sequestration" 2019 *AUDJ* 75.

⁵⁴ *Jhatam & Others v Jhatham* 1958(4) SA 36 (N); *Van Rooyen v Van Rooyen (Automutual Investments (EC) (Pty) Ltd, Intervening creditor* (2002) (1) SA 689 (C) 703.

⁵⁵ Evans "Friendly Sequestrations, the Abuse of the process of court and possible solutions for overburdened debtors" 2001 *SA Merc LJ* 485.

⁵⁶ Evans 2001 *SA Merc LJ* 485.

⁵⁷ Bertelsmann *et al Mars - The Law of Insolvency in South Africa* (2019) 555.

⁵⁸ S 124 of the Insolvency Act.

⁵⁹ Bertelsmann *et al* (2019) 555.

⁶⁰ S 127A of the Insolvency Act.

⁶¹ Bertelsmann *et al* (2019) 555.



discharge of pre sequestration debts which is rehabilitation has always been entrenched in insolvency law as far back as 1771.⁶²

In terms of section 129(1) of the Insolvency Act, rehabilitation has the effect of putting an end to sequestration and relieving the insolvent of every disability resulting from sequestration and discharges all his debts, which were due or the cause of which arose before sequestration.

Roestoff and Coetzee⁶³ believe that debt relief is not the main aim of the sequestration procedure and that the discharge is mostly a coincidence. They submit further that requirements for sequestration do not include the so-called 'No Income No Assets' (NINA) debtors⁶⁴ in that for a debtor to succeed with obtaining a sequestration order he has to prove advantage to the creditors. They argue that the fact that sufficient assets are set as an access requirement are not only for the purpose of covering sequestration costs, but also to ensure an advantage to creditors.⁶⁵ It is also argued that the cost of sequestration is another factor that curtails access and makes sequestration unsuitable as a debt relief measure especially for NINA debtors.⁶⁶

Sequestration has not been very helpful as a debt relief measure because of the nature of the proceedings which require the process to be conducted in the High Court.⁶⁷ As sequestration order affects the status of natural persons, the High Court has to be approached and this results in higher legal costs as the debtor has to pay for representation, thereby increasing the costs of sequestration.⁶⁸ Sequestration was designed as a mechanism for substantially large estates and therefore the cost to a debtor with a smaller estate will be higher.

⁶² *Ibid.*

⁶³ Roestoff & Coetzee 2017 *CILSA* 254.

⁶⁴ Roestoff & Coetzee 2017 *CILSA* 256.

⁶⁵ *Ibid.*

⁶⁶ *Ibid.*

⁶⁷ S 2 of the Insolvency Act defines a court in relation to any matter as the provincial and or local divisions of the Supreme Court which has jurisdiction in that matter.

⁶⁸ Roestoff & Coetzee 2017 *CILSA* 259.



It may thus be argued that although sequestration leads to a legal discharge of debt,⁶⁹ discharge is accidental⁷⁰ and not the primary objective of the legislator with regards to sequestration proceedings.

2.3 Debt Review

The debt review procedure has been introduced by section 86 of the NCA.⁷¹ A consumer applies to a debt counsellor to be declared over indebted.⁷² Once the application has been made, a debtor obtains a type of moratorium and creditors are precluded from enforcing by litigation or other judicial process any right or security they may have against the debtor in terms of the credit agreement.⁷³

The overarching purpose of debt review as enshrined in the NCA is to offer temporary relief to over indebted debtors.⁷⁴ If a debt counsellor is satisfied that a consumer is over indebted, he may make a proposal to the Magistrates court to make orders which include an order that one or more of the consumer's credit agreement be declared reckless credit.⁷⁵ A court may also make an order for the extension of the period of the credit agreement and reduction of the instalment that the debtor ought to pay.⁷⁶

Unlike compulsory sequestration, debt review can only be initiated by the debtor himself,⁷⁷ or by any court hearing a matter where a credit agreement is being considered and where it is alleged that the debtor is over indebted.⁷⁸ The debtor retains control of his estate and does not lose control as in the case of sequestration. The debtor is expected to participate

⁶⁹ See s 129 of the Insolvency Act.

⁷⁰ *Ex Parte Ford* 2009 3 SA 376 (WCC) 383.

⁷¹ The National Credit Act.

⁷² S 86(1) of the NCA.

⁷³ S 88(3) of the NCA.

⁷⁴ *Roestoff et al* "The debt counselling process – closing the loopholes in the National Credit Act 34 of 2005" 2009 *PER* 253.

⁷⁵ S 86(7) (c) of the NCA.

⁷⁶ S 86(7) (aa) (bb) (cc) (dd) of the NCA.

⁷⁷ S 86 (1) of the NCA.

⁷⁸ S 85 of the NCA.



in good faith in the review and in any negotiations designed to result in responsible debt re-arrangement.⁷⁹

The limitation of debt review as a debt relief measure is the fact that the NCA is only applicable to credit agreements, and debt which does not fall within the ambit of the Act⁸⁰ will not be rearranged or extinguished as in the case where debt review is applicable.

Some scholars⁸¹ are of the view that debt review has proved to be insufficient as a debt relief measure because of, *inter alia*, the following reasons: firstly, there has been a sharp increase in the number of consumers applying for debt review; secondly, there has been a concomitant shortage of competent debt counsellors; and thirdly, although an application for debt review precludes credit providers from taking legal action against the consumer, nothing stops the credit providers from pursuing the debt. In essence there is no effective moratorium and consumers will suffer double jeopardy in that if a particular creditor refuses to accept the offer made under debt review, they will proceed to enforce their rights against the debtor.

Debt review therefore does not provide discharge from debt as it merely amounts to a debt rescheduling mechanism.

2.4 Administration Order

According to Coetzee,⁸² the administration order involves a relatively simple and inexpensive procedure whereby the Magistrate's court reschedules overcommitted debtor's obligations. In the case of *Bafana Finance Mabopane v Mokwakwa*,⁸³ the court submitted that the purpose of an administrative order is to protect debtors with small estates, usually those who are poor and either illiterate or unformed about the law or both. The court further emphasised that this procedure is also meant to ensure that

⁷⁹ S 86 5(a)(b) of the NCA.

⁸⁰ Such as delictual claims, professional services and municipal accounts where no interest is charged.

⁸¹ Roestoff *et al* 2009 *PER* 251.

⁸² Coetzee *A comparative reappraisal of debt relief measures for natural person debtors in South Africa* (LLD thesis 2014 UP) 172.

⁸³ 2006 (4) SA 581 (SCA).



creditors to whom money is owed and due for payment by the debtor are able to recover as much as the administrator permit.⁸⁴

According to Boraine,⁸⁵ the administration procedure is a hybrid debt relief measure which makes provision for debt rescheduling and realisation of assets to service debts. As such, it is submitted that there is no real relief from debt that can be obtained through the administration order procedure as it does not lead to a discharge of debts.

When considering the effectiveness of the administration order procedure as a debt relief measure, one has to also take into account the provisions of section 74⁸⁶ which states that the granting of an order under section 74(1) shall be no bar to the sequestration of the debtor's estate. This simply means that a debtor cannot just rely on administration order procedure as he may be sequestrated while in the process of obtaining an administration order.

The administration order procedure is only available to debtors whose debts do not exceed R50 000.⁸⁷ As such it excludes debtors whose estate are more than R50 000 but who are also over indebted.⁸⁸ This amount is determined by the Minister of Justice from time to time.⁸⁹

The MCA does not provide a time frame for the termination of the administration order. The administration process will terminate when all the creditors as well as the costs of administration have been paid in full.⁹⁰ By implication, administration promotes the notion of advantage to creditors in that it ensures that the original debt is paid in full despite how long it takes the debtor to pay off. As such, as a debt relief measure, administration is devoid of discharge from debts.

⁸⁴ *Ibid.*

⁸⁵ Boraine 2012 *De Jure* 87.

⁸⁶ The Magistrates' Court Act.

⁸⁷ Mabe 'Alternatives to Bankruptcy in South Africa that provides for a discharge of debts: Lessons from Kenya' 2019 *PER* 7.

⁸⁸ Mabe 2019 *PER* 7.

⁸⁹ *Ibid.*

⁹⁰ S 74 of the MCA.



In *African Bank Ltd v Weiner*,⁹¹ Griesel J submitted that “the mechanism of an administration order is intended to provide the debtor with relatively short moratorium to assist in the payment of his or her debts in full and to ward off legal action and execution proceedings...”

From the above, it can be seen that even the courts do not view the administration order procedure as a debt relief mechanism, but rather as a way for a debtor to obtain a temporary moratorium, which if he fails to pay off the debt in full may still be sequestered.

2.5 Proposed pre-liquidation composition

A draft Insolvency bill was introduced by the South African Law Reform Commission.⁹² The Bill proposes a debt-relief measure known as a “pre-liquidation composition”. In particular, clause 118 stipulates that the requirement is that liquidation of the estate of a natural person debtor should be advantageous to the creditors, therefore, liquidation is unavailable if the unencumbered assets are not adequate to warrant liquidation. Hence, provision must be made for debtors with little or no assets, who through no fault of their own are unable to pay their debts.⁹³

In pre-liquidation composition, a debtor who cannot pay his debts enters into a binding agreement with his creditors, called a composition.⁹⁴ The debt must not be less than R200 000.⁹⁵ If the offer of composition is accepted by the required majority in number of the creditors, then the composition will be successful.⁹⁶

However, it has been argued that even the pre-liquidation composition procedure does not really offer debt relief to debtors⁹⁷ in that the procedure would only assist those who already have some form of statutory recourse available. In essence, only those with

⁹¹ 051/2004.

⁹² Coetzee “Does the proposed pre-liquidation composition proffer a solution to the No Income No Asset (NINA) debtor’s quandary and if not, what would?” 2016 *THRHR* 18.

⁹³ Cl118 of the Insolvency Bill 2019.

⁹⁴ Coetzee 2016 *THRHR* 23.

⁹⁵ Cl 118(1).

⁹⁶ Cl 118(17).

⁹⁷ Roestoff & Coetzee 2017 *CILSA* 251.



income and assets will be able to succeed in the compulsory negotiation phase. Roestoff and Coetzee submit further that the proposed pre composition procedure involves costs which NINA Debtors will not be able to pay.⁹⁸

Coetzee⁹⁹ further suggests that the aim of pre-liquidation composition is to reach a negotiated settlement between parties. The only advantage of the pre-liquidation composition is that the procedure is cheaper compared to sequestration and is more flexible.¹⁰⁰

The pre-liquidation composition as a debt relief measure falls short in that if the composition is not successful, the process collapses and there will be no debt relief for the debtor. Initially, the proposed Bill allowed for the presiding officer to convert the composition to sequestration proceedings.¹⁰¹ However, the clause was removed as it would enable debtors to avoid the advantage to creditors' requirement by accessing liquidation without proving advantage to creditors. Consequently, the pre-liquidation composition is not a viable alternative to debt relief measure as it is not too far from administration order, coupled with the fact that once it fails, the debtor does not have any other recourse but to opt for sequestration.

2.6 National Credit Amendment Act 2019

The challenges faced by South African debtors are not brought by lack of alternatives to insolvency proceedings, they are caused by the fact that the available alternatives do not provide for a discharge of debt.¹⁰² In an attempt to address this, the National Credit Amendment Act (NCAA)¹⁰³ was passed into law in August 2019. The NCAA introduces a process known as debt intervention.¹⁰⁴ Section 1 of the NCAA defines debt intervention

⁹⁸ *Ibid.*

⁹⁹ *Ibid.*

¹⁰⁰ Roestoff & Coetzee 2017 *CILSA* 251.

¹⁰¹ CI 118(16).

¹⁰² Mabe 2019 *PER* 2.

¹⁰³ Act 7 of 2019.

¹⁰⁴ S 86A of the NCA.



as a measure, as contemplated in section 86A, which aims to assist identified consumers for whom existing natural person insolvency measures are not accessible in practice.¹⁰⁵

In terms of the NCAA, for a natural person or natural persons who own a joint estate to qualify for debt intervention they must:¹⁰⁶

- a) be a consumer under unsecured credit agreements, unsecured short-term credit transactions or unsecured credit facilities;
- b) receive no income, or if they receive an income or have a right to receive an income, regardless of the source, frequency or regularity of that income, that income did not exceed R7500 on an average of six months preceding the application for debt intervention;
- c) is over-indebted, whether due to a change in personal circumstances or other circumstances; and
- d) is not sequestrated or subject to an administration order.

A person wishing to apply for debt intervention may apply to the National Credit Regulator (NCR) in a prescribed manner and form to be declared over-indebted.¹⁰⁷ Section 15A of the NCAA mandates the NCR to assist the debt intervention applicant with, inter alia, the process of being declared over-indebted,¹⁰⁸ to have their obligations re-arranged;¹⁰⁹ to have their debt intervention application considered for an order contemplated in section 87A;¹¹⁰ or to have their application for rehabilitation contemplated in section 88B considered by the Tribunal.¹¹¹

Where the intervention applicant's debts have been re-arranged, such applicant must be issued with a clearance certificate by the NCR within seven business days after they have satisfied all the obligations under every credit agreement that was subject to that was

¹⁰⁵ S 1(b) of the NCA.

¹⁰⁶ S 1(b) of the NCA.

¹⁰⁷ S 86(1)A of the NCA.

¹⁰⁸ S 15A (a) of the NCA.

¹⁰⁹ S 15A (b) of the NCA.

¹¹⁰ S 15A (c) of the NCA.

¹¹¹ S 15A (d) of the NCA.



subject to that debt re-arrangement order or agreement and according to that order or agreement¹¹² or where they have demonstrated as prescribed:¹¹³

- a) financial ability to satisfy the future obligations in terms of the re-arrangement order; or
- b) that there are no arrears on the pre-arranged agreements; and
- c) that all obligations under every credit agreement included in the re-arrangement order or agreement have been settled in full.

After the clearance certificate has been issued, the NCR must submit a copy to all registered credit bureaux.¹¹⁴ In the event that the NCR decides not to issue the clearance certificate or fails to issue it, or where the NCR fails to submit a copy of the clearance certificate to all registered credit bureaux, the debt intervention applicant may apply to the Tribunal for a review of the NCR's decision or failure to issue.¹¹⁵ The Tribunal may then, if he is satisfied that the debt intervention applicant is entitled to the certificate, order the NCR to issue a clearance certificate to the debt intervention applicant or submit a copy to all registered credit bureaux.¹¹⁶

When considering an application for debt intervention, the NCR must provide the debt intervention applicant with counselling on financial literacy as well as access to training to improve the financial literacy of the debt intervention applicant.¹¹⁷ After assessing the application for debt intervention, NCR concludes reasonably that:¹¹⁸

- a) the debt intervention applicant does not qualify for debt intervention, the NCR must reject the application;
- b) the debt intervention applicant does not qualify for debt intervention, but is nevertheless experiencing, or is likely to experience, difficulty satisfying all their obligations under the credit agreements in a timely manner, the NCR must

¹¹² S 71(1A) (a) of the NCA.

¹¹³ S 71(1A) (b) of the NCA.

¹¹⁴ S 71(1A) of the NCA.

¹¹⁵ S 71(3A) of the NCA.

¹¹⁶ *Ibid.*

¹¹⁷ S 86A (5) of the NCA.

¹¹⁸ S 86A (6) of the NCA.



- recommend that the debt intervention applicant and the respective credit providers voluntarily consider and agree on a plan of debt re-arrangement;
- c) a credit agreement that formed part of the application may constitute reckless lending, an unlawful credit agreement or a credit agreement resulting from prohibited conduct, the NCR must refer the credit agreement to the Tribunal for an appropriate declaration;
 - d) the debt intervention applicant qualifies for debt intervention and the obligations of the debt intervention applicant can be re-arranged within a period of five years or such longer period as may be prescribed, the NCR must refer the matter with a recommendation to the Tribunal in the manner and form for an order contemplated in section 87(1A); or
 - e) the debt intervention applicant qualifies for debt intervention, but their income and assets are insufficient to allow for their obligations to be re-arranged during the period of five years, the NCR must refer the matter with a recommendation to the Tribunal in the prescribed manner and form contemplated in section 87A.

In a case where the matter has been referred to the Tribunal, the matter may be considered by a single member of the Tribunal in the prescribed manner and form, referring to all documents included in the referral and any representations contemplated in section 86A (9).¹¹⁹ After considering all information provided, the Tribunal may: make an order that the debt intervention applicant does not qualify for debt intervention and reject the application;¹²⁰ or qualifying suspend all of the credit agreements, in part or in full, for 12 months, which period may be extended for one further 12 months subject to certain qualifications and require the debt intervention applicant to attend a financial literacy programme.¹²¹

Where an order for debt intervention was issued, the NCR must review the financial circumstances of the debt intervention applicant eight months after the order was granted to determine whether the debt intervention has, at that time, sufficient income or assets

¹¹⁹ S 87A (1) of the NCA.

¹²⁰ S 87A (2)(a) of the NCA.

¹²¹ S 87A (2)(b) of the NCA.



to allow their obligations to be re-arranged.¹²² If the NCR finds that the debt intervention applicant has enough income and assets to allow for their obligations to be re-arranged, the NCR must refer the matter with a recommendation to the Tribunal in a manner or form prescribed.¹²³ In the same way, if the debt intervention applicant does not have sufficient income or assets to allow for their obligations to be re-arranged, the NCR must refer the matter to the Tribunal to consider an extension of the period of suspension.¹²⁴

Where the Tribunal decides to grant the debt intervention order, the Tribunal must limit the debt intervention applicant's right to apply for credit contemplated in section 60 for a minimum of six months or for such period as the Tribunal may deem fair and reasonable.¹²⁵ Such limitation must not exceed a period of 12 months.¹²⁶ If, after granting the debt intervention order, the Tribunal finds that the debt intervention applicant was dishonest in his or her application, the Tribunal has the power to rescind or change such order.¹²⁷

Against this background, it is submitted that debt intervention fails to be an alternative debt relief measure mainly because of the earning threshold of R7 500 prescribed by the Act. This excludes a large number of over indebted debtors whose earnings are more than R7 500 per month and whose debts could be slightly more than R50 000 but who cannot service their debt.

2.7 Conclusion

The statutory debt relief measures discussed above were all introduced in consideration of the natural person debtor. However, as far as debt relief is concerned, the mechanisms fall short of effective consumer debt relief. One of the major reasons for the failure of alternative procedures to effectively address debt relief is the fact that the Insolvency Act, had already set the golden thread of advantage to creditors as far as consumer insolvency

¹²² S 87A (5)(a) of the NCA.

¹²³ S 87A (5) (b) (i) of the NCA.

¹²⁴ S 87A (5) (b) (ii) of the NCA.

¹²⁵ S 87A (8) of the NCA.

¹²⁶ S 87A (9) of the NCA.

¹²⁷ S 87A (11) of the NCA.



is involved. Whenever supplementary legislation is introduced there is always a risk of conflict with the Insolvency Act because the insolvency Act was not enacted with the intention of addressing debt relief.

Furthermore, as seen with the National Credit Amendment Act, lawmakers did not annul the advantage requirement, but circumvented it by creating the debt intervention procedure which in turn creates some form of discrimination among low income earners.¹²⁸ As such, there is not sufficient relief from the available statutory procedures and until the Insolvency Act is amended to remove the advantage requirement, there will continue to be multiple supplementary legislation aimed at addressing debt relief for natural person debtors.

¹²⁸ The Act extinguishes debts under R50 000 for debtors earning less than R7 500 per month to the exclusion of other debtors who could be earning slightly more than the gazetted salary and still have the same amount of unsecured debt.



CHAPTER 3:

ADVANTAGE TO CREDITORS REQUIREMENT

SUMMARY

- 3.1 Introduction
 - 3.2 Historical background
 - 3.3 Effect on consumer debt relief
 - 3.4 Impact on law reform
 - 3.5 Conclusion
-

3.1 Introduction

The Insolvency Act was promulgated for the sole purposes of ensuring an orderly winding up and distribution of a debtor's estate.¹²⁹ Sequestration procedures which are discussed above are prescribed by the Insolvency Act as vehicles for winding up a debtor's estate.¹³⁰ The advantage to creditors requirement is one of the access requirements for both voluntary surrender¹³¹ and compulsory sequestration.¹³² As observed,¹³³ the advantage to creditors requirement is a crucial determination in granting an order of sequestration by the courts. Accordingly, this chapter will comprehensively discuss the concept of advantage to creditors, where it originated, the effect it has on debt relief mechanisms as well as its impact on insolvency law reform.

3.2 Historical background

¹²⁹ *Walker v Syfret* NO 1911 AD 141.

¹³⁰ See chapter 2, par 2.2 and 2.3.

¹³¹ S 3(1) of the Insolvency Act.

¹³² Ss 10(c) & 12(c) of the Insolvency Act.

¹³³ Chapter 1, para 1.1.



The Insolvency Act does not define the term advantage to creditors. However, the term inherently implies a financial benefit. Advantage to creditors therefore refers to a financial advantage.¹³⁴ As indicated,¹³⁵ the court in *Meskin and Company v Friedman*¹³⁶ explained the meaning of advantage to creditors as follows:

“the facts put before the court must satisfy it that there is a reasonable prospect, not necessarily a likelihood but a prospect which is not too remote that a pecuniary benefit will result to creditors.”

The court also extended the definition to explain the meaning of creditors in this context to mean that there must be an advantage to the general body of creditors and not advantage to one creditor. The same assertion was also made in the case of *Peyke v Nathoo*.¹³⁷

The advantage to creditors’ requirement has been part of natural person insolvency and traces of this requirement can be found in Roman law under the doctrine of *missio in possessionem*.¹³⁸ This was a means of execution against a debtor’s property and as such, the debtor’s estate would be sold and would be wholly transferred to the person who offered the creditors the largest dividend to their claims.¹³⁹

The advantage to creditors’ requirement can be traced back to the Cape Ordinance¹⁴⁰ which provided for a debtor “surrendering his estate for the benefit of his creditors.”¹⁴¹ The requirement has survived several amendments to the Act and is also found in the present Act. The advantage to creditors’ requirement in a voluntary surrender is found in section 6(1) and provides that the court may accept the surrender of the debtor’s estate and grant a sequestration order when it is satisfied that:

¹³⁴ Evans 2001 SA Merc LJ 488.

¹³⁵ Chapter 1, para 1.1.

¹³⁶ 1948 (2) SA 555 (W).

¹³⁷ 1929 50 NLR 178,185.

¹³⁸ Visser “Romeinsregtelike Aanknopings-punte van die Sekwestrasieproses in the Suid-Afrikaanse Insovensiereg” 1989 *De Jure* 41.

¹³⁹ Bertelsmann *et al* (2019) 7.

¹⁴⁰ Act 6 of 1843.

¹⁴¹ Evans 2001 SA Merc LJ 488.



- a) the estate of the debtor in question is indeed insolvent;
- b) the debtor owns realisable property of sufficient value to defray all costs of the sequestration which will, in terms of this Act, be payable out of the free residue of his estate; and
- c) it will be to the advantage of creditors of the debtor if his estate is sequestrated.

Moreover, the advantage to creditors is also found in section 10 of the Insolvency Act which deals with provisional sequestration. In terms of that section, a court will grant a provisional sequestration order if there is reason to believe that it will be to the advantage of creditors if his estate is sequestrated.¹⁴² Finally, the advantage to creditors' requirement is also provided for in section 12 of the Insolvency Act, which states that a court will grant a final sequestration order if there is reason to believe that it will be to the advantage of creditors of the debtor if his estate is sequestrated.¹⁴³

It is submitted that it cannot be a mere coincidence that the Insolvency Act mentions the advantage to creditors' requirement three times in three places. The repetition of the exact same wording goes to amplify the seriousness of the lawmakers in requiring advantage to creditors in sequestration proceedings. The courts have also done a great deal of religiously applying and enforcing the advantage requirement in sequestration proceedings.¹⁴⁴

3.3 Effect on consumer debt relief

In voluntary surrender applications, a greater onus of proof is placed on the debtor to prove that the surrender of his estate will be to the advantage of creditors.¹⁴⁵ The burden of discharging this onus coupled with other formalities results in sequestration as a whole

¹⁴² S 10(c) Insolvency Act.

¹⁴³ S 12(c) Insolvency Act.

¹⁴⁴ See *Ex Parte Pillay: Mayet v Pillay* 1955(2) SA 309 (N) 311. See also *Amod v Khan* 1974 2 SA 432 (N) 438 where Hathorn JP stated that "a debtor knows all about his own affairs and can easily prove advantage to creditors."

¹⁴⁵ S 6(1) Insolvency Act.



not being a viable option for debt relief for the harassed debtor.¹⁴⁶ The debtor has to prove actual advantage.¹⁴⁷

The South African Law Reform Commission¹⁴⁸ submits that the advantage to creditors' requirement causes difficulties to overburdened debtors in proving such advantage. The advantage to creditors requirement therefore aggravates the burden which consumers already have in fulfilling other requirements for sequestration.

According to Smith,¹⁴⁹ "there is a recurrent motif or dominant thread (if thread is used in the sense of something that runs a continuous course through anything) and that is the advantage to creditors, not one creditor, or some creditors but the creditors as an entity or the *concursum creditorium*." Notwithstanding the trouble that debtors face in proving advantage in sequestration proceedings, the Insolvency Act is replete with other subtle advantage to creditors requirements which, although not specifically mentioned, are designed to benefit creditors.¹⁵⁰ For example, the provision that an insolvent spouse whose separate estate has not been sequestrated must deliver his business records and lodge a statement of affairs with the master.¹⁵¹ It is therefore clear that this provision made to cater for voidable dispositions and ultimately be to the advantage of creditors.

Section 19 of the Act deals with the attachment of property by a deputy sheriff. Although the provision does not specifically state that it is for the benefit of creditors, when read in context of the Act as a whole, it becomes apparent that the attachment of books of accounts, invoices, vouchers, cash, share certificates, bonds, bills of exchange, promissory notes and other securities¹⁵² is actually for the benefit of creditors.

¹⁴⁶ *Ex Parte Swanepoel* 1975(2) SA 367.

¹⁴⁷ Boraine *et al* 'The Pro Creditor Approach in South African Insolvency Law and the possible impact of the Constitution' 2015 *NIBLeJ* 79.

¹⁴⁸ See Explanatory memorandum 46-47.

¹⁴⁹ Smith 'The Recurrent Motif of Insolvency Act – advantage of creditors' 1985 *MBL* 28.

¹⁵⁰ *Ibid*.

¹⁵¹ See s 16 of the Insolvency Act.

¹⁵² S 19(1)(a) of the Insolvency Act.



Similarly, section 20 which deals with the effects of sequestration on an insolvent's property is also without doubt an advantage to creditors' provision. It states that an insolvent's estate shall divest from the insolvent and shall vest in the master¹⁵³ and also orders a stay of proceedings which may have been instituted against the insolvent.¹⁵⁴

Another provision which speaks to the benefit for creditors is found in section 26. It provides for the setting aside by the court of dispositions made without value by the debtor if it was made within two and half years of the sequestration.¹⁵⁵ There are other numerous provisions¹⁵⁶ in the Act which speak to the benefit for creditors. These all point out to the fact that the advantage to creditors' requirement is indeed central to the Insolvency Act in more places than where it was specifically spelt out.¹⁵⁷

3.4 Impact on law reform

The advantage to creditors requirement causes inequality in the treatment of debtors.¹⁵⁸ Many debtors are left without statutory relief in the form of statutory a discharge. The exclusion of many overburdened consumer debtors from a discharge procedure infringes their basic constitutional right to equality under the South African Constitution.¹⁵⁹

The advantage requirement is a major limitation for law reform in natural person insolvency law. The heavy burden of proof required from applicants in sequestration proceedings makes it difficult for many debtors to succeed in obtaining a sequestration order.¹⁶⁰ The advantage requirement has, as such, led to desperation among debtors and it can be argued that it is one of the reasons why the phenomenon of friendly sequestration arose. When considering friendly sequestrations, it is obvious that all other formalities for sequestration are met except for the one requirement which is the advantage to creditors' requirement.

¹⁵³ S 20 of the Insolvency Act.

¹⁵⁴ S 20(1)(b) of the Insolvency Act.

¹⁵⁵ S 26 (10) (b) of the Insolvency Act.

¹⁵⁶ See ss 29, S30, S31, S65, S115, S152 of the Insolvency Act.

¹⁵⁷ Smith 1985 *MBL* 84.

¹⁵⁸ *Harksen v Lane* 1998 (1) SA 300 CC.

¹⁵⁹ *Boraine et al* 2015 *NIBLeJ* 91.

¹⁶⁰ South African Law Commission Project 63 *Review of the Law of insolvency* 41.



3.5 Conclusion

Roestoff and Coetzee¹⁶¹ submit that sequestration is an expensive process and should only be resorted to when it is cost effective do so. Sequestration is an expensive procedure to follow as it involves a costly High court process and costly administrative procedure. Unlike all other formalities which are easy to comply with and prove, the advantage to creditors' requirement is difficult to prove and most debtors fail to satisfy this requirement as it has to do with proving liquidity.

Boraine *et al*¹⁶² refer to the insolvency Act as "antiquated" which in simple terms means old fashioned and outdated. One could not agree any less since the Insolvency Act is the main statutory instrument dealing with natural person debtors. Real change will have to start with the amendment of this crucial piece of legislation specifically the relaxation of the advantage requirement in sequestration proceedings.

The South African Commission in the Draft Insolvency Bill¹⁶³ has retained the advantage to creditors' requirement, meaning the same challenges of a daunting onus of proving advantage in sequestration proceedings will continue to confront over-indebted debtors. The advantage requirement is an obstacle to accessing the formal sequestration procedure and statutory discharge from debt. It also hinders law reform.

Finally, it can be seen from the above that the advantage to creditors' requirement is not only essential to sequestration order proceedings, but it changes the outlook and application of the Insolvency Act as a whole. From a debt relief perspective, the Insolvency Act would be the wrong instrument for over indebted debtors as it was clearly crafted to protect the interest of creditors.

¹⁶¹ Roestoff & Coetzee 2012 SA Merc LJ 59.

¹⁶² Boraine *et al* 2015 NIBLeJ 89.

¹⁶³ CI 7(1)(b) and 8(1)(c) of the Insolvency Bill 2015.



CHAPTER 4:

INTERNATIONAL TRENDS IN CONSUMER INSOLVENCY

SUMMARY

- 4.1 Introduction
 - 4.2 Australia
 - 4.3 United States of America
 - 4.4 Conclusion
-

4.1 Introduction

Insolvency is an ever-evolving practice and regulation of natural person insolvency is in the best interest of every economy and society.¹⁶⁴ The stringency of policy and regulation of insolvency often has socio economic effects.¹⁶⁵ This chapter will look at the trends in Australia and the United States of America where natural person insolvency is referred to as bankruptcy. Comparisons will be drawn with the South African system particularly with regards to access requirements for formal insolvency procedure in the selected jurisdictions.

4.2 Australia

The Australian bankruptcy regime entails a legal process enabling debtors with unmanageable debt to obtain a release from their obligations and start afresh after a period of three years.¹⁶⁶ Providing debtors with the chance to start afresh is popularly regarded as one of the key objectives of bankruptcy legislation.¹⁶⁷ Accordingly, there are

¹⁶⁴ World Bank *Principles for Effective Insolvency and Creditor Rights System (2001)*.

¹⁶⁵ Calitz "Some thoughts on state regulation of South African Insolvency Law" 2011 *De Jure* 310.

¹⁶⁶ Ali *et al* "The Incidence and causes of personal bankruptcy in Australia" 2016 *JASSA FJAF* 27.

¹⁶⁷ Howell "The fresh start goal of the Bankruptcy Act: Giving a temporary reprieve or facilitating debtor rehabilitation?" 2014 *QUT LR* 29.



a number of references in legal, policy and political documents that support the existence of a fresh start goal for the Australian Bankruptcy Act 1966.¹⁶⁸ In particular, debt discharge is an integral element of the Australian bankruptcy law idea of the fresh start.¹⁶⁹ More specifically, section 153 of the Bankruptcy Act provides that from the date of the conclusion of or discharge from their bankruptcy, the debtor is ‘discharged’ or released from their contractual obligations to pay the debts proved in the bankruptcy.¹⁷⁰

Under the Australian bankruptcy regime, a debtor can enter into voluntary bankruptcy which is also called a debtor’s petition.¹⁷¹ By lodging a debtor’s petition with the regulator, Australian Financial Security Authority (AFSA), a debtor can initiate his or her bankruptcy without seeking the consent of creditors or the approval of a court.¹⁷² The requirements for a debtor to file for bankruptcy are firstly, that the debtor must show that he is not able to pay his debts when they are due¹⁷³. Secondly, the debtor must be present in Australia or have a residential or business connection to Australia.¹⁷⁴ Once a debtor can satisfy these formalities, he becomes a candidate for bankruptcy proceedings.¹⁷⁵

Alternatively, when a creditor is unable to recover a debt of more than \$5000 or more, they can file a petition for the liquidation of a debtor.¹⁷⁶ The court may then appoint a trustee to manage the assets of the debtor and the court will grant an order for bankruptcy which is similar to a sequestration order.¹⁷⁷ However, before such order can be made, the court must be satisfied that the debtor has committed an ‘act of bankruptcy’ such as failing to pay a debt or travelling with an intention to evade creditors.¹⁷⁸

¹⁶⁸ Bankruptcy Act 1966 (CTH). See also Howell 2014 *QUT LR* 30.

¹⁶⁹ Howell 2014 *QUT LR* 35.

¹⁷⁰ S 153 of the Bankruptcy Act.

¹⁷¹ S 55 of the Bankruptcy Act.

¹⁷² O’Brien et al “More to lose: The Attributes of Involuntary bankruptcy” 2019 *EP* 16.

¹⁷³ The debtor must have committed an Act of Bankruptcy in terms of s 41 of the Bankruptcy Act.

¹⁷⁴ S 43(1)(i) of the Bankruptcy Act.

¹⁷⁵ S 43 of the Bankruptcy Act.

¹⁷⁶ Ss 43 and 44 of the Bankruptcy Act.

¹⁷⁷ S19 of the Bankruptcy Act.

¹⁷⁸ S 40 of the bankruptcy Act. See also O’Brien 2019 *EP* 16.



When compared with access requirements for sequestration in the South African context, The Australian system is debtor friendly. The formalities for accessing formal insolvency measures are less stringent. There is no requirement for advantage to creditors when applying for bankruptcy. In the South African context on the other hand the advantage to creditors' requirement poses the greatest challenge to debtors who desire to access formal insolvency procedures.¹⁷⁹

In the 2018 the Australian Bankruptcy Act saw a significant amendment which favours debtors when the Bankruptcy Amendment Bill¹⁸⁰ was passed into law. Part 23 thereof reads 'that an Official Receiver can refuse a debt agreement proposal for processing if the Official Receiver reasonably believes that complying with the debt agreement would cause undue hardship to the debtor.' The amendment goes to show the consideration that Australian lawmakers had towards debtors.

Bankruptcy in the Australian context last for a period of 3 years¹⁸¹ and discharges the debtor from all debts. The debtor becomes automatically rehabilitated a day after the expiry of the 3-year period,¹⁸² whereas in South Africa rehabilitation will only take effect after a period of 10 years.¹⁸³ The American legislative system overall does not require the advantage to creditors as is the case in South Africa.

4.3 United States of America

The American Bankruptcy Code¹⁸⁴ regulates natural person insolvency in the United States of America.¹⁸⁵ In *Local Loan Co v Hunt*,¹⁸⁶ the United States Supreme Court held that one of the primary purposes of the Bankruptcy Act was that "it gives to the honest but unfortunate debtor who surrenders for distribution the property which he owns at the

¹⁷⁹ See chapter 3, para 3.3.

¹⁸⁰ Bankruptcy Amendment Bill 2018.

¹⁸¹ S149 of the Bankruptcy Act.

¹⁸² S149 of the Bankruptcy Act.

¹⁸³ S127A of the Insolvency Act.

¹⁸⁴ Bankruptcy Reform Act of 1978.

¹⁸⁵ Bankruptcy Reform Act of 1978- Title 11, 11 and 13 of United States Code. Generally Known as the Bankruptcy Code or Code.

¹⁸⁶ 292 US 234, 244 (1934).



time of bankruptcy, a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debts.”

Chapter 7 of the Bankruptcy Code is entitled ‘liquidations’ and contemplates an orderly, court-supervised procedure.¹⁸⁷ Under Chapter 7 proceedings, a trustee is appointed by the court to collect non-exempt assets from the debtor and distributes them to the creditors.¹⁸⁸ For a debtor to qualify for chapter 7 he has to own property, run a business or reside in the United States of America as well as show an inability to pay off debts or pass a means test.¹⁸⁹ Filing for Bankruptcy under chapter 7 has the result that it discharges the debtor of all debts and gives the debtor a fresh start.¹⁹⁰

Alternatively, chapter 13 provides another method of applying for bankruptcy which consists of a payment plan between the debtor and the creditor.¹⁹¹ It usually applies to large debts such as mortgage bonds.

The requirements for chapter 13 applications are that the application must be made in good faith, the plan must also meet the “best interest” of creditors test and the debtor must satisfy the best efforts test which requires that unsecured creditors be paid a certain amount.¹⁹²

4.4 Conclusion

As seen from the above overview, the American Bankruptcy system is debtor friendly, especially when one looks at chapter 7. It is clear that the requirements for access to statutory debt relief are less stringent. As a result, more debtors file for bankruptcy and are discharged of their debts. They obtain a fresh start without much harm to their socio-

¹⁸⁷ Kanamugire “The Requirement of Advantage to creditors in South African Insolvency Law – A critical Appraisal” 2013 *MJSS* 31.

¹⁸⁸ S701-704 of the Bankruptcy Code.

¹⁸⁹ S109 of the Bankruptcy Code.

¹⁹⁰ S727 of the Bankruptcy Code.

¹⁹¹ S1325 of the Bankruptcy Code.

¹⁹² *Ibid.*



economic standing. In South Africa on the other hand, due to the advantage to creditors' requirement, most debtors are not able to access statutory relief.

The chapter also revealed that Chapter 13 of the US Code now incorporates a requirement for "best interest for creditors". Although worded as such, in practice the requirement is less stringent than the South African requirement for advantage to creditors. This is because a debtor in the United States does not have to show substantive evidence to be declared bankrupt filing a petition.

The research further indicated that the Australian system is debtor friendly and access to formal statutory Bankruptcy is easy for debtors. The system also provides a shorter period of 3 years before a debtor can be rehabilitated.

South African natural person insolvency could be greatly enhanced if lawmakers could repeal the advantage requirement for access to sequestration proceedings. A look at the Australian and the American reveal that these systems place value on assisting the debtor to obtain a fresh start than in enforcing payment of debts.



CHAPTER 5

CONCLUSION

SUMMARY

5.1 Introduction

5.2 Recommendations

5.1 Conclusion

The main objectives of this research were: to evaluate the natural person insolvency system as a whole, with particular attention to sequestration, debt review and administration; to specifically evaluate the advantage to creditors' requirement and whether it should be retained; to compare the advantage to creditors requirement in South Africa with international trends as regards access requirements in Europe and the United States of America; and to look at international guidelines specifically on access to formal sequestration or debt relief measures.¹⁹³

In this regard, the research discussed the sequestration as a process that provides for a procedure to sequester an insolvent debtor's estate.¹⁹⁴ In particular, the research revealed that in South Africa, the process of sequestration takes three forms namely: voluntary surrender,¹⁹⁵ compulsory sequestration¹⁹⁶ and friendly sequestration.¹⁹⁷ Under voluntary surrender, a debtor who wishes to surrender his estate may do so by publishing a notice of surrender in the government gazette and in the newspaper circulating in the

¹⁹³ Chapter 1, para 1.1.

¹⁹⁴ Chapter 1, para 1.1.

¹⁹⁵ Chapter 2, para 2.2.1.

¹⁹⁶ Chapter 2, para 2.2.2.

¹⁹⁷ Chapter 2, para 2.2.3.



district in which he resides, or in which his principle place of business is located.¹⁹⁸ However, the court can only surrender such estate where the debtor has proved that their liabilities exceed their assets, that they have sufficient assets in the free residue to defray the costs of the sequestration and that the sequestration will be to the advantage of the creditors.¹⁹⁹

Moreover, as observed from the above discussion, compulsory sequestration is another way in which a debtor's estate may be sequestrated.²⁰⁰ This process is initiated by creditors.²⁰¹ Then there is a friendly sequestration where a debtor's estate is sequestrated by an amicable creditor.²⁰² This process is not explicitly provided for by the Insolvency Act but it has been developed in practice. Central to the process of sequestration is the requirement for advantage to creditors which entails that the sequestration of a debtor's estate should be to the advantage of creditors. ²⁰³ As discussed above, the advantage to creditors requirement is a crucial determination in granting an order of sequestration by the courts.²⁰⁴

In *Ex Parte Ogunlaja*,²⁰⁵ the court stated that “unless and until the Insolvency Act is amended, the South African insolvency law requires that advantage to creditors be met before the estate of an individual can be sequestrated.” The court went further to stipulate that as much as the troubled economic times might have engendered sympathy for debtors whose financial burden became too much to bear, the aim of the insolvency law is to protect the interests of creditors to the extent that a minimum advantage is ensured for the concurrent creditor when the hand of the law is laid on the insolvent estate.²⁰⁶ This was the remark by Bertelsmann J, with regards to the advantage to creditors in the Insolvency Act.

¹⁹⁸ Chapter 2, para 2.2.1.

¹⁹⁹ *Ibid.*

²⁰⁰ Chapter 2, para 2.2.2.

²⁰¹ *Ibid.*

²⁰² Chapter 2, para 2.2.3.

²⁰³ See Chapter 3 for a comprehensive discussion of this requirement.

²⁰⁴ Chapter 1, para 1.1.

²⁰⁵ *Ex Parte Ogunlaja* [2011] JOL 27129.

²⁰⁶ *Ibid.*



According to Boraine,²⁰⁷ several insolvency authorities agree with the court's assertion and I also agree. The advantage to creditors' requirement plays a pivotal role in the exercise of the court's discretion in sequestration applications.²⁰⁸ It is on this basis that a court will, more often than not, decline to accept a voluntary surrender application or grant an order for the compulsory sequestration of an estate even though all the other requirements for the granting of a sequestration order have been satisfied.²⁰⁹

Based on the above assertion, it is clear that the courts' discretion as far as sequestration proceedings are concerned is guided by the Insolvency Act. Therefore, it is submitted that this is a double jeopardy for the debtor as he cannot easily obtain recourse from both the statute and the courts. Boraine *et al* further submit that as a result of the advantage to creditors' requirement in the Act, courts have a tendency of being extremely unsympathetic to debtors.²¹⁰

Apart from sequestration, the research revealed that there are alternative measures for insolvent debtors under the insolvency law and those are rehabilitation,²¹¹ administration,²¹² debt review²¹³ and the recently established debt intervention.²¹⁴ As discussed, rehabilitation allows the insolvent to make a fresh start, free from his pre sequestration debts.²¹⁵ According to the Insolvency Act, rehabilitation put an end to the sequestration process and relieves the insolvent of every disability resulting from sequestration as well as discharges all his debts, which were due or the cause of which arose before sequestration.²¹⁶

²⁰⁷ Boraine *et al* 2015 *NIBLeJ* 78.

²⁰⁸ *Ibid.*

²⁰⁹ *Ibid.*

²¹⁰ *Ibid.*

²¹¹ Chapter 2, para 2.2.4.

²¹² Chapter 2, para 2.4.

²¹³ Chapter 2, para 2.3.

²¹⁴ Chapter 2, para 2.6.

²¹⁵ Chapter 2, para 2.2.4.

²¹⁶ *Ibid.*



The research also discussed debt review as an alternative to sequestration.²¹⁷ As alluded, a debt relief process allows a consumer to apply to a debt counsellor to be declared over indebted.²¹⁸ However, as discussed, debt review offers temporary relief to over indebted debtor.²¹⁹ Furthermore, the research discussed administration order which basically involves a relatively simple and inexpensive procedure whereby the Magistrate's court reschedules overcommitted debtor's obligations.²²⁰ However, as seen from the discussion, the courts do not view the administration order procedure as a debt relief mechanism, but rather as a way for a debtor to obtain a temporary moratorium, which if the debtor fails to pay off the debt in full they may still be sequestered.²²¹

Last but not least, the research discussed the newly implemented debt intervention process which was introduced by the National Credit Amendment Act.²²² This process was introduced as a measure to assist identified consumers for whom existing natural person insolvency measures are not accessible in practice.²²³ It remains to be seen whether this newly implemented measure will indeed deliver on its objectives or not.

As stated in the objectives of this study, a comparative study of Australia was undertaken. The study revealed that the Australian system is debtor friendly and therefore, the formalities for accessing formal insolvency measures are less rigorous.²²⁴ This means that there is no burden placed on the debtor when applying for bankruptcy.²²⁵ Another comparative study was carried out on the United States of America, which study revealed that Chapter 13 of the US Bankruptcy Code now incorporates a requirement for "best interest for creditors".²²⁶ However, unlike in South Africa, a debtor in the United States does not have to show substantive evidence to be declared bankrupt.²²⁷

²¹⁷ Chapter 2, para 2.3.

²¹⁸ *Ibid.*

²¹⁹ *Ibid.*

²²⁰ Chapter 2, para 2.4.

²²¹ *Ibid.*

²²² Chapter 2, para 2.6.

²²³ *Ibid.*

²²⁴ Chapter 4, para 4.2.

²²⁵ *Ibid.*

²²⁶ Chapter 4, para 4.3.

²²⁷ *Ibid.*



As seen from the discussion, despite the alternative debt relief measures being available in the South African natural person insolvency framework, administration and debt review procedures do not provide any discharge from debt.²²⁸ It is only sequestration that provides a discharge through rehabilitation. However, proof of advantage to creditors is required.²²⁹ The advantage to creditors' requirement has survived several amendments to the Insolvency Act despite most academics suggesting that it should be repealed.²³⁰ The South African Law Reform Commission in its proposed Insolvency Bill,²³¹ has also retained the advantage to creditors requirement. That being said it would be safe to conclude that the Insolvency Act was not intended as a debt relief measure and debtors who require a discharge do not really have recourse in the Insolvency Act.

5.2 Recommendations

There is urgent need for insolvency law reform in South Africa, particularly in respect of the Insolvency Act. The Insolvency Act has become archaic and Boraine et al²³² refer to it as antiquated. When considered in light of the South African Constitution and the Bill of Rights, the Insolvency Act is outdated. This is largely because it was enacted before the advent of the Constitution.²³³

In this regard, it is submitted that a unified Insolvency Act could go a long way in the regulation of natural person insolvency. Currently there are several legislative instruments²³⁴ which seem to cause conflict with the interpretation and application of the Insolvency Act. It is submitted, therefore, that having a unified Insolvency Act would reduce the need for numerous amendments and supplementary legislation.

²²⁸ Boraine et al 2015 *NIBLeJ* 78.

²²⁹ *Ibid.*

²³⁰ Boraine et al 2015 *NIBLeJ* 88.

²³¹ Draft Insolvency Bill and explanatory memorandum by the South African Law Reform Commission, entitled *The review of the Law of Insolvency*; Draft Insolvency Bill and explanatory memorandum working paper 66, Project 63.

²³² Boraine et al 2015 *NIBLeJ* 89.

²³³ Boraine et al 2015 *NIBLeJ* 61.

²³⁴ Insurance Act 27 of 1943, The Long-term Insurance Act 52 of 1998.



It is also submitted that there is an urgent need for adoption of the proposed amendments into law to prevent prejudice of debtors. For instance, the proposed Draft Insolvency Bill by the South African Law Reform Commission was first mooted in 2000. However, nine years later it still has not been passed and some of the propositions contained therein are already in need of amendments because of the constantly changing consumer trends.

Lastly, I recommend that law makers consider international trends in insolvency. As much as South African Insolvency law has its foundations in the Anglo-American system, it is of uttermost importance that it remains abreast with the developments in those jurisdictions to avoid a situation where the law is out of touch with reality as most consumer trends are constantly evolving.



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