

SMALLER PRACTICE FEATURE

The Rapidly Changing Landscape for South African Practitioners



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Two significant new pieces of legislation and a possible change in policy relating to the manner in which appointments of insolvency practitioners (“IP’s) are being made, will have a dramatic impact on the manner and structure of practice of smaller practitioners in South Africa.

The New Companies Act 71 of 2008 (“the Act”) and the Consumer Protection Act 68 of 2008 (“CPA”) both come into effect on 1st April 2011.

Business Rescue Act

Chapter 6 of the Act provides for a new business rescue regime, in terms of which a company may appoint a “Business Rescue Practitioner” (“BRP”). In a manner akin to Chapter 11 in the USA, a company may now adopt a resolution to initiate business rescue proceedings. The regulations to the Act allows for an IP, with suitable experience, to be appointed as a BRP if he/she belongs to a legal or accounting body, subject to regulation, or is licensed by the regulatory body of BRPs about to be formed.

IPs may see this as an opportunity to become involved in business rescue. Remuneration of BRPs will be determined on a time based system which will enable IPs to restructure their practices and become BRPs.

However, experience teaches that most South African small companies are liquidated because of financial failure and that no business rescue regime would have saved them. The aim with the Act was to, inter alia, stem the flow of liquidations but it is unlikely that it will decline as a result of the Act. Business failures will always be with us.

The Act defines a company as “financially distressed” when it is reasonably unlikely that the company will be able to pay its debts as they fall due and payable within the immediately ensuing six months, or if it appears to be reasonably likely that the company will become insolvent within the

immediately ensuing six months.

Where the board of a company has reasonable grounds to believe that the company is financially distressed, but fails to adopt a business rescue resolution, the board must in terms of the Act deliver a written notice to the company’s creditors stating the reasons for not adopting such a resolution.

Will there be a radical increase in the implementation of business rescues? By virtue of the suicidal effect of such notice, financially distressed companies are unlikely to send such a notice under distressed circumstances and will trade for as long as possible in the hope that conditions may improve. By the time they realise that they are on the brink of failure, most small to medium companies are so cash strapped that they can hardly meet their normal day to day financial commitments let alone the charges for the services of a BRP.

The BRPs remuneration will be time based as provided for in the draft regulations. In respect of small to medium companies, this could mean that, conservatively assessed, an amount of some R60,000 (£5,500) per week would have to be paid to the BRP working full time. This will in most cases be out of the reach of medium to small companies which are invariably virtually penniless at that stage.

Insofar as IPs may perceive that the new business rescue regime may lead to a major inflow of lucrative work, they should remind themselves that this legislation came into force on April’s fool day. That could be a very appropriate day for them to reconsider their position, at least if they believe that they will, from that moment onwards, have a new lease on professional life.

Consumer Protection

The CPA is social welfare legislation implemented with a view to curb the over indebtedness of consumers. It also aims to balance the interests of consumers and suppliers of goods and services, correcting an imbalance which is a consequence of South Africa’s apartheid past.

The CPA will impact on insolvency practice in areas such as proof of claims based on warranties, claims for defective products and the sale of assets via auctions.

IPs appointed in cases where goods are supplied and who elect to continue trading should be aware that as a supplier of goods they may under certain circumstances be bound by the CPA to (at the consumer’s election) repair, replace or refund the purchase consideration of goods sold.

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Section 61 of the CPA also changes the common law position in that the producer, importer, distributor and retailer of goods are jointly and severally liable for defective goods, irrespective of negligence on the part of the supplier. Although certain defences are available to a supplier of goods, an IP who ventures to trade the business of an insolvent company may well incur obligations which had never been contemplated or intended.

The CPA contains important provisions which have an impact on public auctions. For example, unless notice is given to the contrary, the owner or auctioneer of property is not allowed to bid or employ anyone to bid on their behalf. The draft regulations also provide for the mandatory advertising of auctions to ensure that the general public has had a reasonable opportunity to become aware of the auction, the goods on sale, and the rules governing the sale.

The CPA also prohibits the practice of fixing a minimum price without the seller's consent, to deviate from the advertised sequence of goods. There are also requirements to keep a Bidder's record. IPs should take notice of these new provisions which will certainly impact on a scenario where the auction route is considered for purposes of realising assets.

Creditor Rights and Possible Regulation

Like in many other jurisdictions, creditors have the final say in the destiny of the affairs of an insolvent entity or individual, by virtue of their power to vote for the appointment of an IP of its/their choice. Our Insolvency Act provides that the Master of the High Court ("the Master") **may** provisionally appoint an IP upon the granting of the Order of Court sequestrating an individual's estate or placing a company in liquidation. However, a final appointment of the IP is only made at the first statutory meeting of creditors once creditors with voting powers exercised their votes in favour of an IP.

For the past few decades it has become standard practice for the Master to make a provisional appointment based on "requisitions" lodged by creditors long before the first statutory meeting of creditors. A requisition is a one page document in terms of which a creditor states the value of its claim and its intent to vote at the first meeting for the appointment of a particular provisional IP of its choice. Based on the wishes of creditors expressed in the requisitions the Master would make a provisional appointment/s which enabled such provisional appointees to take early control of the affairs of the insolvent estate of the liquidated company as opposed to having to wait until the statutory first meeting of creditors.

The Department of Justice called a meeting in December 2010 with a view to discussing regulation and other issues of concern relating to insolvency practice in South Africa and invited delegates from the ranks of IPs.

During this meeting it was proposed by some delegates that the so-called "requisition system" be abolished as they perceived it to be discriminatory in that black practitioners were not being considered by major creditors and banks for nomination as IPs. They based their views on the strict provisions of the Insolvency Act in terms of which the Master "may" appoint a provisional IP. The IP's present at the meeting however resolved that the Master's panel of IP's should be "cleaned up" first and that the "criteria" and qualifications to be placed in the Master's panel of IP's would be determined. This is a major step towards regulation of the profession.

Quite ironically, Germany would appear to be going through a turmoil of exactly the opposite nature at present. It is understood that creditors are lobbying for a change in the laws in Germany to the effect that appointments IPs be made based on the wishes of creditors, as opposed to the Courts appointing the IPs on a rota basis as at present.

In jurisdictions where creditors have no say and where appointments are being made by the Court or the authorities, IP's are regulated or licensed, unlike the present South African position. The rest of 2011 may therefore become a watershed period for IPs in South Africa. 🌐