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QUESTION 1

A bankruptcy system is essential as world conditions show the existence of the interdependency of bankruptcy laws and credit markets. Financial failure needs a system of predictable, fair and orderly procedures and laws. These procedures and laws bring an end to, or extend the control externally to a debtor's execution of further credit performance and transactions. Bankruptcy sets in motion the collective process which subjects the creditors' claims to a regime whereby all assets are totally or partially removed from the control of the debtor. Lastly, this process should allow the debtor to be discharged of all debt and reintegrated back into society with full financial control.

Fletcher states in *The Law of Insolvency* (1990) that the roots of bankruptcy law can be found in the following Roman law procedures.

Cessio bonorum (assignment of property)

Distraction bonorum (forced liquidation of assets)

Remission and *dilation* (composition with creditors)

These procedures originally developed from the individual debt collecting procedures which gave rise to the development of insolvency law which entails collective debt collecting devices in circumstances where the debtor was found to be insolvent as creditors needed protection from defaulting debtors as well as from each other.

The development of Insolvency law in Europe arose from the *lex mercatoria* which is the Latin word for "merchant law" and which is the body of commercial law which was used throughout Europe during the medieval period and was only used by merchants. Similarly to English Common Law, the *lex mercatoria* evolved as a system of custom and best practice enforced throughout a system of merchant

courts along all major trade routes. It furthermore functions as the international law of commerce.

Bankruptcy however stems from Italian “banca” rotta” which literally means “breaking the bench”. During the medieval period, should a debtor have failed to pay his debts whilst operating in the market place, his creditors would break his bench or counter, thus affecting the closure of his business operations and trade. Only traders, during this period, could be declared bankrupt and would face harsh and severe punishment for failing to meet the obligations of their creditors. Punishments included, inter alia, imprisonment and sometimes even death.

It is at this point, that bankruptcy was seen as a pro-creditor system and it was only until much later that the discharge of debt, alternatively known in some states as a “fresh start” developed which in turn brought out the abolishment of imprisonment or harsh alternative sentences on the debtors.

One of the main aims of an insolvency system is that it should bring about a *concursus creditorium* which effectively brings about the ranking of creditors in a group rather than the individual interest of creditors. This process can be seen to crystallise the debtor’s position and the hand of the law is laid upon the estate and all rights of the general body of creditors are taken into consideration preventing a race against creditors to the assets of the estate and thereafter the *pari passu* distribution to creditors according to their claims in the estate, ensuring that creditors are dealt with fairly.

Wood states in *Principles of International Insolvency Law* (Thomson) 2007 that there is only one truly universal feature in the law of bankruptcy which is that any further action by individual creditors against the debtor are frozen and individual pursuit is stayed.

South African Insolvency Law has origins in both Roman-Dutch and English Law with its true foundation evolving from the Ordinance of Amsterdam 1777. South African Insolvency Law is regulated to a large extent by the Insolvency Act 24 of 1936 which is our primary source of Insolvency Law. The former Companies Act 61 of 1973 as amended and the Companies Act, Act 71 of 2008 (as amended) as well as the Close Corporations Act 69 of 1984 deal with the winding-up or liquidation of Companies and Close Corporations. Common Law provisions are further applicable to the liquidation and winding-up of Close Corporations and Companies. It is therefore stated that a multiplicity of legislation exists in South Africa which legislature need to be considered in conjunction with each other. With the introduction of the 2008 Companies Act, a business rescue procedure has been introduced. This procedure has replaced the previous judicial management as a formal rescue procedure. Other special provisions apply to the winding-up of other legal entities i.e banks.

Statistical data available in South Africa strongly suggests that there is something serious wrong with our insolvency system and major reform is needed. We have been attempting to adopt new Legislation which commenced in the 80's. The aim of this reform is to bring about a modern insolvency law system which is needed as a key foundation of sustainable economic development and a system which could best serve the interests and needs of society to ensure that public confidence is reintroduced into our system whilst ensuring that the underlying values of the Constitution are upheld. Various bodies including The World Bank and The United Nations Commission on International Trade Law have acknowledged the need for a modern insolvency system.

As a result of a multiplicity of legislation, a Report and Draft Bill was published by the South African Law Reform Commission during 2000 wherein the cabinet approved a unified Insolvency Act which would apply to various types of debtors. As it currently stands, our Act does not merge individual and corporate insolvency.

As a consequence of South African Insolvency Law being largely based on Roman Dutch law and which is influenced by early English law, we currently operate a distinctly pro-creditor orientated procedure. Historically, defaulting debtors were treated harshly and there was a lack of solicitude for debtors. A major difficulty faced in debtor-creditor law is the lack of alternative procedures for a debtor that provide for a “fresh-start”. As a result of alternative procedures, debtors utilise the very expensive procedures of the Insolvency Act in order to make a fresh start. The following procedures are available for debtors :

1. Administration – this procedure is for debt under R50 000.00 and affords rescheduling of debt but does not provide for a discharge.
2. Voluntary composition with creditors – discharge of debt is based on consent.
3. Voluntary surrender of the debtor’s estate (sequestration) – the debtor would need to prove a benefit to creditors and discharge is available through rehabilitation subject to the ratification of the Court.
4. Debt review in terms of the National Credit Act (NCA) – this procedure does not provide for a discharge of debt.
5. Regulation of the Credit Bureaux in terms of the National Credit Act.

The following remedies are available to creditors :

1. Individual debt collecting procedures (judgment followed by attachment).
2. Compulsory sequestration.

Discharge is not a principal aim of our Insolvency Law but as a consequence of rehabilitation. South Africa lacks remedies which provide for the discharge of debtors from their debts.

South Africa should attempt to find a balance between debtors and creditors interest and the following should be taken into consideration :

1. Re-evaluation of our “creditor-friendly” approach and creating affordable access to insolvency procedures which would lead to an eventual discharge
2. Developing a single portal alternative debt-relief system sustainable to the debtor to whom the formal insolvency procedure would not be feasible
3. Debtor counselling and financial management training is an intergral part of insolvency and pre-insolvency procedures
4. Developing a strong institutional framework and the possibility of appointing courts specifically dealing with insolvencies and financial distress.

It is stated by Dalhuizen that “[B]ankruptcy is viewed more and more as an extraordinary measure to be reserved for exceptional circumstances.” This “extraordinary measure” is being extensively used in South Africa as a result of the lack of alternative options to debtors seeking relief.

The statistics of the data available in South Africa reflect that in 28,6% of cases concurrent creditors will receive a dividend whilst 40,6% will be liable to make a contribution thus supporting the need for reform of an ailing system.

A distinct feature of the Insolvency Law of England and Wales is seen in the division between the Law of insolvent individuals and the law governing corporate insolvency. The decision of the House of Lords in *Salmon v Salmon & Co* is known to have changed commercial law where it was found that a company when duly formed, was “a distinct person in law and the company’s debts were separate and self-contained”. It was at this point, that two separate collections of statutes dealing with individual and corporate insolvency were introduced.

Corporate bankruptcy is achieved by one of three modes, namely, the court, creditors’ voluntary winding-up and members’ voluntary winding-up. These methods are used for Companies and Close Corporations. Further special provisions are

applicable for the winding-up of other legal entities such as pension funds, banks, medical funds etc.

At it currently stands, the main characteristic of South Africa's corporate rescue mechanism is Business Rescue. As a result of the failure and criticism of the Section 311 regime and the low incidence of successful cases, an alternative more modern regime was devised to assist financially distressed businesses in the form of Business Rescue. It is stated by Professor Rajak that "Business Rescue has been invoked where insolvency is believed to be temporary and the debtor is able, with assistance, to return to commercial life as an advice and successful entrepreneur". Business Rescue is supported in that there is preservation of employment and a possibility of some payment to creditors, in part or in full which would place them in a better position financially than the position they would have been in should the Company have been liquidated. Consideration to the size of a business seeking a form of discharge from debt should be taken into account. Because business rescue is an expensive process, small business might not benefit by this procedure and it would be too costly for a small business. Alternative options for financially distressed small enterprises is needed in South Africa and perhaps procedures which are less formal and which are free of court and professional involvement which would be more affordable to a small enterprises.

All affected persons, especially employees should be considered during insolvency proceedings and business rescue proceedings. 1999 saw notice being given that would require an amendment to the insolvency laws of South Africa which were to alleviate the adverse effects of liquidation upon employees. This was one of the most significant manifestations of pressure exerted by the labour movement on the insolvency law fraternity ever experienced in South African legal history. The new Section 38 of the Insolvency Act provides that "contracts of employment of employees whose employer has been sequestrated are suspended with effect from the date of the granting of a sequestration order".

After the initial suspension contracts of employment may either be terminated or will automatically terminate after the final appointment of the trustee or liquidator however subsequent to consultation with the affected persons. The previous section of the Insolvency Act dealing with employees made no provision for consultation with the employees and provided for immediate termination of employment. Should the business be sold as a going concern, all contracts of employment are transferred from the old to the new employer which system was introduced into South African Labour Law during 1996.

Section 38 of the Insolvency Act should be read in conjunction with S98A of the Act in that it regulates the order of preferential payment to employees for arrear salaries and leave payment where contracts of employment have been terminated by virtue of Section 38.

In conclusion it can therefore been seen that a bankruptcy system is needed to deal with the financial failure of companies to ensure a system of predictable, fair and orderly procedures and laws which are set in motion at the time of the *concursus*. Alternative discharge procedures are urgently needed outside bankruptcy as it is evident from data available that our system currently is not working and is extremely costly and as a result of the pro-creditor system, does not allow for a discharge of debt or a fresh start for debtors which in turn is resulting in an abuse of the system. In attempting to adopt new legislation, South Africa has become isolated and have ignored global trends and it would be beneficial for South Africa to attempt to integrate the knowledge and experience of the US into its economic and cultural environment rather than adopting a foreign process entirely as the US has been classified as “a model for consumer insolvency reform” which reform is much needed in South Africa.

QUESTION 2

(a) The EU Insolvency Regulation has been formed in an attempt to harmonize insolvency law In Europe which has arisen as a consequence of the lack of a uniform system of security rights in Europe and a great diversity of national insolvency laws as to the priority given to different classes of creditors. It was formed to establish a common framework for insolvency proceedings in the EU with the main objective being to avoid the transfer of judicial proceedings or the transfer of assets from one EU country to another. The EU Regulation is binding and is directly applicable in any Member States of the Union (except Denmark) where main insolvency proceedings are opened. Main proceedings in insolvency take place in the state of the centre of main interest (COMI). The applicable law will be that of the law of the opening state and proceedings apply to all goods of the debtor in the European Union. If proceedings are contrary to the public policy of another country they do not affect the rights in rem and can be ignored.

A Working Group was formed which consists of 15 professionals from ten countries to study the question of how the differences can be reconciled. The Working Group have developed 14 principles which deal with the following topics :

- Insolvency proceedings
- Institutions and participants
- Effects of the opening of procedures
- Management of the assets
- Obligations incurred by, and fees of, the administrator
- Treatment of contracts
- Position of employees
- Reversal of juridical acts
- Security rights and set-off
- Submission and admission of insolvency claims
- Reorganization
- Liquidation
- Closure of proceedings
- Debtor in possession

On the other side of the scale the UN Model Law on Cross-Border Insolvency has been designed to assist States to equip themselves with a modern legal framework to address cross-border insolvency and proceedings concerning debtors experiencing financial distress or insolvency. The Model Law focuses on encouraging cooperation and coordination between jurisdictions and a UNCITRAL Practice Guide on Cross-Border Insolvency Co-operation was adopted setting out guidelines to judges on information on protocols and court to court co-operation. The Model Law focuses on the following four elements which have been identified as key to the conduct of cross-border insolvency :

- Access
- Recognition
- Relief (assistance)
- Cooperation

The UN Model Law is designed to assist states to manage transnational insolvency cases. Transnational insolvency relates to insolvency proceedings in one country with creditors located in at least on additional country and in some complex cases it can involve multiple proceedings with creditors in numerous nations.

Model Law does not attempt to harmonise local insolvency law and addresses a large range of international, legal and economic concerns whereas the EU Insolvency Regulation attempts to harmonise local insolvency to avoid transference of judicial proceedings between countries.

Unlike the EC Regulation, which has automatic effect throughout the EU, the Model Law provides for countries, if they wish, to modify or leave out provisions within the model in order to adapt the law to their own country's particular circumstances. In fact, countries are not bound to implement the Model Law at all.

In conclusion, whereas, the EU Regulation is only specific to the Nations of the United Kingdom, the Model Law has been developed by a large number of States with different legal traditions and is an instrument to compromise solutions and should it be enacted as part of an existing insolvency registration will co-ordinate and facilitate cross-border insolvency proceedings. Model Law can be seen as a valuable tool to provide more unified rules for cross-border insolvency and result in reciprocity which will facilitate future work towards a more comprehensive and ambitious regime as well as provide a modern framework to address insolvency proceedings.

(b) England and Wales are constituents of the United Kingdom and are considered to be one jurisdiction and in considering the rules that apply in England and Wales, one would need to distinguish between whether the insolvency proceedings occurred without the UK or outside of the UK.

Other countries which make up the United Kingdom include Scotland and Northern Ireland. Further, the United Kingdom is considered to be one country and which provisions for deciding on cross-border insolvency matters can be found in their domestic legislation, largely being the Insolvency Act of 1986. As a consequence of the UK being considered one country, the UNCITRAL Model Law on Cross-Border Insolvency cannot be utilised to decide on matters that arise between the countries within the United Kingdom. The United Kingdom is obliged by Section 426 of the Insolvency Act to assist courts within the jurisdictions of the UK together with foreign courts on matters which occur within the UK.

Under English Law all property belonging to the insolvent, wherever situated, is covered by the Act which empowers the liquidator or trustee to deal with all assets. In practice, however, it is often the case that the country in which the property is situated will retain control of the property, regardless of the making of an insolvency order in England and Wales.

Should the cross-border insolvency occurs within the UK, the following rules will need to be applied :

Any insolvency law court orders which are made in the United Kingdom should be enforced in any other part of the United Kingdom as if the order were made by a court in that jurisdiction, expect for any orders which relate to property. Should this happen the jurisdictional court will have the discretion on how to enforce the order.

Mutual assistance between courts in the United Kingdom is required and any court having jurisdiction relating to insolvency law in any part of the United Kingdom should assist courts which have corresponding jurisdiction in other parts of the United Kingdom.

Official receivers who are dealing with property situated in a part of the UK other than England and Wales should apply for requests for assistance from the courts in another part of the UK where the property is situated to seek assistance in that regard. In retrospect, where an official receiver wishes to make application for an order to take proceedings in relation to a property situated in a part of the UK other than England or Wales, they must apply to a Court in England/Wales where the insolvency proceedings have commenced. That court may request the court in the other jurisdiction to assist.

Cross-border warrants of arrest relating to insolvency law are enforceable in any part of the United Kingdom.

Should the cross-border insolvency occurs outside the UK, the following rules will need to be applied :

The official receiver will attempt to deal with the matters on an informal basis due to time and cost constraints and attempt to obtain cooperation of the debtor. Where difficulties are encountered, the official receiver will then be required to determine whether the country outside of the UK has signed up to the UNCITRAL Model Law and consider the appropriate further action required and what is actually possible.

Should the outside country (not situated in the UK) and one that has not implemented the UNCITRAL Model Law, the official receiver will need to seek assistance of the foreign court under local laws of that country to grant an order for assistance to enable the continuation of the statutory duties of the receiver.

(c) One of the main aims of the Cross-Border Insolvency Act is to provide easy and speedy access and recognition of foreign representatives or creditors, while retaining measures to curb abuse. The equal treatment of local and foreign ordinary creditors is provided for in the act, however safeguards the rights of local secured and preferent creditors. The Act is currently in force, however only once all the States who will participate are designated will the Act become effective.

The most substantial difference and an important deviation between the Cross-Border Insolvency Act in South Africa and the UNCITRAL Model Law is that the Act requires reciprocity. Section 2 provides that the Act applies in respect of States designated by the Minister responsible for the administration of justice. The Minister may only however designate a state if satisfied that the recognition accorded by the Law of such a State to proceedings under the laws of the Republic relating to insolvency justifies the application of the Act to foreign proceedings in such a State. The Minister has not designated any States and it seems that designation (which much be tabled in Parliament) is not imminent. Reciprocity results in both inward bound and outward bound

requests on insolvency matters and the Act is somewhat more limited in application to the Model Law.

As a consequence of the USA adopting the Model Law, they have made significant changes to the process and procedures of their international insolvencies and have in this adoption continued to favour universalism (one primary proceeding) rather than a territorialist approach which provides for multiple proceedings. These preferences taken together will favour the "home country" of the foreign debtor as the location for the main bankruptcy action. Numerous other countries including Canada and Australia have followed the precedent of the USA.

In conclusion the lack of reciprocity provisions in Section 2 of the Act could seriously impede South Africa entering the international arena.

QUESTION 3

(a) As a consequence of a liquidation order having been granted in Mozambique and as a result of the company having movable assets situated across its border, cross-border insolvency would need to be applied.

Because foreign sequestrations affect the rights of third parties they should not be merely seen as judgements. It is stated in *Stegmann* Innes JP that "foreign sequestration orders were not to be classed (as in Roman-Dutch law) merely as foreign judgments", he further went on to say that they were "special" as a result of affecting other third parties rights.

As it currently stands, the Cross-Border Insolvency Act is not yet in force or effect in South Africa and as it stands Cross-Border Insolvency is governed by the principles of the Common Law. Like many other systems, the South African legal system blends two contradictory approaches to cross-border insolvency, the territorialist theory and the universalist theory.

It would be recommended to the foreign liquidation that he should take cognisance of the fact that they have entered South Africa through the gateway of the Cross-Border Insolvency Act and will have to abide by the local rules. This process will be more efficient and much quicker as the foreign representative would be able to rely on the local knowledge in South Africa.

Under South African law, a foreign representative would need to be recognised as a representative in South Africa. Irrespective of whether the property belonging to the debtor is immovable or movable, a foreign liquidator, as a matter of practice would need to apply for formal recognition by the local court. The granting of this recognition order by a South African court would entitle the Liquidator of the foreign country to deal with the assets as if they were in the foreign country. It would not be necessary for the liquidation order to be recognised because it is only dealing with movable assets which movables "follow the person" and the court order issued by the court of the insolvent's domicile automatically vests those assets in the trustee which have not been vested in them. This is seen at *Mars op cit at 178; cf Re Estate Morris 1907*. The order, would however, be subject to the South African Courts imposition of conditions for the protection of its local creditors or recognition of the requirements of South African laws.

The principles of "comity, convenience and equity" would play an essential role in the exercise of the discretion of the court to recognise a foreign Liquidator.

Comity can be described as :

"the courteous and friendly understanding, by which each national respects the laws and usages of every other, so far as may be without prejudice to its own rights and interests".

Recognition of the foreign order has the same effect on the asset as a local order of liquidation. The Court in granting the recognition order will set conditions for the administration and realization of the local assets. These conditions can be seen in *Ex parte Steyn*.

A rule *nisi* should be directed in respect of the Application to the High Court and should call on all persons to show cause, if any, why the order should not be granted. Furthermore the rule *nisi* should include a temporary interdict and directions for serving the notice on the debtor. The type of order which the court will grant when a foreign representative applies for recognition is to be found in *Moolman v Builders & Developers (Pty) Ltd*.

Rights exist relating to administration, as if the law applied thereto, on the date of the recognition order. The rights defined by the South African Insolvency Law, and if applicable to the Company Law, in favour of the Master, a creditor, and an insolvency or company being would up, in regard to meeting of creditors, proof, admission and rejection of claims, sale of assets, plans of distribution of proceeds, and the rights and duties of a trustee or liquidation concerning those matters are considered. The applicant would further requested to provide security for proper performance and the order is subject to amendment by the Court. The applicant is further required to comply with all provisions relating to the operation of banking accounts and the transfer of funds out of South African.

The South African Court should take the undermentioned points into account when considering an application for recognition and especially with a view to protecting local creditors :

1. The interests of the creditors generally, particularly if local creditors' rights are not harmed by the recognition order;

2. The commonality of the foreign law and South African law;

3. The number and value of creditors in the foreign country, compared with those in South Africa;

4. The debtors assets and their value in the foreign country compared with those in South Africa;

5. The foreign sequestration order's provision for South African creditors – convenience for them to prove their claims, the guarantee of the foreign trustee's properly administering the estate, the safeguards in the recognition order ie. that nearly all the rights created by the South African Insolvency Act extend to interested parties;

6. Foreign creditors' ease and expense of proving their claims in South Africa. Such creditors may use powers of attorney to prove their claims;

7. Equity is an important consideration.

8. A possible converse of the rule in *Ex parte Wessels & Venter NNO: In re Pyke-Nott's Insolvent Estate* 1996 (2) SA 667 (O).

The listed factors have to be weighed against each other to establish the balance of convenience and can be illustrated by *Re Estate Morris* 1907 TS 657.

(c) In support of the above application for recognition the following documents are to be attached to the application :

1. A certified copy of the decision commencing the foreign proceedings and which appoint the foreign representative, alternatively
2. A certificate from the foreign court affirming the existence of the foreign proceedings and of the appointment of the foreign representative; or
3. In the absence of the evidence referred to in paragraphs (a) and (b), any other evidence acceptable to the court of the existence of the foreign proceedings and of the appointment of the foreign representative, and also by
4. A statement identifying all foreign proceedings in respect of the debtor that are known to the foreign representative.

QUESTION 4

In ordinary usage the word “void” means a lack of existence, a nullity, However, “void” is a very powerful word and contemplates an absolute. The main role of voidable dispositions in South African Insolvency law is to avoid certain transactions which are to the detriment of creditors developed concomitantly with execution (debt collecting) procedures of property. When a creditor uses their rights by way of a judgement or execution to realise property of the debtor it is classified as an individual debt collection device, however, these rights become collective when a debtor becomes bankrupt which sets in motion the collective debt collecting procedure. It is necessary to consider the disposal of assets prior to the granting of a liquidation order.

Rules have been developed by legal systems in an attempt to discourage debtors from putting their assets beyond the reach of their creditors which problem arose

within the ambit of individual debt collecting procedures. A doctrine of avoidable transactions form an important part in execution law of the collective devices.

Voidable transactions are divided into two categories, both of which categories are within creditors' rights :

1. Fraudulent Conveyance Law
2. Preference Law

Fraudulent conveyance law started out as individual execution however became operative within the collective debtor process for example bankruptcy. The principle of fraudulent conveyance law is to nullify actions made by the debtor which would hinder or defraud creditors or transactions made without due consideration thereby diminishing the assets available for execution to the general body of creditors.

Preference Law addresses payments made by the debtor to settle pre-existing debt which will in effect improve that particular creditor's position on crystallisation of the estate and will promote the creditors position in the hierarchy of creditors. This enhances the creditor's chance of receiving a better dividend by promoting their rank in the distribution order of creditors. Preference law is accepted as an integral part of insolvency or bankruptcy law and is restricted to the debt collective procedure of bankruptcy law.

In *Cooper NNO v Merchant Trade Finance Limited* (2000 3 SA 1009 (SCA)), the Court dealt with certain core aspects of voidable dispositions and the subjective elements of both Sections 29 and 30 of an intention to prefer on the part of the debtor. This case further dealt with the definition of a "disposition" and the security obtained by a creditor in terms of a general notarial bond and the outcome of the perfection of the bond which would improve his ranking amongst other creditors.

Walker v Syfret (1911) AD 141 states that the "rationale for a law permitting the avoidance of preferences is to promote the *pari passu* principle, referred to within the ambit of the *concursus creditorum* in South African law".

It is pointed out by Jackson and Kronman in "Voidable Preferences and Protection of the Expectation Interest" 1976 Minnesota Law Review 971 977 that American Law is addressing preference rules and are attempting to move away from the inherent subjectivism of the "fraud" idea and are attempting to set principles rather based on objective criterion which will assist in excluding subjective intent. This could be compared to the effect of s 88 of the South African Insolvency Act relating to bonds registered within 6 months not granting security for the debt.

The Law Commission's Draft Insolvency Bill has retained subjective elements in the application of preference rules and have in addition included a number of rebuttable presumptions to attempt to make it more difficult for the debtor to prove that the disposition was made in the ordinary course of business.

South African law, unlike English Law does not recognise the "floating charge". This charge does not attach to specific assets and is a general charge of all the assets, current and future. In South Africa, general notarial bonds are registered in a similar fashion i.e. over the stock of a liquor store. The floating charge will become a fixed charge (referred to as crystallisation) when specific events occur, inter alia, failure of the debtor to pay the principal or interest instalment, liquidation of the debtor, appointment of a receiver under the charge, cessation of the business or enforcement by another creditor of its security. Crystallisation fixes the debtor's floating charge and this provides for real security over the assets.

QUESTION 5

Section 2 of the Insolvency Act of 1936 defines “security” as “in relation to the claim of a creditor of an insolvent estate, means property of that estate over which the creditor has a preferent right by virtue of any special mortgage, landlord’s legal hypothec, pledge or right of retention”.

A secured creditor therefore is a creditor who holds security for its claim and who are almost assured of receiving settlement of their claims in part or in full.

Forms of real security which are recognised by the Insolvency Act include, mortgage bonds of immovable property, special notarial bonds over movable property specifically describing the hypothecated property (registered after 7 May 1993) and special notarial bonds over movable property in the KwaZulu-Natal province registered in terms of Section 1 of the Notarial Bonds Act (Natal) 1932, a lessor’s tacit hypothec over the *invecta et illata* of the lessee and the hypothec of a credit grantor in terms of an instalment sale transaction, a pledge and a lien.

Some unsecured creditors are secured and these are referred to as statutory preferences (excluding real securities) and are are acknowledged in the South African legal system which include, inter alia, employee’s claims in respect of unpaid salaries and wages, South African Revenue Services in respect of vat, staff taxes i.e PAYE, income taxes, customs duties and certain charges in favour of local authorities.

The purpose of real security is to afford priority to the secured creditor for repayment of his debt. This security results from the agreement formulated between the creditor and debtor and which agreement enables or provides the creditor with options to demand security against the finance or not. Real security is exceptionally important in commerce to allow for the implementation of a structure to allow the debtor to maximise its potential wealth by offering its property for credit and thereby

protecting the creditor against the non-payment for which they have taken the financial risk. In a modern credit-driven economy it is essential to have real security.

The idea of a *pari passu* distribution is thwarted by existence of preferential debt. The Cork Report which was prepared by a Committee under the chairmanship of the late Sir Kenneth Cork pointed out that "they had received a considerable volume of evidence, much of it critical of the law at that time (1982) and they describe it :

"*deeply hostile to the retention of any system of preferential debts".*

The Committee contend that preferential debt hindered and went against the principle of *pari passu* distribution. This in effect deprived unsecured creditors and non-payment of concurrent claims in part of full, which rarely ever happens, would cause further financial hardship and future insolvencies.

Rights to preferential claims in Australia and Canada have been removed and significantly reduced. It can be seen that there is a substantial difference of treatment of preferential claims throughout the world and in particular to taxes.

English Law makes for a provision of a floating charge. South Africa does not recognise the floating charge, however, a general notarial bond can be registered in similar circumstances to the floating charge and is often over movable assets i.e. stock of a liquor store. A floating charge is over the assets and will only crystallise in certain circumstances for example liquidation or failure of the debtor pay the debt. On crystallisation, the debtor's floating charge becomes fixed and results in the creditor obtaining real security over the assets. The advantage of the floating charge is that it applies to present and future property of the debtor.

QUESTION 6

The Insolvency profession in South African is and always has been an unregulated profession. The large increase in the number of Insolvency Practitioners registered reflects that the previous “small band” of professionals in the changing liquidation environment in South Africa is fast changing with the inclusion of previously disadvantaged individuals. An unregulated body of professionals is often a cause for concern as it results uncertainty, irregular and unsatisfactory practices and often confusion and tension within the industry which in effect has diminished and impaired the confidences of the professionals and public in the industry.

The Master of the High Court currently regulates the Insolvency profession in South Africa. However, because the responsibility of the appointee is a substantial role to play it is of utmost importance that experience, qualifications, ability and knowledge be addressed. It is said that as a result of light restrictions on who can be appointed as a practitioner, it is often found that inexperienced and poorly qualified persons are being appointed.

It is stated by the Cork committee that “the success of any insolvency system is very largely dependent upon those who administer it”. The committee has recommended that every practitioner should have a minimum qualification or member of a professional body and further the practitioner should satisfy criteria specifically stated.

In order to attempt to bring about the reform needed in South Africa the unsatisfactory practices experienced need to be addressed. An example can be taken from the Insolvency Act 1986 of the United Kingdom which saw a comprehensive review of bankruptcy in over a century and which introduced government-monitored self-regulation which formed an executive agency within the department of trade and industry under the direction of the inspector-general of insolvency who are responsible for the regulation of insolvency practitioners. It is

felt that mere regulation by professional bodies was insufficient and allowed poorly qualified persons to be appointed as insolvency practitioners.

Because insolvency practitioners are appointed in a position of trust, the person should be subjected to entry-level requirements which should be introduced to regulate the industry. Formal training should be given to candidates and specialised training programmes developed to enable the person entering the profession to deal with the often complex nature of matters which might arise.

Further reform in South Africa would be achievable through the review of the requisition system and how the appointment of practitioners is made. Review of the process will restore faith into the system which has seen fraud and unethical practises over the years.

The European Bank for Reconstruction and Development (EBRD) have developed a set of principles from their assessments and surveys which they regularly conduct. This measures the effectiveness and extensiveness of insolvency laws within its countries of operation. The laws are then measured against best practices and international standards. These principles include a 12 step approach to ensure that appropriately qualified professionals are appointed to hold office. The principles are:

Principle 1 – Qualification and licensing generally

Principle 2 – Appointment in an insolvency case

Principle 3 – Review of Office Holder appointment

Principle 4 – Removal, Resignation & death of Office Holder

Principle 5 – Replacement of Office Holder

Principle 6 – Standards of Professional and Commercial conduct

Principle 7 – Reporting and supervision

Principle 8 – Regulatory and Disciplinary functions

Principle 9 – Remuneration and expenses

Principle 10 – Release of Office Holder

Principle 11 – Insurance and Bonding

Principle 12 – Code of Ethics

In conclusion by establishing a regulated profession and regulated framework which South Africa seems to lack, it could install a degree of respect in the Insolvency industry which will instil a sense of professionalism and efficiency to that of an international standard and in alignment with modern trends throughout the world.

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