GETTING THE DEAL THROUGH

Restructuring and Insolvency

in 57 jurisdictions worldwide

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1 Legislation

What legislation is applicable to bankruptcies and reorganisations?

Insolvency in South Africa is primarily governed by the Insolvency Act 24 of 1936 (the Insolvency Act), which governs the sequestrations of the estates of individuals, trusts and partnerships that are insolvent. The winding-up and reorganisation of companies is governed by the Companies Act 61 of 1973 (the Companies Act), which incorporates by reference portions of the Insolvency Act in dealing with companies tthat cannot pay their debts. Close corporations are in turn governed by the Close Corporations Act 68 of 1984 which incorporates by reference the provisions of the Companies Act and, accordingly, the Insolvency Act. A close corporation is a simple form of juristic person akin to a partnership with limited liability, with members taking the role of both shareholders and directors. In a liquidation of a company or close corporation, a liquidator is appointed, while in a sequestration of an individual or trust or partnership, a trustee is appointed.

The Magistrate's Court Act 32 of 1944 contains provisions pertaining to a moratorium granted to individuals who cannot pay their debts, although it does not involve a sequestration of their estate. Since June 2007, new consumer protection legislation aimed at curbing reckless credit patterns and controlling money lenders came substantially into effect (the National Credit Act 34 of 2005). Under this legislation (which supplements but does not replace the existing moratorium rights under the Magistrate's Court Act), individuals and small businesses with an asset value or annual turnover less than 1 million rand, which are trapped by excessive debt, can approach a registered 'debt counsellor', who reviews the debt and, if satisfied, proposes a repayment plan to impose on creditors. The debtor then applies to the Magistrate's Court to have the plan made an order of court, which is then binding on creditors. The court can also make an order setting aside any credit agreement if the money lender granted the credit recklessly.

Reorganisations of companies are dealt with under section 311 of the Companies Act. Judicial management of companies is dealt with in terms of sections 427 to 440 of the Companies Act.

Although the liquidation or winding-up of insurance companies, banks and pension funds is governed primarily by the Insolvency Act and the Companies Act, specific legislation pertains to those entities such as the Banks Act 94 of 1990, the Long-term Insurance Act 52 of 1998, the Short-term Insurance Act 53 of 1998 and the Pension Funds Act 24 of 1956, which contain specific provisions pertaining to the administration of that liquidation or winding-up.

2 Excluded entities

What entities are excluded from bankruptcy proceedings and what legislation applies to them?

Certain entities such as banks, pension or provident funds, long-term and short-term insurers, or companies in which the government has the sole shareholding, are subject to specific rules and to the supervision of the body regulating the industry.

3 Secured lending and credit (immoveables)

What are the principal types of security devices that are taken on immoveable (real) property?

The principal type of security that may be taken over immoveable property is a mortgage bond. A mortgage bond is registered over the debtor's immoveable property in favour of the creditor in the Deeds Office (which, for each province, contains a register of all ownership of immoveable property as well as certain security over moveable property; see question 4). Ownership in the immoveable property remains vested in the debtor, but the creditor acquires the right, on default by the debtor, to attach and sell in execution the immoveable property and apply the proceeds thereof in discharge of the outstanding indebtedness. During the existence of the mortgage bond, the debtor cannot transfer the property without the consent of the mortgage creditor. Immoveable property can be owned outright or by way of sectional title (in the case of townhouses and apartments). Mortgage bonds can thus be ordinary mortgage bonds or sectional mortgage bonds. Certain long-term leases for 10 years or more may be registered in the Deeds Office. Mortgage bonds can be taken over such leases, although this is effectively a mortgage over a right of occupancy rather than over the immoveable property itself.

4 Secured lending and credit (moveables)

What are the principal types of security devices that are taken on moveable (personal) property?

The principal types of security over moveable property are: notarial bonds, cessions, pledges and liens. A creditor may have a further form of security by means of a reservation of title or ownership.

A notarial bond may be registered in the Deeds Office by a creditor over a debtor's corporeal or incorporeal moveable property. While ownership and possession in the moveables remains vested in the debtor, the creditor has the right, on default by the debtor, to apply to court to take possession of the moveables and to sell them and discharge the indebtedness with the proceeds. There is no register of cessions. By contract, however, the debtor may cede, for example, his or her book debts (receivables) to a creditor as security for a loan or other obligation. Cessions of book debts usually convey a right to the creditor, if there is a default by the debtor, to advise the debtors so ceded of the existence of the cession and to require them to pay the creditor the amount of the debt (receivable) direct to the creditor. A pledge need not be registered in the Deeds Office and is created by the creditor taking possession of corporeal and incorporeal moveables. The debtor retains ownership but the creditor has the right to possess the moveables until the debt has been paid in full. On default

by the debtor, the creditor has the right to sell the moveables and discharge the indebtedness with the proceeds. Liens arise by operation of law out of certain contractual relationships and are not required to be registered. A builder, for example, has a lien over a building for payment of the work done. The debtor retains ownership while the creditor has the right to possess the moveables until the debt has been paid in full. On default by the debtor, the creditor has the right to sell the moveables and discharge the indebtedness with the proceeds.

Landlords also enjoy a common law lien (termed a hypothec) over the possessions of a tenant as security for arrear rental. In insolvency, the security under the hypothec is limited to three months' arrear rental.

There is also provision in statutes to pass mortgage bonds over ships and aeroplanes.

A supplier of goods may protect him or herself by inserting a clause in the supply agreement to the effect that ownership or title in the goods so supplied will not pass to the purchaser until the supplier has been paid in full.

5 Unsecured credit

What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

An unsecured creditor must issue summons against the debtor claiming payment of the amount outstanding. If the debtor does not defend the action, judgment can be granted by default without the need to lead evidence, usually within three to six weeks depending on where the defendant conducts business. If the debtor defends the action, the matter can take up to 15 months to finalise. If the defence is without substance, the creditor can apply for summary judgment or provisional sentence, in certain circumstances, which can take up to three to four months to obtain if opposed. Only once judgment has been obtained can the creditor seek to enforce the judgment. This can be done by directing the sheriff of the court to attach and sell the debtor's assets or to attach a credit balance in a debtor's bank account, or to attach ('garnishee') a debt or income owing to the debtor. Debtors can apply for rescission of or appeal against a judgment, which slows down the execution process.

In special circumstances, if a creditor who is awaiting judgment can demonstrate that the debtor is dissipating assets to frustrate the claim, the creditor can apply to court for an order that assets to the value of the amount claimed can be attached or frozen pending judgment.

There are no special rules for foreign creditors, except that if a claim is disputed, the debtor may obtain a court order requiring the foreign creditor to provide security for the debtor's legal costs by way of a payment into court (which is repaid to the creditor if it is successful, or used to cover the debtor's costs if he or she is not).

6 Courts

What courts are involved in the bankruptcy process? Are there restrictions on the matters that the courts may deal with?

Only the High Court has the power to wind up companies and sequestrate the estates of individuals, trusts and partnerships. Although close corporations may be wound up in the High Court, they may also be wound up in the magistrates' court. All insolvent estates, be they of companies, close corporations or individuals, trusts or partnerships, are administered under the control of the master of the High Court. Enquiries or interrogations by trustees or liquidators are convened either in the magistrates' court or under the auspices of a commissioner appointed by the master.

7 Voluntary liquidations

What are the requirements for a debtor to commence a voluntary liquidation of its business? What are the effects of the commencement of the liquidation?

An individual may voluntarily surrender his or her own estate by way of a voluntary petition to the High Court and demonstrate that his or her liabilities exceed his or her assets, after having given notice of any intention to do so to his or her creditors, employees and the South African Revenue Services (SARS), and after having provided a detailed statement of his or her assets and liabilities, to lie for inspection at the local magistrates' court or master's office. A company may voluntarily seek to wind itself up by way of an application to court or by way of a resolution of its shareholders. The winding-up may take the form of the following.

Members' voluntary winding-up

The shareholders of a company must pass a special resolution (75 per cent majority) to wind up the company in circumstances where a company has no debt. The directors must sign an affidavit and the auditor must also sign a certificate, to this effect; otherwise the company must put up security for the debts of the company to be incurred in the year from the date of liquidation. A liquidator is appointed, who winds up the company according to the directives of the shareholders.

Creditors' voluntary winding-up

Despite the misleading name, the shareholders of a company must pass a special resolution (75 per cent majority) to wind up the company, in circumstances where the company has unpaid debt. No notice of the meeting for the passing of the resolution is given to creditors, but the employees are advised of the fact that the company is likely to be wound up. There is no need to put up security for the debts of the company because the appointed liquidator winds up the company according to the directives of creditors, not of the shareholders. In the case of a close corporation, no distinction between types of resolution is made and the members must unanimously pass a resolution agreeing to wind up the close corporation, whether insolvent or not.

The application to court can be made by the company in terms of a resolution of directors or by a shareholder; and, in the case of a close corporation, by a member or by a resolution of members.

The effective date of liquidation is:

- in the case of an application to court, the day the application papers are issued at court by the Registrar of the Court; and
- in the case of a voluntary shareholders' resolution, the day the special resolution is registered at the office of the Registrar of Companies.

Once the liquidation has commenced, whether by way of resolution or application to court, and whether the resolution is a members' voluntary winding-up or a creditors' voluntary winding-up, all pending legal proceedings are suspended until the appointment of a trustee (individuals) or a liquidator (corporate entities). The company or individual's estate is effectively frozen and no creditors may seek to obtain further preference.

8 Involuntary liquidations

What are the requirements for creditors to place a debtor in involuntary liquidation? What are the effects of the commencement of the liquidation?

Section 344 of the Companies Act provides that a company may be compulsorily wound up by court at the application of a creditor

on various grounds, not necessarily related to the company's insolvency, such as when the company has suspended its business for a whole year. Most commonly, however, creditors will seek to wind up a company involuntarily on the basis that the company cannot pay its debts. A company is deemed to be unable to pay its debts if any court official charged to satisfy a judgment cannot find sufficient disposal property to satisfy the judgment, or a creditor, to whom the company is indebted in a sum of not less than 100 rand, has served a letter on the registered office of the company demanding payment of the debt and the company has not paid the debt within a period of three weeks or disputed the debt within that period on bona fide, reasonable and substantial grounds. There are similar provisions relating to close corporations. With effect from the date of issuing of the papers with the registrar of the High Court, the company is in liquidation. All legal proceedings against the company are suspended until the appointment of a liquidator. Any civil attachment of assets of the company after the commencement of the winding-up is void. All assets of the company vest in the master and, ultimately, in the liquidator.

9 Voluntary reorganisations

What are the requirements for a debtor to commence a financial reorganisation? What are the effects of the commencement of the reorganisation?

A debtor company may seek to implement an informal reorganisation by approaching creditors to comprise their debts or grant a moratorium or both. The terms and effect of such a reorganisation will depend on the terms negotiated with the creditors, and, to achieve the desired result, all creditors have to agree. A formal reorganisation may be achieved in one or two ways: the company may apply for judicial management in terms of sections 427 to 440 of the Companies Act, or it may apply for a scheme of compromise in terms of section 311 of the Companies Act (a 311 scheme), with or without going into liquidation. There is no provision for the judicial management of close corporations and only a more limited form of compromise is possible. When a company is mismanaged and is unable to pay its debts because it is illiquid, a court may grant an order placing the company under judicial management on application by the company itself, a creditor or a shareholder. Effectively, the consequences of the imposition of a judicial management order are that the control of the company's affairs by its directors is replaced by that of the judicial manager and the company is granted a moratorium in which creditors cannot institute action against the company. The judicial manager has the sole discretion to use what money is available to pay the ongoing costs of the business operation and, if possible, any pre-judicial management claims. The judicial manager is required to operate the business and accordingly cannot sell off the assets of the business, save in the ordinary course of business, without the leave of court. A judicial manager is obliged to examine the affairs of a company to see that he or she is satisfied that the company is solvent and can, with the passage of time, pay its creditors in full. If the judicial manager cannot satisfy him or herself in this respect, he or she must apply for the liquidation of the company.

A 311 scheme is an arrangement between the company and its members or the company and its creditors. Typically, a 311 scheme between the company and its creditors involves creditors being requested to accept a reduced compromise of their claims on the basis that the dividend that they will receive in respect of their claims is greater than what they would receive on liquidation. Often such schemes entail a third party, the proposer, acquiring the compromised claims of creditors, as well as the shares in the company. Section 311 of the Companies Act empowers the company to enforce the scheme on all creditors, even those who do not agree with it, if the requisite majority of votes of 75 per cent in value and 75 per cent in number at a meeting of each class of creditors present at the meetings are obtained. The meetings are chaired by an independent party, the receiver, who administers the scheme. Typically, the classes of creditors will be creditors who are preferent, secured and concurrent. Once the requisite majorities are obtained, the scheme must still be sanctioned and approved by the court. If the company is in liquidation at the time the 311 scheme is proposed, the scheme can provide that once the creditors all accept or are deemed to accept a compromise of their claims, the company is brought out of liquidation. Provided the creditors get paid in terms of the compromise, they cannot take action against the company.

10 Involuntary reorganisations

What are the requirements for creditors to commence an involuntary reorganisation? What are the effects of the commencement of the reorganisation?

In our view, a creditor may not apply for a section 311 scheme. A creditor may propose a 311 scheme, but the company itself or its liquidator will have to bring the formal proceedings. A creditor may apply for judicial management.

In a 311 scheme, the company (if in liquidation) may be brought out of liquidation and may continue trading as normal, with all debts either reduced or expunged by payment from the proposer. In the case of a judicial management, no creditors may commence action against the company while it is under judicial management, and will receive payment as and when the judicial manager sees fit. Creditors may, however, intervene in the application for judicial management and apply for liquidation of the company.

11 Mandatory commencement of insolvency proceedings

Are companies required to commence insolvency proceedings in particular circumstances (to avoid personal liability to directors and officers or otherwise)? In what circumstances must companies do so? If proceedings are not commenced, what liabilities can result?

Unlike some jurisdictions in Europe, there is no obligation placed on directors or shareholders of a company or close corporation to commence insolvency proceedings. Indirect pressure is, however, placed upon directors or members of insolvent companies or close corporations to either take steps to wind up the company or to resign as directors by means of section 424 of the Companies Act or section 64 of the Close Corporations Act. As detailed in question 25, any person who is knowingly a party to the carrying on of the company's business in a reckless or fraudulent manner may be declared liable by the court for all or some of the debts or liabilities of the company. Thus, directors and corporate officers of a company which is trading in insolvent circumstances, who fail to resign as such or commence steps to place the company into liquidation, may run the risk of being held personally liable for some or all of the company's debts.

12 Doing business in reorganisations

Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use of assets and to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities?

311 scheme

If a company is not in liquidation, no insolvency considerations apply and the business carries on in the ordinary course subject to commercial terms both during and before the implementation of the 311 scheme. If a company is in liquidation and the liquidator obtains leave of the court to continue the business of the company, then all

debts and obligations incurred by the liquidator must be paid and fulfilled as an administrative expense, before the pre-liquidation claims of unsecured creditors.

Judicial management

The judicial manager is empowered to run the business in its ordinary course but may not sell assets other than in the ordinary course of business. He or she is obliged to pay creditors who supply goods and services after the judicial management order on the usual terms and conditions, out of funds that he or she has available. The judicial manager carries on the business of the company at his or her sole discretion but with due regard to the interests of creditors. He or she does not, however, act according to the directives of creditors. Creditors are entitled to receive reports setting out the status of the company and to regularly attend meetings so as to be appraised of the state of the company. The judicial manager is effectively an officer of the court. The court tends not to play an active role in supervising the company's business activities unless the judicial manager applies to court for directives on certain issues. Creditors are not obliged to continue to supply the judicial manager, save where the company has enforceable supply contracts with them.

13 Rejection and disclaimer of contracts in reorganisations

Can a debtor in a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party?

In informal compromises, the compromise is only binding on those creditors who agree to the compromise, so the other party to an unfavourable contract is unlikely to consent to the rejection.

In formal compromises (311 schemes), the scheme can only propose a compromise of claims, not a rejection or disclaimer of contracts viewed as unfavourable.

In judicial management, the judicial manager has the power to investigate and if necessary set aside or void contracts or transactions entered into by the company before the judicial management order was granted. The transactions that may be voided are the so-called impeachable transactions – see questions 31 and 32.

14 Sale of assets

In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets?

Reorganisation

The terms of a 311 scheme will determine the sale of specific assets or the business as a whole. Typically, a 311 scheme will provide that the proposer will sell all or certain assets of the company and apply the proceeds towards the claims of creditors. Since all creditors are bound by the scheme, the assets are sold 'free and clear'.

In a judicial management, the judicial manager must continue the business of the company but may not sell off its assets other than in the ordinary course of business without the leave of court. Clearly the entire business of the debtor cannot be sold without the court's approval. All creditors' claims are bound by the judicial management so assets are again sold 'free and clear'.

Liquidation

A provisional liquidator is appointed by the master of the High Court and has a duty to secure and preserve the business and he or she may have been given the power, or later apply to court for the power, to continue the business with a view to preserving it for ultimate sale. A final liquidator is appointed by the creditors at the first meeting of creditors. A final liquidator sells the assets according to the directions of creditors. It may, for example, result in a higher price for the liquidator to sell the business as a going concern rather than sell off the assets piecemeal. The insolvency legislation specifically provides that no liabilities can be transferred out of the liquidation (as that would prefer those creditors) so the assets are sold 'free and clear'.

15 Stays of proceedings and moratoria

What prohibitions against the continuation of legal proceedings or the enforcement of claims by secured and unsecured creditors are imposed by legislation or court order in liquidations and reorganisations? In what circumstances may secured or unsecured creditors obtain relief from such prohibitions?

Liquidation

All legal proceedings against a liquidated company are suspended from the date of liquidation (either the date of issue of the court application or the date of registration of the special resolution) until the date of appointment of a liquidator. Most creditors prove claims against the estate. They can proceed with litigation once the liquidator has been appointed or apply for leave of the court to institute proceedings. No assets of the company may be attached or executed upon in terms of that judgment. Any judgment will then become a claim in the estate.

Reorganisation

Once a 311 scheme has been sanctioned by court, the company operates as usual. Thus, any creditor not bound by the scheme may institute proceedings and may attach assets. The moratorium (in relation to creditors who are bound by the scheme) only dates from the time the scheme is sanctioned, not from when leave is sought to convene the meetings of creditors prior to sanction. In the case of judicial management, no creditors may institute action against the company while the judicial management order is in place. If creditors wish to pursue legal proceedings or attach assets, they would be obliged to seek the leave of court, although relief is unlikely to be granted.

16 Arbitration processes in bankruptcy

How frequently are arbitration procedures used in insolvency proceedings? What limitations are there on the availability of arbitration procedures in insolvency cases? In insolvency proceedings, will the court allow arbitration proceedings to continue after an insolvency case is opened?

In terms of the South African Arbitration Act 42 of 1965, if the estate of any party to an arbitration is sequestrated, wound up or placed under judicial management, any insolvency law applies in the same manner as if a reference of a dispute to arbitration under an arbitration agreement were an action or proceeding or a civil proceeding or a legal proceeding under such insolvency law. Accordingly, the position as set out in question 15 applies equally to arbitration proceedings. The Arbitration Act specifically provides that, unless an arbitration agreement provides otherwise, an arbitration agreement or the appointment of an arbitrator is not terminated by the insolvency of a party.

A liquidator may refer a dispute to arbitration, provided that the prior written authorisation of the creditors or the master is obtained. If the other party believes that the liquidator would not be able to pay the costs of the other party if he or she is successful, the other party may apply to court, which may require the liquidator to provide security for costs and stay the arbitration until security is given.

Specifically, if arbitration proceedings are commenced against

a party before the party or company was declared insolvent, these proceedings are stayed until a final trustee or liquidator is appointed. Thereafter, the proceedings may be continued, provided that the party who instituted the arbitration proceedings gives notice of his or her intention to proceed with the proceedings within three weeks of the first meeting of creditors (failing which the arbitration lapses).

17 Set-off and netting

To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

Liquidation

Section 46 of the Insolvency Act provides effectively that, where the insolvent debtor company and a creditor have liquidated claims against each other, and the company is liquidated within a period of six months after the taking place of set-off, the liquidator may either elect to abide by the set-off or, with the approval of the master, disregard it if he or she can show that the set-off was not effected in the ordinary course of business. Thus, set-off can operate, but may be set aside on certain grounds. Set-off is specially preserved in master contracts relating to interest, swaps and derivatives. Post-liquidation set-off is not permitted.

Reorganisation

Set-off continues to operate in judicial managements. The terms of a 311 scheme will determine if set-off operates in that context.

18 Intellectual property assets in insolvencies

May the licensor or owner of the IP terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with an IP licensor or owner to continue to use the IP for the benefit of the estate?

It is accepted that intellectual property rights are 'property' in a liquidation and these rights may be sold off by the liquidator either separately or as part of a sale of the business as a going concern.

Where an insolvent estate does not own intellectual property but merely has the right to use intellectual property in terms of a licence arrangement, the liquidator generally has a choice as to whether to cancel or abide by the licence arrangement. Executory contracts are contracts that have not terminated at the date of liquidation or reciprocal contracts with ongoing obligations. Under common law, certain contracts automatically terminate on the liquidation of one of the parties but, generally, with executory contracts, the contract continues, subject to the liquidator's choice whether to cancel or abide by the contract. If the liquidator cancels the contract, the other party to the contract has a concurrent claim for damages. If the liquidator elects to abide by the contract, the liquidator must ensure that all obligations of the insolvent estate are performed in full.

Accordingly, if an insolvent estate has intellectual property rights under a licence agreement, these are not automatically terminated by the liquidation and the liquidator must decide whether to cancel the licence agreement or abide by it. If the liquidator cancels the licence agreement, the insolvent estate must cease using the intellectual property rights. If the liquidator elects to continue using the intellectual property, the liquidator must pay all necessary licence fees and perform in full in terms of the licence agreement.

A common feature of executory contracts is a provision entitling one party to cancel the agreement on the other party's insolvency. Whether these clauses are valid in South African law has not yet been settled but our view is that these clauses are not valid for various reasons. Accordingly, if a licence agreement contains a provision entitling the licensor to cancel the licence agreement on the licensee's insolvency, our view is that the licensor would not per se be entitled to cancel the licence agreement if the licensee were placed into liquidation and that the election as to whether to cancel or abide by the contract remains with the liquidator.

19 Post-filing credit

Does your country's insolvency system allow a debtor in a liquidation or reorganisation to obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

Liquidation

Liquidators of companies in liquidation may obtain the permission of court to incur credit for the purpose of continuing the company's business while trying to find a buyer for the business. These loans or credit must be paid by the liquidator as a cost of administration, which is a first charge against the unsecured assets of the company.

Reorganisation

If the company to which a section 311 scheme is applicable is in liquidation, then the above rules will apply until the scheme is implemented. If the company is not in liquidation or judicial management, then it is subject to the ordinary requirements and repayment terms of commercial banking. If there is a judicial management order in place, the judicial manager can, depending on the wording of the judicial management order, obtain credit facilities without the need to obtain a further order of court.

20 Successful reorganisations

What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan create releases in favour of third parties, and, if so, in what circumstances?

In a 311 scheme, the scheme must be an arrangement between the company and its creditors or shareholders. Even if the scheme entails a third party proposer buying the claims of creditors, the consent by the company to the cession of its claims to the proposer is regarded as sufficient for the purpose of constituting a 311 scheme. Creditors are usually classified into their various classes, being preferent creditors, secured creditors and concurrent creditors. A meeting is held with each class of creditors and the scheme put to such creditors. A majority, calculated in number and in value, of 75 per cent of the creditors in each class attending the meeting must be obtained before the scheme can be approved. Even if the creditors approve the scheme, the scheme must still be sanctioned by the court to become binding. In a judicial management, the company itself or a creditor of the company may apply to the court for judicial management. In theory, a 311 scheme can propose the release of third parties, but it is unlikely to be approved by creditors.

The granting of a judicial management order lies within the court's discretion and the court will decide whether or not it is warranted. Any creditors who have strong feelings about the order may intervene and file affidavits. The court, in exercising its discretion, must be satisfied that the judicial management will be in the interests of all shareholders and creditors. It must be established that, as a result of mismanagement or for any other cause, the company is unable to pay its debts or is probably unable to meet its obligations and has not become, or is prevented from becoming, a successful concern and there is a reasonable probability that, if judicial management ensues, that it would be able to pay its debts, meet its obligations and become a successful concern. Creditors are again classified into their various classes: preferent, secured and concurrent. The judicial

manager is usually empowered to compromise claims of the company against third parties but he would have to exercise this discretion prudently with regard to the merits of the claim against the likely costs and recovery.

21 Expedited reorganisations

Do procedures exist for expedited reorganisations?

Procedures do not exist for expedited reorganisations. If reorganisations are implemented informally with the consent of all creditors, then the terms and conditions and any time periods are negotiated by agreement.

22 Unsuccessful reorganisations

How is a proposed reorganisation defeated and what is the effect of the plan not being approved? What happens if there is default by the debtor in performing an approved plan?

A section 311 scheme can be defeated by not obtaining the requisite majorities of 75 per cent of each class of the creditors according to number and value, or, even if the requisite majorities agree, if the court refuses to sanction it, for example if the terms are too onerous or contrary to public policy. If the scheme is not approved, the company remains in the same condition it was in prior to the scheme being proposed. The implications of default will depend on the terms of the scheme. In many schemes, the proposer assumes the liability for the payment of creditors' claims as prescribed by the scheme. If the proposer defaults on making payments, the creditors can sue the proposer and, if the proposer has put up security, exercise their rights against it. Alternatively, the creditors may apply to court for an order setting aside the scheme of arrangement and reinstating the status quo. If the 311 scheme requires the debtor company to pay in terms of an approved claim and the debtor company fails, then the receiver appointed to administer the 311 scheme can either apply to court to have the scheme set aside or to have the debtor company placed into liquidation. In a judicial management, where a judicial manager realises that there is no prospect of the company returning to being a successful concern, then he or she must make application to court to place the company into liquidation. A creditor who has not been paid in terms of a judicial management scheme may apply to court either to have the debtor company placed into liquidation or to have the judicial management order set aside, thereby restoring the status quo.

23 Bankruptcy processes

During a bankruptcy case, what notices are given to creditors? What meetings are held? What committees are or can be formed? What powers or responsibilities do these committees have? May creditors initiate proceedings to pursue remedies against third parties?

Where a liquidation takes place by way of a shareholders' resolution (either a members' voluntary winding-up or a creditors' voluntary winding-up), no notice, either of the meeting or of the fact that the order is granted, is given to creditors. If the winding-up at the instance of the shareholders is a creditors' voluntary winding-up, notice must be given to the employees. Once the special resolution for winding-up is registered, notice of this fact must then be given to the employees and to SARS. In a compulsory application to court, the papers are served on the debtor company, as well as on SARS and the employees. There is no requirement under South African law that notice is given to the creditors but, as a matter of practice, various jurisdictions have developed rules as to when it would be appropriate to give notice to creditors. Once a provisional order or liquidation is granted by the court, the provisional order is again served on the debtor company, its employees and SARS, and notification is given to creditors of the granting of the provisional order by way of an advertisement in two local newspapers and in the Government Gazette. The same process is adopted when a final order is granted.

Once a provisional liquidator is appointed, he or she sends a notice by post to all known creditors advising of the liquidation. By law, two general meetings of creditors are required to be held, together with various ad hoc meetings, when required. Creditors' committees are generally not formed in the South African jurisdiction. It does happen that certain groups of trade creditors with common interests join together and speak with one voice, but no formal committees are recognised in law. In fact, the Insolvency Act provides that if a particular creditor were to take cession of other creditors' claims in the hope of building up a 'block' of claims for the purpose of manipulating voting, such claims, acquired by cession after the winding-up order, do not carry any votes. Creditors may institute proceedings against third parties such as sureties and against reckless or fraudulent directors of the company, without recourse to, or obtaining the permission of, the liquidator.

24 Insolvency of corporate groups

In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be combined into one pool for distribution purposes?

In a voluntary winding-up or reorganisation of companies within a corporate group, the liabilities of subsidiaries may be settled by its parent company and the assets distributed to the parent company which facilitates the voluntary winding-up or reorganisation. In this instance, the group is in control of the winding-up or reorganisation. The assets and liabilities of the group are not combined into one pool as each company is a separate legal entity, with its own creditors and shareholders. In a compulsory winding-up of companies within a group, different liquidators may be appointed in respect of each company and the assets and liabilities of each company are dealt with in turn. There is provision, in voluntary winding-ups, for a liquidator to sell a business to another group company and to receive shares in the recipient as consideration, for distribution to the shareholders of the company in liquidation. This does not mean that the assets and liabilities of both group companies are pooled.

25 Modifying creditors' rights

May the court change the rank (priority) of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

In terms of the Insolvency Act, if, after a debtor's estate is liquidated, that debtor colludes with another person to dispose of assets belonging to the debtor in a manner which has the effect of prejudicing his creditors or preferring one of his creditors above another, a court may, on application by the liquidator or a creditor, set this transaction aside and order that any person who was a party to the collusive transaction forfeits his claim in the estate, as well as being liable to making good any loss caused to the estate and paying a penalty. The court does not have any additional powers to change the ranking of a claim. The master can refuse to recognise claims, or to refuse to recognise a secured claim (if the security instrument is invalid) and admit the claim only as unsecured. The master's decision can be taken on review to the court.

26 Enforcement of estate's rights

If the insolvency administrator is without assets to pursue a claim that is available to the estate, are there procedures by which the creditors can pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

The Insolvency Act provides that, if a liquidator has a right of action to recover property in respect of the insolvent estate or to set aside dispositions or preferences and chooses not to do so (for example, if the insolvent estate is without assets to pursue such a claim), any creditor may take these proceedings in the name of the liquidator, provided the creditor bears the costs of these proceedings and indemnifies the liquidator against any costs. Any amounts recovered by such creditor are first applied to settling that creditor's claim and, to the extent that there is a surplus, the surplus would be applied towards settling the claims of other creditors. Alternatively, the creditors can vote to contribute towards the costs.

27 Claims and appeals

How is a creditor's claim submitted and what are the applicable time limits? How are claims disallowed and how does a creditor appeal a disallowance? Are there any provisions that deal with the purchase, sale or transfer of claims against the debtor?

Creditors' claims are submitted by way of an affidavit duly supported with copies of the relevant contracts and documents. All claims must be submitted at the first and second creditors' meetings. If a claim is not submitted at the second meeting of creditors, it may be submitted at an extraordinary meeting to be called for that purpose within three months after the second meeting. Thereafter, if claims are to be admitted, the consent of the master must be obtained. On submission of the claims, the liquidator investigates them with the assistance of the directors of the company. If the liquidator believes that the claim is inflated or unenforceable, he or she submits a report to the master, on notice to the creditor concerned, and requests that the claim be expunged. The creditor has an opportunity to substantiate or amend his or her claim before the master makes a decision. If the master disallows the claim, the creditor may take his or her decision on review to the High Court in limited circumstances. South African law does recognise the right of a creditor to cede his or her claim; however, any claims acquired by cession after the date of liquidation do not carry votes, a provision designed to avoid creditors controlling liquidations by building up 'blocks' of votes.

28 Priority claims

What are the major governmental and non-governmental privileged and priority claims in liquidations and reorganisations? Which priority and privileged claims have priority over secured creditors?

These privileged and priority claims, termed 'preferent' claims in South African law, constitute, in order of rank, charges against the non-secured assets of the insolvent estate, followed by the concurrent creditors. In order of rank:

- the costs of liquidation, being the costs of the court application, the liquidator's and master's costs; and the sheriff's costs;
- the arrear remuneration, leave pay, retrenchment and other employee claims (it should be noted that the claims have a limited preference of between 4,000 and 12,000 rand (US$600 to US$1,800), the balance of the claim being concurrent);
- various arrear levies and duties owed by the insolvent to government, including arrear income tax and value added tax, all of which rank in equal portions;
- the balance to any claims filed by a creditor who had the security of a general notarial bond.

None of these preferent or priority claims has priority over secured creditors in respect of the proceeds of the secured assets, except for local authorities (municipalities), which are entitled to be paid for rates and property taxes in arrears for up to two years preceding the date of liquidation out of the proceeds of the immoveable property in preference to, and even to the exclusion of, the mortgage bondholder (a similar preference over the mortgage bondholder is given to a body corporate of a sectional title property scheme for arrear levies). In general, however, when the secured creditor claims either the secured asset or the proceeds thereof, the secured creditor will be obliged to pay the liquidator's costs of preserving and selling the asset as well as his or her fee, the so-called 'section 89' costs, which, in practice, amount to approximately 12 per cent of the value of the secured assets or the proceeds thereof.

29 Liabilities that survive insolvency proceedings

Do any liabilities of a debtor survive insolvency so that they are enforceable against the debtor after it has reorganised?

Generally, no liabilities of a debtor survive insolvency so that they are enforceable against the debtor after it has reorganised or against a purchaser of the debtor's assets in an insolvency. Once a debtor has been liquidated, the creditors receive a dividend in full settlement of their claim and the creditors have no further recourse to the debtor. If the debtor submits a written offer of composition in respect of his, her or its estate and this offer is accepted, any creditor who failed to prove a claim before the liquidator made a final distribution in respect of the composition is entitled to recover directly from the insolvent within six months of the confirmation by the master. If the composition is achieved in terms of a section 311 compromise, then there is no recourse to the debtor, unless there is a breach of the terms of the section 311 compromise.

Assets purchased from a liquidator cannot be attached by the insolvent's creditors. The Insolvency Act specifically prohibits a liquidator from delegating liabilities out of the liquidation.

30 Distributions

How and when are distributions made to creditors in liquidations and reorganisations?

In liquidations, distributions are made in terms of a liquidation and distribution account, which is published for objection by creditors before being implemented. A liquidation and distribution account should be prepared within six months of liquidation and thereafter whenever sufficient funds are available. In section 311 schemes, distributions are made to creditors by the receiver either at his or her discretion, or in terms of the agreed distributions (if such distributions are specified in the scheme).

In a judicial management, distributions are made by the judicial manager when and how he or she sees fit, at his or her discretion.

31 Transactions that may be annulled

What types of transactions can be annulled or set aside in bankruptcies and what are the grounds? What is the result of a transaction being annulled?

The liquidator is entitled to recover from any third party any assets of the company which were disposed of prior to liquidation to third parties, including the shareholders and directors, in circumstances which constitute impeachable transactions as contemplated by sections 26, 29, 30 and 31 of the Insolvency Act. Thus, if a company disposes of any assets, at a time when its liabilities exceed its assets, at less than market value or in a manner that prefers or prejudices creditors, the liquidator can recover the assets from the third party. Any transac-

tion entered by the debtor company before liquidation whereby it, in collusion with another, disposed of property belonging to it in a manner which has the effect of prejudicing creditors or preferring one above the other is a collusive dealing and may be set aside. Section 88 of the Insolvency Act provides that where a special notarial bond or a mortgage bond is passed over assets to secure a previously unsecured debt, which was unsecured for at least two months before the registration of the notarial bond or mortgage bond, and the debtor is liquidated within six months of the registration of the notarial bond or mortgage bond, no preference is recognised under the notarial bond or mortgage bond. Effectively, the creditor loses his or her security.

Section 34 of the Insolvency Act also provides that if a company or individual sells a business or any assets forming part of the business (other than in the ordinary nature of business) and fails to advertise the sale in the Government Gazette and two local newspapers for not more than 60 days and not less than 30 days before the date of the transfer, and the company is subsequently liquidated within six months of the transfer, the liquidator can call upon the third party to give back the assets and the business. In most impeachable transactions, the other party must, for no consideration, return the asset so disposed or its value to the estate and then prove a concurrent unsecured claim for any loss it suffers. In the case of a collusive dealing, the other party can, in addition, forfeit his or her claim and is guilty of a criminal offence. Section 341(2) of the Companies Act provides that any disposition by a company of its property after the date of liquidation (the date of issue of the application papers or the date of registration of a special resolution for winding-up) is void if the company is unable to pay its debts. There is a limited power for the recipient of the disposition to seek the court's intervention to validate the transaction.

32 Proceedings to annul transactions

Does your country use the concept of a 'suspect period' in determining whether a transaction by an insolvent debtor can be annulled? May voidable transactions be attacked by secured creditors or by unsecured creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or suspension of payments or only in a liquidation?

South Africa does not in general recognise a particular 'suspect period' and there is no general time period in which all transactions are voidable. The impeachable transactions set out in sections 26, 29, 30 and 31 of the Insolvency Act (as set out in question 31) are subject to specific time limits as set out in the Act - the transactions under sections 26, 30 and 31 are not limited by time, whereas section 29 is limited to the six months prior to liquidation. In general, however, all voidable transactions must take place when, factually, the debtor's liabilities exceed its assets. In the case of a company or corporate body, all transactions taking place after the effective date of liquidation (see question 7) are void (not merely voidable).

Voidable and void transactions can only be attacked by a liquidator or trustee, but the creditors (be they secured or un-secured) can instruct the liquidator to do so. If the liquidator is reluctant to do so (for example, if there are no funds in the estate), a creditor may take action in the name of the liquidator provided he has indemnified the liquidator against any costs.

In an informal reorganisation or a 311 scheme, the company has no power to set aside voidable or void transactions. In the case of judicial management, when it is apparent that the company will not be able to pay its debts, the Companies Act specifically empowers the judicial manager to exercise all the powers of a liquidator in setting aside voidable or void transactions.

33 Directors and officers

Are corporate officers and directors liable for or can they be made to pay obligations owed by their corporations?

Whether the company is wound up by way of a shareholders' special resolution or by way of a compulsory application to court, the shareholders will not, as a general rule, incur any liability other than a loss in their investment if the assets of the company are not sufficient to pay all of the creditors of the company. Directors and corporate officers may, however, incur personal liability for pre-liquidation debt in certain circumstances. The most relevant provision is section 424 of the Companies Act, which provides that any person who was knowingly a party to the carrying on of the company's business in a reckless or fraudulent manner may be declared liable by the court for any or all of the debts or liabilities of the company. There is a similar provision in the Close Corporations Act. In limited circumstances, if there is gross abuse of the separate juristic personality of the company or corporation, the court may hold the directors or members liable.

In addition, South African tax law requires every company or corporate body to appoint a natural person to be the public officer (who is usually a director). In certain limited circumstances, the public officer can be held personally liable for unpaid income tax, employees' tax and VAT, if the company is unable to pay the said taxes for any reason.

34 Duties of directors to creditors prior to bankruptcy

Do corporate directors and officers have any liability for pre-bankruptcy actions by their companies? Can they be made subject to sanctions or penalties for other reasons?

As set out in question 33, corporate directors and officers can be held personally liable for the debts of the company under section 424 of the Companies Act if they were a party to the reckless or fraudulent carrying on of the business of the company. In addition, section 424 provides that any person who was knowingly a party to the carrying on of the business of the company in a reckless or fraudulent manner is also guilty of a criminal offence and liable for a fine or imprisonment for a period of not more than two years, or both such fine and imprisonment. If any directors or corporate officers defrauded the company prior to liquidation by, for example, misappropriating funds, the liquidator can sue them civilly under an action for common law fraud and can also pursue criminal charges. If the company is wound up on the basis that it cannot pay its debts, then the directors and corporate officers can also be charged criminally for certain actions prior to liquidation: the falsifying of business records; the disposition of the company's assets other than in the ordinary course of business; the obtaining of credit based on false representations as to ownership of assets or amount of liabilities; the failure to maintain proper business records; and the incurral of credit without the reasonable expectation of being able to repay the debt.

35 Creditors' enforcement

Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

South African law therefore recognises the rights of debtors and creditors to agree in their security documentation that the creditor can take possession and ownership at fair value of the secured asset or sell the asset to a third party for fair value, without recourse to the courts. This is subject to the proviso that the debtor has the right to approach the courts for relief if it regards the creditor as abusing its position and taking the secured assets at less than market value.

Such provisions also may not be used to allow a creditor that is not in possession of the asset to obtain possession and deal with the asset without recourse to the courts.

However such contractual provisions will NOT be upheld by South African courts where the security is over immoveable property.

36 Corporate procedures

Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

Yes, there are two forms.

The first corporate procedure is the shareholders' or members' resolution to wind up the entity, which may be granted in circumstances where the entity is insolvent, as well as in circumstances where the entity is perfectly solvent or simply a dormant shell. In the case of a company, the winding-up is either a members' voluntary winding-up or a creditors' voluntary winding-up and must be passed on the basis of a 75 per cent majority. The procedure is set out in more detail in question 7. In the case of a close corporation, no distinction is made and the members must unanimously pass a resolution agreeing to wind up the close corporation, whether insolvent or not.

The shareholders of a company and the members of a close corporation may also resolve to wind up the company or close corporation by way of an application to court.

The second corporate procedure is deregistration, a process in terms of which a corporate entity ends its corporate existence. Deregistration entails the cancellation of the company's articles and memorandum of association in terms of K 73 of the Companies Act and, in the case of a close corporation, entails the cancellation of the founding statement in terms of section 26 of the Close Corporations Act. Deregistration may be effected at the instance of the registrar of companies or the registrar of close corporations, if he or she has reasonable cause to believe that the company is not trading and has no assets and liabilities, or at the request of the company itself.

Deregistration differs from liquidation (whether by special resolution or by compulsory application to court) in that no liquidator is appointed, as the entity has no assets or debts that need to be administered. Moreover if an entity is insolvent, the liquidation expunges the debt; the deregistration on the other hand, merely suspends as unenforceable any debts that may exist – if the entity is re-registered, the debts are enforceable again. A liquidated entity cannot be re-registered.

37 Conclusion of case

How are liquidation and reorganisation cases formally concluded?

The liquidators file their final liquidation and distribution account, make any payment in terms thereof and then advise the master that the administration of the estate is complete. The master, in the case of a company or close corporation, will then transmit a certificate to that effect to the Registrar of Companies and close corporations. The registrar then records the formal dissolution of the company or close corporation and publishes notice thereof in the Government Gazette. The formal date of dissolution of the company or close corporation is the date of the recording of that fact. Once all creditors are paid in terms of a 311 scheme, the creditors are notified of the conclusion of the scheme – there is no need to return to court.

38 UNCITRAL Model Law

Is the adoption of the UNCITRAL Model Law on Cross-Border Insolvency under consideration in your country? If so, what is the present status of this consideration?

The UNCITRAL Model Law on Cross-Border Insolvency has been favourably received by the government and has been embodied, although not incorporated by reference, into the Cross-Border Insolvency Act 42 of 2000. While the Act came into effect on 28 November 2003, the Act applies to 'States designated by the Minister'. Thus, the Act will not take practical effect until the states are designated, which has not yet happened.

39 International cases

What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments?

The South African government recognises and supports the UNCITRAL Model Law on Cross-Border Insolvency. Thus, the Cross-Border Insolvency Act, referred to in question 36, was enacted and comprises substantially the provisions of the UNCITRAL Model Law on Insolvency. The Act entrenches a spirit of cooperation with foreign liquidators, trustees and courts in specified states and provides for liquidators or trustees appointed in a foreign country to gain recognition in South Africa by way of application to court and to grant to such recognised liquidators or trustees all the powers of a South African trustee or liquidator. The Act also provides for the coordination of foreign and local proceedings.

Until the Cross-Border Insolvency Act takes effect, at common law a liquidation or sequestration order has no effect per se on the immoveable property owned by an insolvent that is situated in a foreign country. Such property remains vested in the insolvent, but with regard to moveables, the position is different. A sequestration or liquidation order granted by the court where the debtor was domiciled, ipso facto, divests the insolvent of all moveable property wherever situated, even in a foreign country. If the sequestration or liquidation order is granted by a court in which the insolvent is not domiciled, then the order has no operation on his or her assets, whether moveable or immoveable, situated out of the court's jurisdiction. It follows that, where an insolvent has been sequestrated or liquidated by the order of a foreign court in whose jurisdiction the insolvent was domiciled at the time of sequestration or liquidation, any moveable property found in South Africa belonging to the insolvent would vest in the trustee or liquidator appointed by the order.

Although formal recognition by the local courts of the foreign trustee or liquidator to enable him to deal with the insolvent's moveable property is not strictly necessary, as a matter of practice an application is invariably made. Formal recognition by South African courts is, however, required by a foreign trustee or liquidator to deal with the insolvent's immoveable property situated in South Africa, or in circumstances where the foreign court was not the court of domicile of the insolvent and there is moveable property situated in South Africa.

The grant of recognition is no mere formality. South African courts have the absolute discretion to grant or refuse an application for recognition. The discretion is usually exercised on the basis of comity or convenience. It is unlikely that such a discretion will be exercised in favour of recognising the foreign trustee or liquidator if the insolvent was not domiciled in a foreign country at the date of insolvency. A foreign creditor may prove his or her claim in the

Update and trends

The most significant development under South African insolvency law is the introduction of the new business rescue model (replacing judicial management) which is due to be enacted and in effect by late 2009 or early 2010. The new model is significant departure from South Africa's largely creditor friendly regime to a more debtor-friendly regime. For more detail, see question 41.

same manner as a local creditor. The Act, when effective, will further protect the interests of foreign creditors, by, for example, obliging local trustees or liquidators to extend all notices to foreign creditors, recognising the ranking of foreign creditors as not below that of local concurrent creditors and granting foreign creditors additional time in which to prove claims.

40 Cross-border insolvency protocols and joint court hearings

In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?

Save for the enactment of the Cross-Border Insolvency Act 42 of 2000, South Africa has not entered any cross-border insolvency protocols or other arrangements with any other countries. Save for South African courts granting orders recognising foreign trustees or liquidators, the courts in South Africa have not held 'joint hearings' with courts in other countries in cross-border cases.

41 Pending legislation

Is there any new or pending legislation affecting domestic bankruptcy procedures, international bankruptcy cooperation or recognition of foreign judgments and orders?

For a number of years there have been calls for a reform of, and consolidation of, insolvency law in South Africa. A draft Insolvency and Business Recovery Bill was approved for tabling in parliament during 2003. The Bill sought to combine the Insolvency Act and the liquidation provisions of the Companies Act into a single piece of legislation. However, the Bill was put on hold pending a commission of enquiry into aspects of the insolvency industry.

In the meantime, it was decided to overhaul the Companies Act and to replace it in full with a new Companies Act. The new Companies Bill has been published but is unlikley to be enacted and in force before 2009/2010. A draft of the new Companies Act was published for comment in early 2007, and introduced a new form of business rescue (replacing judicial management), based loosely on the bankruptcy proceedings under chapter 11 of the US Bankruptcy Code. The new business rescue proceeding is a significant departure from the current judicial management model, and is much more debtor-friendly. The Companies Bill, in keeping with international trends, broadens the concept of 'business rescue' away from simply trading the debtor back to solvency (as under judicial management) to include the sale of the whole business to generate a better return than a liquidation dividend. The Bill contemplates that a debtor can invoke business rescue and an immediately effective moratorium simply by filing a resolution at the Companies Office, and an aggrieved creditor is obliged to launch a court application to object. Following the resolution for business rescue, the board of directors stays in office throughout the business rescue period but in addition, a 'supervisor' is appointed by the master. This dual appointment (the board and the bankruptcy supervisor) is unique as bankruptcy regimes in international jurisdictions have either a bankruptcy administrator or the board is simply left in office as a 'debtor in possession', subject to court supervision. Following the appointment of a supervisor, the company must prepare a business plan which is then voted on by creditors. Unique under the South African business rescue model is the fact that employment contracts cannot be terminated unless ordinary employment law procedures are followed, namely the debtor company would have to demonstrate proper grounds for retrenchments. This restricts a supervisor from employing one of the most effective methods to reduce overheads. All 'pre-business rescue' contracts and agreements, as well as individual provisions thereof, can be unilaterally cancelled by the board and supervisor (this power is unqualified and there is no need to prove that the contractual provisions constitute impeachable transactions – see questions 31 and 32). Pre-business rescue suppliers are also compelled to supply on same terms and conditions provided they are paid on current basis.

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South Africa

Applicable bankruptcy law, reorganisations: liquidations

The Insolvency Act 24 of 1936, the Companies Act 61 of 1973.

Customary kinds of security devices on immoveables

Mortgage bond.

Customary kinds of security devices on moveables

Special and general notarial bonds, pledges, cessions of book debts (receivables), mortgages over ships and aeroplanes, reservation of ownership (title).

Stays of proceedings in reorganisations/liquidations

311 scheme: No moratorium until scheme sanctioned by court following meetings of creditors

Judicial management: Proceedings stayed on grant of provisional order until order discharged.

Liquidation: Stay of proceedings either the date of registration by the registrar of a special resolution for winding up or the date of issue of court application for involuntary winding up by registrar of court.

Duties of the insolvency administrator

Liquidation: Take possession and control of assets, continue trading in short-term, sell business and assets, either as going concern or piecemeal, recover debts, investigate creditors' claims, prepare a liquidation and distribution account and pay claims.

Judicial management: Take control of assets and business, evaluate likelihood of trading out of difficulty, run the business, report to creditors, pay pre-judicial management creditors as judicial manager sees fit.

Set-off and post-filing credit

If debtor liquidated within six months of set-off, the liquidator may, with the approval of the master, disregard set-off if he can show that set-off was not in the ordinary course of business. In a judicial management, set-off operates as usual. Liquidators may incur credit, as a cost of administration. If the company is not in liquidation or judicial management (eg subject to a 311 scheme), then credit is subject to the ordinary requirements and repayment terms. Judicial manager may obtain credit facilities and the repayments are a cost of administration.

Filing claims and appeals

Creditors' claims are submitted at creditors meetings by way of affidavit. The liquidator can request master, on notice to creditor, to set aside claim. Creditor can substantiate or amend claim before the master makes a decision. If the master disallows claim, the creditor may take decision on review to high court in limited circumstances.

Priority claims

'Preferent' claims, constitute, in order of rank, first charges against the non-secured assets of insolvent estate, ranking ahead of concurrent creditors: the costs of liquidation; employee claims (note: limited preference); arrear levies, duties and taxes owed by the insolvent to government or social service bodies, all of which rank equally; balance of claims filed by a creditor who had security of a general mortgage or notarial bond; and local authorities (municipalities) entitled to be paid for rates and property taxes in arrear for up to two years preceding liquidation out of proceeds of the immoveable property in preference to, and even to the exclusion of, mortgage bond.

Major kinds of voidable transactions

Any disposition by a company of its property after commencement of liquidation (see stay of proceedings) is void if the company unable to pay debts. Transactions can be avoided if assets are disposed of while the company is insolvent in circumstances where assets are not sold for value or in a manner preferential to certain creditors or with intention to prejudice other creditors. If a debtor that is a trader sells business or assets which form part of business without publically advertising the sale in the prescribed manner and is liquidated within six months of the sale, the sale can be set aside.

Operating and financing during reorganisations

A judicial manager takes over functions of the board of directors and runs the business in the ordinary course with a view to restoring the health of the company. For financing, see Set-off and Post-Filing Credit above.

Requirements for approval of reorganisations

311 Schemes: A majority of 75% of creditors in each class of creditors must vote in favour of scheme. Even if creditors approve scheme, scheme must still be sanctioned by the court to become binding.

Judicial management: The granting of a judicial management order lies within the court's discretion. It must be established that as a result of mismanagement or for other cause, the company is unable to pay debts or meet obligations and has not become or is prevented from becoming a successful concern and there is reasonable probability, if judicial management ensues, that it would be able to pay debts, meet obligations and become a successful concern. Creditors' views are not decisive.

South Africa cont

Liabilities of directors and officers

Personal liability for pre-liquidation debt can be attributed to directors and officers if the business is run in a reckless or fraudulent manner.

Pending legislation

The Cross-Border Insolvency Act 42 of 2000 (enacted but not yet in operation at the time of publication). The draft new overhauled Companies Bill 2007 proposes to overhaul and substitute the Companies Act, and introduces a form of Business Rescue based on bankruptcy under Chapter 11 of the USA Bankruptcy Code, unlikely to take effect before 2009 or 2010.

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