



INSOL
INTERNATIONAL



PROGRAMME IN SOUTH AFRICAN INSOLVENCY LAW AND PRACTICE 2023

Summative Assessment (Examination): Paper 1

Date: 23 - 24 November 2023

Time limit: 24 hours (from 13:00 SAST on 23 November to 13:00 SAST on 24 November 2023)

EXAMINER

Ms B Bennett

MODERATORS

Ms R Bekker Dr D Burdette Ms J Calitz Mr Z Cassim Mr E Levenstein

It is imperative that all candidates read and take cognisance of the examination instructions on the next page.

All candidates are expected to comply with ALL the instructions.

AWARDED 83/100

INSTRUCTIONS

1. This assessment paper will be made available at **13:00 (1 pm) SAST on Thursday 23 November 2023** and must be returned / submitted by **13:00 (1 pm) SAST on Friday 24 November 2023**. Please note that assessments returned late will not be accepted.
2. All assessments must be submitted electronically in Microsoft Word format, using a standard A4 size page and an 11-point Avenir Next font (if the Avenir Next font is not available on your PC, please select the Arial font). This document has been set up with these parameters – **please do not change the document settings in any way. DO NOT** submit your assessment in PDF format as it will be returned to you unmarked.
3. No limit has been set for the length of your answers to the questions. Please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case). Candidates who include very long answers in the hope it will cover the answer the examiners are looking for, will be appropriately penalised.
4. You must save this document using the following format: **studentID.Paper1Summative**. An example would be something along the following lines: 202223-336.Paper1Summative. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words “studentID” with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked.**
5. The assessment can be downloaded from your student portal on the INSOL International website. The assessment must likewise be returned via your student portal as per the instructions in the Course Handbook for this course. **If for any reason candidates are unable to access their student portal, the answer script must be returned by e-mail to david.burdette@insol.org.**
6. Due to the high incidence of load shedding currently taking place across South Africa, candidates are required to determine whether any load shedding is scheduled during the examination period and, if so, to make alternative arrangements to write elsewhere if at all possible.
7. Enquiries during the time that the assessment is written must be directed to David Burdette at **david.burdette@insol.org** or by WhatsApp on +44 7545 773890 or Brenda Bennett at **brenda.bennett@insol.org** or by WhatsApp on +27 66 2282 010. Please note that enquiries will only be responded to during UK office hours (which are 9 am to 5 pm GMT, or 11 am to 7 pm SAST).

8. While the assessments are open-book assessments, it is important to note that candidates **may not receive any assistance from any person** during the 24 hours that the assessment is written. **Answers must be written in the candidate's own words; answers that are copied and pasted from the text of the course notes (or any other source) will be treated as plagiarism and persons who make themselves guilty of this will forfeit the assessment and disciplinary charges will follow.** When submitting their answers, candidates will be asked to confirm that the work is their own, that they have worked independently and that all external sources used have been properly cited. If you submit your assessment by e-mail, a statement to this effect should be included in the e-mail.
9. Once a candidate's assessment has been uploaded to their student portal (in line with the instructions in the Course Handbook), a confirmatory e-mail will be auto-generated confirming that the assessment has been uploaded. If the confirmatory e-mail is not received within five minutes after uploading the assessment, candidates are requested to first check their junk / spam folders before e-mailing the Course Leader to inform him that the auto-generated e-mail was not received.
10. If a candidate is unable to complete this summative assessment (examination), please note that a re-sit assessment will only be given if there are exceptional circumstances that prevent the candidate from completing or submitting it (such as illness). Feedback on the final assessment will be provided within four weeks of the paper having been written - please do not enquire about your marks before four weeks have elapsed.
11. You are required to answer this paper by typing the answers directly into the spaces provided (indicated by text that states [Type your answer here]). For multiple-choice questions, please highlight your answer in yellow, as per the instructions included under the first question.
12. Unless otherwise indicated, all references to sections are references to sections of the Insolvency Act 1936.

PART 1 - MULTIPLE CHOICE QUESTIONS (20 MARKS)

ANSWER ALL THE QUESTIONS

QUESTION 1

Questions 1.1 – 1.20 are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and **mark your selection on the answer sheet by highlighting the relevant paragraph in yellow**. Select only **ONE** answer. Candidates who select more than one answer will receive no mark for that specific question. Each of the 20 questions count 1 mark.

Question 1.1

Select the **correct** statement:

Which of the following **does not** constitute an act of insolvency?

- (a) If the debtor makes, or attempts to make, any disposition of any of his property which has, or would have the effect of prejudicing his creditors or preferring one creditor above another.
- (b) If the debtor removes, or attempts to remove, any of his property with intent to prejudice his creditors or to prefer one creditor above another.
- (c) Where judgment is given against the debtor and it appears from the return by the office that he has not found sufficient disposable property to satisfy the judgment (*nulla bona* return).
- (d) A debtor who is over-indebted and unable to pay his debts and has applied for debt review. ✓

Question 1.2

Select the **correct** statement:

Indicate which of the following courts have jurisdiction to sequestrate an estate of a debtor:

- (a) Magistrate's Court.
- (b) Regional Court.

(c) Local or Provincial Division of the High Court. ✓

(d) Both (a) and (c).

Question 1.3

Select the **correct** statement:

The granting of a winding-up order:

(a) Suspends all civil proceedings until the appointment of a liquidator. ✓

(b) Has no effect on pending civil proceedings.

(c) Suspends all civil proceedings until the winding-up process has been completed.

(d) Immediately ends all pending civil proceedings which must be instituted again after the winding-up process has been completed.

Question 1.4

Select the **correct** statement:

Property acquired by an insolvent after sequestration of his estate:

(a) Generally forms part of the insolvent estate.

(b) Does not form part of the insolvent estate.

(c) Vests in the division of the High Court that granted the sequestration order.

(d) Vests in the Master and, after his or her appointment, in the trustee of the insolvent estate until an offer of composition has been accepted.

Question 1.5

Indicate the **incorrect** statement:

(a) The insolvent is not entitled to enter into contracts after sequestration.

(b) The insolvent may, with the written consent of the trustee enter into a contract by which he or she disposes of property of his or her estate.

(c) The insolvent may enter into an engagement contract after sequestration.

(d) The insolvent may enter into a contract if it does not affect his estate negatively.

Question 1.6

Select the **correct** statement:

Which of the following statements accurately reflects the treatment of municipal debts related to immovable property under the Insolvency Act and the Local Government: Municipal Systems Act 2000?

- (a) Municipal debts incurred within three years immediately preceding the date of sequestration are considered as part of the costs of realising the property.
- (b) Municipalities have the authority to embargo the transfer of property until all outstanding municipal debts, irrespective of the two-year period, are fully settled.
- (c) Section 118(2) of the Local Government: Municipal Systems Act takes precedence over section 89(1) of the Insolvency Act, determining the applicable period for calculating municipal debts.
- (d) The Court in *City of Johannesburg v Kaplan NO* clarified that all service charges, basic fees, and refuse removal fees are considered taxes under section 89(5) of the Insolvency Act. ✓

Question 1.7

Select the **correct** statement:

- (a) The trustee's remuneration (fee) is determined by a tariff which is laid down by statute, but which must thereafter be taxed by the Master or the Registrar.
- (b) The trustee's remuneration (fee) is determined by a tariff which is laid down by statute, but which must thereafter be taxed by the Registrar.
- (c) The trustee's remuneration (fee) is determined by a tariff which is laid down by statute, but which must thereafter be taxed by the Master. ✓
- (d) The trustee's remuneration (fee) is determined by a tariff which is laid down by statute, but which must thereafter be taxed by the Master or the Court.

Question 1.8

Select the **correct** statement:

Section 44(1) of the Insolvency Act deals with the time limit for proof of claims. Which case decided that the time limit of three months after the closing of the second meeting, except with the leave of the court or the Master, also applies to liquidations?

- (a) *Stone & Stewart v Master of the Supreme Court*;
- (b) *Mayo v De Monthlehu*; ✓
- (c) *Wishart v BHP Billiton Energy Coal South Africa Limited*;
- (d) None of the above.

Question 1.9

Indicate whether the following statement is **true** or **false**:

Confidentiality is a defence that can be raised by a witness who has been subpoenaed to an enquiry.

- (a) True
- (b) False ✓

Question 1.10

Select the **correct** statement:

The property of the insolvent's spouse, married out of community of property to the insolvent:

- (a) Vests in the Master and thereafter in the trustee after his appointment as such. ✓
- (b) Does not vest in the Master or the trustee of the insolvent.
- (c) Vests in the division of the High Court that granted the sequestration order.
- (d) Only vests in the trustee when the High Court on application by a creditor of the estate grants an order for the vesting of the property.

Question 1.11

Select the **correct** statement:

In terms of section 346 of the Companies Act 1973, an application for the winding-up of an insolvent company by court order may be made by:

- (a) The company itself.
- (b) One or more of its creditors (including contingent or prospective creditors).

- (c) A shareholder.
- (d) Jointly by any or all the parties in (a), (b) or (c). ✓

Question 1.12

Select the **correct** statement relating to special meetings of creditors:

- (a) The primary purpose of a special meeting is to allow creditors to vote on important matters related to the insolvent estate. The trustee must convene a special meeting when requested by the insolvent, regardless of expenses.
- (b) Special meetings are convened for creditors to prove their claims, and the trustee must convene one if requested by an interested person who tenders payment of all expenses related to the meeting. ✓
- (c) The main objective of a special meeting is to finalise the distribution of assets to creditors and must be convened by the trustee after the second meeting.
- (d) A special meeting cannot be convened for the purpose of interrogating an insolvent as the primary purpose of a special meeting is to prove claims.

Question 1.13

Indicate whether the following statement is **true** or **false**:

The perfecting of a general notarial bond can go as far as the bondholder being allowed to take over the debtor's business as a going concern.

- (a) True ✓
- (b) False

Question 1.14

Select the **correct** statement:

Which of the following statement is correct in relation to a compromise between a company and its creditors in terms of section 155 of the Companies Act 71 of 2008?

- (a) A proposal for a compromise in terms of section 155 is adopted by the creditors of the company, or a class of creditors, if it is supported by a majority in number representing at least 75% in value of the creditors or class present and voting in person or by proxy.
- (b) Section 155 does not apply where a company is under business rescue proceedings.

(c) A liquidator where a company is being wound up may propose an arrangement or a compromise of the company's financial obligations.

(d) Paragraphs (a) and (c) are correct.

(e) Paragraphs (a), (b), (c) and (d) are correct.

Question 1.15

Select the **correct** statement:

Under what circumstances can a mortgage bondholder insist on selling immovable property free from a lease entered into prior to sequestration?

(a) The bondholder, as a secured creditor, can always insist on selling the property free from a lease, regardless of when the lease was entered into.

(b) If the lease was entered into after the registration of a mortgage bond, the bondholder may insist on selling the property free from the lease, provided the sale subject to the lease did not realise enough to pay the bondholder's secured claim.

√

(c) The property must always be sold subject to the lease, regardless of when the lease was entered into.

(d) If the property is sold without reference to a lease concluded after the registration of a mortgage bond, the sale is valid even if it did not realise enough to pay the mortgage bond in full.

Question 1.16

Select the **correct** statement:

There are three steps that must be taken to determine whether a specific provision of the Insolvency Act 1936 applies to the liquidation of a company. These steps include:

(a) Whether the provision is capable of being applied in a winding-up.

(b) Whether the matter is specifically provided for by the Companies Act.

(c) Whether the provision applies to the type of winding-up.

(d) Only paragraphs (a) and (c) are correct.

(e) Paragraphs (a), (b) and (c) are correct. √

Question 1.17

Select the **correct** statement relating to rehabilitation:

- (a) Rehabilitation is also available to partnerships, companies and other legal entities, allowing them to apply for a fresh start.
- (b) Automatic rehabilitation occurs after a period of 10 years from the date of provisional sequestration, unless ordered otherwise by the court upon application by an interested person.
- (c) Since the insolvency of an individual affects a person's status, any Court may grant a rehabilitation order.
- (d) When an insolvent applies to the court for rehabilitation, the insolvent is not expected to repay a contribution that creditors had to pay, as rehabilitation results in the release of an insolvent person from their pre-sequestration debts and affords the insolvent the opportunity to make a so-called "fresh start".

Question 1.18

Indicate whether the following statement is **true** or **false**:

There is no provision in the Companies Act 1973 determining that the liquidator's report, or resolutions that the liquidator wishes to adopt, must be posted to creditors. The provisions of section 81(1)*bis* of the Insolvency Act do not apply to companies.

- (a) True ✓
- (b) False

Question 1.19

Select the **incorrect** statement relating to a partnership:

- (a) A partnership is a legal entity, at common law, having an existence separate from the individual partners. ✓
- (b) The "assets" of the partnership are indistinguishable from the assets of the partners.
- (c) The "partnership debts" are in law the debts *in solidum* (jointly and severally) of all partners.
- (d) A partnership creditor can sue the partners, if necessary, the one after the other, for the partnership debt.

Question 1.20

Select the **correct** statement:

Which of the following statements describes the position of employees during business rescue proceedings?

- (a) During a company's business rescue proceedings, employees of the company immediately before the beginning of those proceedings continue to be so employed on the same terms and conditions, except to the extent that changes occur in the ordinary course of attrition, or the employees and the company agree on different terms and conditions of employment, in accordance with applicable labour laws. ✓
- (b) During a company's business rescue proceedings, the business rescue practitioner can unilaterally vary the employment terms and conditions of the employees of the company immediately before the beginning of those proceedings, subject to the approval of the company's creditors at the first meeting of creditors.
- (c) During a company's business rescue proceedings, all employment contracts that existed immediately before the beginning of those proceedings are automatically suspended.
- (d) All of the above

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**** END OF QUESTION 1 ****

QUESTION 2 FOLLOWS ON NEXT PAGE / ...

PART 2 - SEQUESTRATION (40 MARKS)

QUESTION 2

Questions 2.1 - 2.9 are based on the set of facts provided below. Answer ALL the questions.

Mr and Mrs Solar were married to each other out community of property in 2012. They reside in a four-bedroom property in an upmarket country estate on the beautiful east coast in Ballito, KwaZulu-Natal. The immovable property is subject to a mortgage bond in favour of ABC Bank. The marital home is fully furnished and the Solar's acquired some beautiful luxury and antique furnishings during the course of their marriage. In the latter part of 2021 Mr Solar donates a valuable and timeless Victorian sofa and server to his wife which she proudly exhibits in the home. The remaining furniture and antiques have been paid for in cash, apart from the photocopier in the home office which is subject to a lease agreement concluded with Speedy Copiers (Pty) Ltd by Mr Solar.

Mr Solar also owns a small apartment in Florence, Italy where the family enjoy spending their annual holiday.

Mr Solar drives a 2022 BMW X5 which was purchased on instalment sale agreement and financed by FCM Vehicle Finance Ltd. Mrs Solar drives a 2016 Hyundai i20 which Mr Solar purchased from Mr Green in terms of an ordinary credit sale agreement. The agreement was concluded on 5 August 2022. Mr Solar paid a deposit in the sum of R20,000 and by agreement ownership in the vehicle had passed on delivery. The balance of R80,000 is due to be paid by way of monthly instalments of R10,000 each until the balance is paid, to date, Mr Solar has paid R40,000 in terms of the agreement.

On 5 December 2022 and after being pressured by Mr Hasty, an irate creditor who loaned Mr Solar money, Mr Solar delivers one of his valuable antique clocks to him to settle his debt in full.

On 5 January 2023 an application for the sequestration of the estate of Mr Solar is filed in the KwaZulu-Natal High Court Division, Durban at the instance of Axit Finance in respect of an unpaid personal loan. Mr Solar's estate is provisionally sequestrated on 15 January 2023 and the order is made final on 20 February 2023.

On the date of sequestration Mr Solar is a director of an accounting firm, Sum-It-Up (Pty) Ltd and earns a generous salary of R120,000 per month. Mrs Solar works at the local high school as a teacher and earns R25,000 per month.

Two months after the final order of sequestration is granted, Mr Solar inherits R500,000 from his father, which inheritance he accepts on 1 May 2023. Mrs Solar decides to resign from her position at the local school and receives a pension pay out of R600,000. Mr Solar has a life-insurance policy in terms of which he is the life insured. The surrender value of the

policy is R800,000 and the policy has been in force from 1 February 2018. In December 2022 a job opportunity as a sales representative, earning an average income and just sufficient for Mr Solar to support his family, becomes available to Mr Solar and the Solar family decide to relocate to Gauteng.

Ms Abel is appointed as the provisional trustee of Mr Solar's estate and the trustee's appointment is made final at the first meeting of creditors on 10 April 2023. The second meeting of creditors is held on 5 June 2023. Axit Finance fails to lodge its claim at either the first or second meeting and approaches Ms Abel on 6 September 2023 to prove its claim.

Question 2.1

On the date of the sequestration order of Mr Solar, the principle known as *concursum creditorum* will apply. Explain the concept of *concursum creditorum* and how this will affect the creditors of the estate. In your answer refer to relevant case law. (4)

In *Walker v Syfret*, the court explained the concept of *concursum creditorum*. Essentially, the sequestration order crystallises the insolvent's position and the hand of the law is laid upon the estate. At this point, the rights of the general body of creditors must be taken into consideration and their general interest as a group ranks above the interest of an individual creditor.

The realisation of and distribution of the insolvent's estate must be done in accordance with the order of preference as stipulated by the law of insolvency. Therefore, once sequestration has commenced, a single creditor cannot receive full payment of its claim at the expense of other creditor claims. 4

Question 2.1

Write a short paragraph and explain what possible remedy is available to Ms Abel to deal with the antique clock which Mr Solar delivered to Mr Hasty in full and final settlement of his claim. In your answer refer to the relevant section of the Insolvency Act that will apply and what requirements must be met. (7)

In terms of Section 29 of the Insolvency Act, a disposition by a debtor can be set aside as a voidable preference if it can be proved that said debtor favoured a particular creditor by settling a pre-existing debt in full.

Ms Abel, the trustee, will need to prove the following to have the disposition set aside as a voidable preference:

1. Disposition was made within 6 months of the sequestration date;
2. That the effect of the disposition was to prefer one creditor above the others; and

3. That immediately after making such disposition, the debtor's liabilities exceeded the value of his assets.

Requirements 1 and 2 are straightforward – the antique clock was delivered within 6 months of sequestration and it is clear that Mr Hasty was favoured above the remaining creditors.

In terms of the third requirement, it should be reasonably possible to show that immediately after the disposition, the value of Mr Solar's liabilities exceeded the value of his assets, in light of his financial situation.

Section 30(1) deals with undue preferences (1) – the trustee must prove (1) – (a) that there was a disposition of property (1) – (b) that was made any time before sequestration (1) – (c) at a time when the insolvent's liabilities exceeded his assets (1) – (d) that the disposition was made with the intention of preferring one of his creditors above another (1) – (e) the trustee must also prove the subjective intention of the debtor, which can be shown that the debtor was aware of the debtor's insolvent estate or contemplated sequestration but nevertheless made the disposition (1)

Question 2.2

Axit Finance, as the applicant creditor seeking a provisional order of sequestration against Mr Solar, must meet specific requirements outlined in section 10 of the Insolvency Act. Write a short paragraph setting out the requirements that must be met. (5)

As the applicant creditor, Axit Finance must, in terms of section 10 of the Insolvency Act, *prima facie* prove the following:

1. That they qualify as a creditor who may bring such application, (claim must be more than R100 in this case as it is only a single applicant creditor);
2. That the debtor is factually insolvent, or that the debtor has committed an act of insolvency; and
3. That there is reason to believe that the sequestration would be to the advantage of creditors. 5

Question 2.3

With regards to the inheritance that Mr Solar receives from his father after the sequestration order, explain whether the R500,000.00 inheritance will vest in the insolvent estate. In your answer refer to relevant case law. (3)

Two conditions need to be met for the inheritance to vest in the insolvent case. The first condition is that the right of inheritance must accrue before the rehabilitation of the insolvent estate. In this case, as Mr Solar has not yet been rehabilitated, this condition is met.

The second condition is that the insolvent needs to accept the inheritance. In *Wesse's NO v De Jager*, the Supreme Court of Appeal decided that before acceptance of an inheritance, the beneficiary has no rights to the inheritance and only a "competence".

this case, Mr Solar accepted the inheritance, and as such both conditions are met and the R500 000 inheritance will vest in the insolvent estate. ✓ **3**

Question 2.4

For the purpose of this question, assume that Mr and Mrs Solar are married **in community of property** and their joint estate was sequestrated. Explain whether the pension pay-out of R600,000 that Mrs Solar receives will vest in the joint insolvent estate. In your answer refer to the applicable section of the Insolvency Act that applies. **(2)**

In terms of section 23(7) of the Insolvency Act, the insolvent may for her own benefit recover any pension to which she may be entitled for services rendered, and therefore the pension pay-out received by Mrs Solar will not vest in the joint insolvent estate. **2**

Question 2.5

With reference to the motor vehicle driven by Mrs Solar, briefly explain whether ownership of the vehicle vests in the insolvent estate at the date of sequestration. Additionally, discuss whether Mr Green would have a claim against the estate in respect to the vehicle and, if so, specify the type of claim he would have. **(4)**

As Mr Green has entered into a credit sale ✓ of movable property, and with the transaction not being an instalment agreement in terms of the National Credit Act, section 84 of the Insolvency Act does not apply, and as such, the transaction is a normal credit sale ✓ in terms of the common law. ✓

In terms of a credit sale, ownership of the vehicle passed to Mr Solar (Mr Solar is the purchaser) upon delivery and therefore it belongs to the insolvent estate. ✓

Mr Green will only have a concurrent claim on the outstanding balance due to him. ✓ **4**

Question 2.6

Who must convene the first meeting of creditors and how is this meeting convened? **(2)**

The first meeting is convened by the Master upon receipt of the final order of sequestration. A notice of meeting is required to appear in the Government Gazette not less than 10 days before the date of the proposed meeting. **2**

Question 2.7

Ms Abel urgently needs to sell the movable assets of the insolvent estate, claiming that the sale cannot wait until she receives instructions from the creditors at the second meeting. What steps would Ms Abel need to take in order to sell the assets prior to the second meeting of creditors? Support your answer by referring to the necessary statutory provisions. **(4)**

Ms Abel may approach the Master ✓at any time before the second meeting of creditors✓ and request that he authorises the sale of the property. Ms Able, as provisional trustee, may not sell estate property until she has the authority of the Master to do so.

If the Master is approached, section 18(3) must be read with section 80bis✓ and if the Court is approached in terms of section 18(3) for the sale of property of the insolvent estate. "such sale shall furthermore be after such notices and subject to such conditions as the Master may direct." ✓ **3**

Permission from secured creditor

Question 2.8

Question 2.8.1

In relation to the foreign assets, indicate whether the immovable property in Italy automatically vests in the insolvent estate of Mr Solar and explain whether Ms Abel will be able to exercise control over the property. **(4)**

Answer:

The immovable property in Italy does not automatically vest ✓in the insolvent estate as in terms of section 2, ✓ "property" as defined, only includes property situated in the Republic. However, should Ms Able obtain recognition of her appointment as trustee from the relevant Italian court in terms of the relevant principles in Italy, ✓she will be able to gain control of the immovable property and then it will vest in the insolvent estate✓. **4**

Question 2.8.2

Would your answer to the above question be different if the property located in a foreign country is movable property? **(2)**

Yes, ✓as movable property of the insolvent that is located in a foreign country will, according to the common law, vest in the insolvent estate if the estate is sequestered by the court where the insolvent is domiciled. Crucially, it is not a requirement that the trustee obtain recognition of her appointment. ✓ **2**

Question 2.9

Question 2.9.1

Assuming that Mr Solar traded Sum-It-Up Accounting as a partnership, briefly explain how the partnership and the partners are treated in terms of the Insolvency Act when a provisional sequestration order is granted. **(2)**

In terms of the Insolvency Act, √the estates of the partnership and its partners are treated as separate entities, and as such, a partnership is treated as a separate entity with an estate which may be sequestrated as if it were a natural person. √ **2**

Question 2.9.2

What effect would Mr Solar's sequestration have on the partnership? (1)

The effect of Mr Solar's sequestration would be the dissolution of the partnership, however it would not cause the sequestration of the partnership estate. √ **1**

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**** END OF QUESTION 2 ****

QUESTION 3 FOLLOWS ON NEXT PAGE / ...

PART 3 - LIQUIDATION (40 MARKS)

QUESTION 3

Questions 3.1 - 3.10 are based on the set of facts provided below. Please answer ALL the questions.

RNH Plastics (Pty) Ltd (RNH) is a private company duly incorporated and registered under the applicable company laws of South Africa. RNH has been operating a profitable injection moulding operation for the past 13 years, manufacturing plastics chairs from a large industrial property in Willowton, Pietermaritzburg.

The Board of Directors consists of Mr Ronald, Mr Naseer and Ms Hlope. RNH occupies the industrial property under a lease agreement with The Willow Family Trust, which is set to expire in 2026.

RNH employs a significant number of staff members, including management, production, sales, maintenance, machine operators and administrative personnel. Most of RNH's employees are represented by MAWU (Moulding and Allied Workers Union), a registered trade union focusing on the interests of employees in the injection and moulding industry.

South Africa is currently facing a severe energy crisis, impacting RNH's manufacturing operations heavily. RNH relies on power to operate its large injection moulding machines, making generator usage economically unfeasible. As a result, RNH is struggling to meet customer demands and has faced contract terminations, further impacting their revenue. Cash shortfalls have hindered RNH's ability to repay creditors and suppliers, resulting in legal actions and judgments against the company, increasing the possibility of liquidation.

In December 2022, amidst the ongoing energy crisis, RNH urgently requires raw material to meet demand. They approach Rand First Bank for a loan, which is granted subject to them registering a general notarial bond over certain of the movable assets as security. The injection moulding plant is already subject to a special notarial bond. Additionally, RNH has a shipment of raw materials at the Durban harbour, but they need funds to pay customs and excise duty before it can be released.

RNH has recorded substantial losses in the 2021 and 2022 financial years, worsened by increasing repo rates and additional cash flow required for monthly repayments on vehicle and truck instalment sale agreements with SABA Bank.

Recognising the dire situation they are in, the Board decide to commence business rescue proceedings on 12 February 2023, and lodge the required documents with CIPC on 14 February 2023. The Board is not aware that an aggrieved creditor, who is owed a substantial sum of money for raw materials supplied, has already initiated a liquidation application against the company which was filed and served by the Sheriff of the High Court on an employee of the company on 11 February 2023. The employee unfortunately placed the documents in his desk drawer and failed to bring the application to the attention of management.

QUESTION 3.1

In the context of the liquidation of RNH, distinguish between commercial insolvency and factual insolvency and provide an example of each. In your answer state whether RNH is commercially or factually insolvent. **(max 5)**

Factual insolvency is when a company's liabilities exceed the value of its assets. ✓

Commercial insolvency pertains to a liquidity issue whereby the entity is unable to pay its debt obligations in the course of business. This entity may not be factually insolvent - it's possible that its assets exceed its liabilities. ✓

It appears that RNH may only be commercially insolvent, ✓ in that it is struggling to pay its debt obligations as they fall due. It is also unlikely that Rand First Bank would have made a loan to them if the company was factually insolvent. ✓ **4**

QUESTION 3.2

Under whose custody and control will the assets of RNH (the company) be once the provisional liquidation order is granted? **(1)**

Once the provisional liquidation order is granted, control of the company vests in the Master and then the liquidator. **1**

QUESTION 3.3

Briefly discuss the general effect the provisional order of liquidation of RNH will have on the employees' contracts of employment. **(3)**

Upon commencement of liquidation proceedings, contracts of employment are suspended. ✓ In other words, employees do not have to tender their services, ✓ however, their contracts can be terminated by the liquidator in terms of section 38 of the Insolvency Act. **2 45 days?**

QUESTION 3.4

Explain what effect the liquidation order of RNH will have on the lease agreement with The Willow Family Trust which will expire in 2026. In your answer discuss what statutory provisions will apply and discuss whether The Willow Family Trust will have any preference in respect of a claim against the liquidated estate for the arrear rental only. **(6)**

The general principle is that a lease is not automatically terminated by the sequestration of either the lessor or lessee. ✓

The liquidator may, subject to the consent of the Master, ✓at any time before a general meeting is ✓convened, terminate any lease by means of a written notice. If the liquidator terminates the lease, the lessor will have an unliquidated claim against the estate for damages for breach of contract.

Should the liquidator not terminate the lease, the lease will automatically be terminated three months after the appointment of the trustee unless the trustee notifies the lessor within those three months that they intend to continue with the lease. ✓

The lessor has a tacit hypothec over any movable property ✓that the lessee brought onto the property, with this hypothec securing the lessor's claim for arrear rental which was due before the sequestration date. Rental that became due after the the sequestration enjoys a preference as part of the sequestration costs. ✓

Therefore, The Willow Trust, as lessor will have a secured claim for any arrears rental that there may be. Should RNH occupy the premises after liquidation, the Willow Trust will have a preferential claim for any rent due over this period, with it forming part of the liquidation costs. Should RNH terminate the lease, the Willow Trust will have a concurrent claim for damages suffered due to the premature termination of the lease. **6**

QUESTION 3.5

Briefly discuss the overall effect that the liquidation order of RNH will have on civil proceedings that have commenced against the company prior to the provisional order being granted. **(2)**

In terms of section 20(1)(b) of the Insolvency Act, any civil proceedings that have commenced against the company are stayed until a trustee is appointed. **2**

QUESTION 3.6

Section 402 of the Companies Act 1973 lists the matters that a liquidator must report on at the second meeting of creditors. Discuss any six aspects that Mr Hue should include in his report to creditors. **(max 6)**

The trustee should include the following in his report to creditors:

1. The assets and liabilities of the company (itemised list of all assets and liabilities and their corresponding values – balance sheet); ✓
2. The causes of the failure of the company (the company has been struggling to meet customer demand essentially due to a manufacturing slowdown directly attributable to load shedding); ✓
3. Whether any of the directors or former directors should be held personally liable for any of the actions taken by the company (in this case there is no mention of anything indicating this to be the case); ✓
4. Whether there are any legal proceedings against the company (there is mention of legal actions and judgments against the company – these will need to be included in the report); ✓
5. Whether there is any reason to hold an enquiry into the failure of the company (if the company contravened the Insolvency Act, or committed any other offence); ✓ and
6. Whether or not the company complied with all accounting requirements (in this case there is no mention that the company had not adhered to good accounting practices). ✓ **6**

The trustee will also need to deal with the progress and prospects of the winding-up, and any matters requiring the further direction of the creditors.

QUESTION 3.7

MAWU ask Mr Hue to explain the statutory preferent right of the employees to claim for arrear salaries, and other amounts) owing to them. Write a short paragraph advising MAWU of the position. **(5)**

In terms of section 98A ✓an employee is entitled to certain statutory preferent claims in terms of remuneration owed to the employee. These preferent claims are subject to maximum values as determined by the Minister of Justice, and outlined as follows:

- Any outstanding salary and wages✓. set at a maximum of R12 000. ✓
- Any payment in respect of leave pay ✓which has accrued, set at a maximum of R4 000.
- Any payment in respect of any other form of paid absence, set at a maximum of R4 000. ✓
- Any severance benefit due to the employee, set at a maximum of R12 000. ✓

The outstanding salary and wages, and any other form of paid absence remuneration, is limited to the that accrued to the employee for the three months preceding sequestration. This effectively means that an employee will only be able to claim a maximum of three months salary, but capped at R12 000. No proof of this preferent claim is required. Any unpaid salary, leave pay, absence pay and/or severance benefit above the stipulated maximum will be a concurrent claim against the estate. **5**

QUESTION 3.8

In order for a bondholder of a special notarial bond to confer a right of preference to the proceeds of the movable property covered by such bond, the Security by Means of Movable Property Act sets out three basic requirements to be met for such preference to be recognised. List these requirements. **(3)**

In terms of the Security by Means of Movable Property Act, the three requirements that need to be met are as follows:

- the special notarial bond needs to be registered in terms of the Deeds Registries Act; ✓
- the special notarial bond will need to cover corporeal movable property; and ✓
- the property must be specified and described in a way that makes it readily recognisable. ✓ **3**

QUESTION 3.9

With regards to the raw material that is located at the Durban harbour, discuss the position of SARS in the hierarchy of creditors when enforcing a customs and excise lien over the assets under their control. **(4)**

In terms of section 114✓ of the Customs and Excise Act, SARS has a special security right allowing it to secure the payment of customs and excise duties. Whilst this security right is referred to as a "lien" in the Act, it operates more like a statutory pledge, ✓essentially allowing SARS to detain the imported property to which the duties relate. ✓Once SARS detains the property, by "sealing, marking, locking, fastening or otherwise securing or impounding it on the premises where it is found or by removing it to a place of security", SARS effectively becomes a secured creditor of the detained assets. This lien cannot vest over assets not owned by the debtor, which used to be possible. ✓ **4**

QUESTION 3.10

Explain whether the Board of Directors will succeed in placing RNH into business rescue. In your answer discuss the concept of "initiation" of liquidation proceedings. Make reference to case law in your answer. **(5)**

In terms of section 131(7) of the 2008 Companies Act, a court may place a company into business rescue at any time during the course of any liquidation proceedings. An affected person may approach the court with an application to commence business rescue proceedings after the initiation of liquidation proceedings, in which case the liquidation proceedings will be suspended.

Business rescue proceedings can commence via a company resolution (voluntary) or via court application by an affected person (compulsory). However, a company resolution cannot be passed once liquidation proceedings have commenced, ✓and therefore, in this case, business rescue may only commence via a court application (the business rescue proceedings initiated by RNH's board will be null and void). **1**

In this instance the Board will not succeed in placing the company in business rescue as liquidation proceedings have already been initiated (1). - Section 129 of the Company Act

1973 deals with resolution to begin business rescue proceedings - resolution contemplated in subsection (1) - may not be adopted if liquidation proceedings have been initiated by or against the company (1) - initiated deemed to be the filing and service of the application papers on the company - the resolution will be a nullity. (1) Tjeka Training Matters (Pty) Ltd v KPPM Construction (Pty) Ltd and Pan African Shopfitters (Pty) Ltd v Edcon Limited and others. (1)

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***** END OF ASSESSMENT *****

TOTAL MARKS: [100]