

REALISATION OF SECURITIES

It would appear that, owing to malpractices which have been knowingly been permitted by certain Insolvency Practitioners over many years, a general perception developed amongst certain secured creditors, especially financial institutions who finance movable assets in the nature of motor vehicles etc., that they may deal with "their" assets in whichever way they deem fit. Under these circumstances they invariably instruct an auctioneer to take possession of what they "their" assets. Most insolvency practitioners go along with this as they are reluctant to jeopardize the relationship between themselves and the financial institution.

The general position at common law is that a creditor holding movable property as security may not realize such property but must deliver it to the trustee or liquidator. Authority for this is to be found in the *De Hart NO v Virginia Land and Estate Company Limited and Another 1954 (4) SA 501 (O)* at page 505. See also *Millman NO v Twiggs and Another 1995 (3) SA 674 (A)* "When a right is ceded with the avowed object of securing a debt the cession is regarded as a pledge of the right in question: dominium of the right remains vested with the cedent and vests upon his insolvency in his trustee, **who is under the common law entitled to administer it 'in the interests of all the creditors, with due regard to the special position of the pledge'**"

Section 83 of the Insolvency Act deals with the realization of securities for claims and Section 83 (1) provides that a creditor of an insolvent estate who holds as security for his claim any **movable property** shall, before the second meeting of the creditors of that estate, give notice thereof in writing to the Master, and to the trustee, if one has been appointed.

It would appear from the wording of this sub-section that the legislature intended it to be applicable to movable assets only as the meaning of "property", in terms of section 2 of the Insolvency Act is movable property or immovable property, wherever situated in the Republic of South Africa whereas Section 83 (1) specifically refers to movable property.

Section 83 applies to liquidated companies and close corporations by virtue of section 339 of the Companies Act 61 of 1973 (*Bowman v De Souza Roldao 1988 4 SA 326 (T)*; *Venter v Avfin (Pty) Ltd 1996 1 SA 826 (A)*.)

I would further appear that is peremptory for a secured creditor who holds a movable asset as security to give written notice thereof of the trustee and the Master. This is also provided for in Section 83 (1). ("the section 83 (1) notice")

Section 83 (3) states that the trustee must be afforded the opportunity to exercise an election to "take over" the movable

property, either at a value agreed upon then or at the full amount of the creditor's claim. The effect of this is that the trustee must effectively purchase the property from the creditor at a consideration equal to the value of the creditor's claim. (The reference to "trustee" in the context of section 83 (1) and (3) is a provisional trustee- **Meskin Insolvency Law - 12.4.2**)

The effect of which is then to settle the creditor's claim. The asset then becomes an estate asset to be realised and the proceeds of which will form part of the free residue.

The trustee's election in this regard must be made within seven days from the latest of:

- the receipt of the Section 83(1) notice; or
- from the date upon the trustee's provisional certificate of appointment in terms of section 18 (1) or
- from the date that his final certificate of appointment in terms of section 56 (2) reaches him.

If the trustee or liquidator does not take over the property the creditor may:-

After the expiration of the abovementioned period of 7 (seven) days; but

Before the second meeting of creditors, realise the property by public auction on condition that the trustee or liquidator be afforded a reasonable opportunity to inspect the property and after having given notice of the time and place of the sale. – **Section 83 (8) (d)**.

As soon the trustee has directed the creditor to give notice thereof, the trustee must give written notice of the time and place of the sale to all other creditors: - **Section 83(9)**.

It should be noted that a secured creditor may only sell the property by public auction. Once sold the nett proceeds must be paid to the trustee. –**Section 83 (10)**.

Section 83 (5) provides for the creditor to, as soon as possible after he has realized such property, prove his claim secured by the asset so realised the creditors shall attach to the affidavit submitted in proof of his claim a statement of the proceeds of the realization and of the facts on which he relies for his security.

In **STANDARD BANK OF SOUTH AFRICA LTD v TOWNSEND AND OTHERS 1997 (3) SA 41 (W)** it was held that the effect of s 83(10) was that the realisation by a creditor of its security was not for his own immediate benefit but for that of the estate. The proceeds belonged

to the estate and had to be delivered to the liquidator in that instance.

The creditor is obliged to realise the property before the second meeting of creditors and if he has not done so, the creditor is obliged, as soon as possible after the meeting, to deliver the property to the trustee/liquidator. – **Section 83 (6).**

If the creditor has not delivered the property to the trustee within a period of 3 (three) days as from the commencement of the meeting, the trustee or liquidator may demand delivery of the asset from the creditor.

Should this creditor then fail to comply with the demand from the trustee or the liquidator the Master of the High Court shall, at the request of the trustee or liquidator and after notice to the creditor, direct the Sheriff within whose area of jurisdiction the property is situated to attach the property and deliver it to the trustee or liquidator.

Let's see what happened in **VENTER NO v AVFIN (PTY) LTD 1996 (1) SA 826 (A)**

THE FACTS:

Townsend Plant Hire CC had entered into various instalment sale agreements with Avfin in terms of which it bought earthmoving equipment.

In terms of each agreement, ownership vested in the Avfin pending payment of the full purchase price. After the equipment had been delivered, Townsend was provisionally liquidated.

Venter was appointed liquidator of Townsend. At the first meeting of creditors, it was agreed that creditors who had concluded instalment sale agreements with Townsend would repossess the subject matter of each agreement and hold such property as security.

Avfin took possession of the equipment it had sold to Townsend but did not notify the Master or the Appellant (as required by section 83(1)) that it held the equipment as security.

The equipment was not realised before the second meeting of creditors as provided for in section 83(6).

Venter demanded the delivery of the equipment to him in terms of section 83(6) but Avfin ignored the demand and submitted a claim for the amount owing to it in terms of the instalment sale agreements.

Avfin eventually realised the equipment but did not follow the procedure set out in subsections 83(8) and (9).

The proceeds of the sale of the equipment were not paid to Venter.

Venter then lodged proceedings in terms of section 83(10) which provided that where a creditor had realised his security "as hereinbefore provided", he had to pay the proceeds of the sale to the trustee or the Master.

The court a quo held that the phrase “as hereinbefore provided” meant that the relief in section 83(10) was only available where the creditor had followed the procedure set out in subsections 83(8) and (9).

As the Avfin had failed to comply with this procedure, Venter could only use the common law to vindicate the property from the possessor or recover the value thereof from Avfin.

The application in terms of section 83(10) was therefore dismissed and Venter appealed against the decision.

On Appeal:

The Court considered the meaning of the phrase “as hereinbefore provided” and held that, in subsection 83(10), the legislature was dealing primarily with what was to be done where a creditor had realised his security.

Had the legislature intended the meaning attributed to the phrase by the court a quo, one would have expected an express provision dealing with the consequences of non-compliance by the creditor with the specified procedure and not merely a general reference to earlier provisions.

The court a quo’s interpretation was also not consistent with the broader context of the Insolvency Act and the common law.

Accordingly, the Court held that the reference to preceding provisions in the relevant phrase was no more than a general reference to the realisation of securities as contemplated in the earlier subsections of section 83 and compliance with those subsections was not a precondition to the obligation of the creditor to pay over the proceeds of his security to the trustee.

The Court then considered Avfin’s defence that section 84(1) (and thus section 83) did not apply because some of the equipment was not in the possession of Venter and that, consequently, ownership did not pass to Venter. This argument was in accordance with the decision in *UDC Bank Ltd v Seacat Leasing and Finance Co (Pty) Ltd and Another* 1979 (4) SA 682 (T).

The Court rejected the reasoning in that case and preferred to adopt the approach used in *Hubert Davies Water Engineering (Pty) Ltd v The Body Corporate of “The Village” and Others* 1981 (3) SA 97 (D) where it was held that although possession was assumed for the purposes of section 84(1), a trustee who did not have possession of assets of the estate had to obtain such possession when faced with a demand from a creditor. This defence accordingly failed.

The Court rejected Avfin’s argument that section 83(10) created a reciprocal obligation on the part of the trustee, who received the proceeds of realised security from a creditor, to pay the creditor his preferent claim out of such proceeds.

The Court held that section 83(10) imposed an obligation upon the creditor to pay the proceeds to the trustee as soon as the security was realised; the receipt of payment out of the proceeds arose thereafter and only if certain requirements were met.

The appeal accordingly succeeded with costs.

It should be noted that, only after the claim of the creditor was proved and admitted and the trustee or liquidator is satisfied that the claim was in fact secured by the property so realised, shall the creditor be entitled to payment.

The payment that the creditor is entitled to, is the abovementioned nett realisation less the costs of maintaining, concerning and realising the property which includes:

- the trustee's/liquidator's remuneration),
- a proportionate share of the costs incurred by the trustee/liquidator in giving security for his proper administration of the estate and
- a proportionate share of the Master's fees.

Insolvency Practitioners are often requested for a so called advance or interim dividend. Let's examine the legality thereof:

Lets look at **GRUFIN FINANCE CO (PTY) LTD v COHEN AND OTHERS NNO 1991 (2) SA 345 (W)** - Note that Meskin doubts the correctness of this decision.- 22.1 below

THE FACTS:

- Grufin provided financing services to a company which was subsequently placed in liquidation ('the company'). It conducted business as factor.
- When the factoring agreement was entered into Grufin took cession of the book debts of the company.
- Prior to the company being placed in liquidation Grufin also caused a general notarial covering bond to be executed in its favour.
- When it appeared that the company was unable to meet its commitments Grufin obtained an order perfecting its security under the bond and took possession of the business and the movable assets of the company. Thereafter the company was placed in liquidation.
- The liquidators of the company, considered Grufin a secured creditor and advised creditors that Grufin intended to realise its security which it had taken control over in terms of the order.
- The assets were disposed of at a sale by public auction and at the second meeting of creditors Grufin proved its claim in an amount of R3,6 million. The claim was duly admitted and proved in terms of s 44 the Insolvency Act.
- On the same day Grufin handed over the proceeds of the sale to the liquidators and demanded payment of the amount of R800 000,00, being the balance after deduction of the liquidator's and the Master's fees from the proceeds.
- The liquidators refused to pay over the amount.
- Grufin contended that as it had properly complied with the provisions of section 83(10) and it was entitled to payment of the amount claimed and sought an order compelling the liquidators to pay over the amount to them.

- The liquidators admitted that Grufin was a secured creditor in terms of the cession of book debts but denied that it was a secured creditor in terms of the notarial bond.
- The liquidators contended furthermore that they had not had the opportunity of inspecting and perusing the claim prior to the meeting and although they were unable to dispute the claim they believed that there may well be reasons to dispute the claim, or to dispute that part of that claim not secured by the property in question.
- In addition they questioned the true nature of the factoring agreement and to this end experts had been employed and they said that an enquiry in terms of ss 417 and 418 of the Companies Act 61 of 1973 would be resumed.

The Court held that:

- Section 83(10) provided an exception to the rule that a creditor in the ordinary course of events, even though a preferent creditor, had no right to be paid until the account had been confirmed.
- In enacting s 83(10) the Legislature intended it to provide a speedy and relatively inexpensive procedure to resolve matters of an interim nature which did not require proof of a debt on a balance of probabilities.
- the liquidators had to satisfy themselves of the validity of the security or to dispute it: they were not obliged to finally decide the issue one way or another.
- the Court similarly was not called upon to decide finally the validity of the preference and the security relied upon.
- in considering the order to be made the Court had to take into consideration the harm which an applicant or a respondent might suffer and the balance of convenience.
- The application was granted and an order made that the liquidators pay the amount of R800 000 to the applicant subject to provision of a bank guarantee for the repayment of the amount in the event of the applicant's claim being reduced or disallowed by the Master in terms of section 45.

Meskin submits that the Court proceeded on the basis that its power under section 83(10) could be invoked immediately after payment of the proceeds of the realisation of the security to the trustee (or liquidator) and that on the language of s 83(10), the procedure of an application to the Court is intended to be strictly alternatively available to that of objection to the account, which indicates that the former procedure is not to be available prior to the lodgement of the account.

Once the statutory second meeting has been held and the resolutions have been adopted by creditors, the trustee's power to sell property of the estate includes the power to "abandon" immovable or movable property held in security to the creditor concerned in settlement of his claim which is, effectively, to sell the property to the creditor for a price equal to the amount of his claim, or to such other amount as may be agreed, payable by way of set-off.

Such an abandonment effectively renders the provisions of the Insolvency Act which would otherwise regulate the realization of the security inoperative. *Rand Metal Bed Manufacturers (Pty) Ltd v Botha* 1937 WLD 49 at 52; but cf *United Building Society Ltd and Another NO v Du Plessis* 1990 (3) SA 75 (W) dealt with the argument that the abandonment fell foul of the provisions of **the Alienation of Land Act 68 of 1981**. **The Court held that** the agreement was not a sale or an exchange or a donation. It was a payment in kind or an agreement in the administrative process of winding up the insolvent estate and the provisions of the **Alienation of Land Act** were accordingly not applicable thereto and there was no reason why the agreement could not be verbal.

In conclusion, Insolvency Practitioners, who take their professional duty seriously, should “*unite*” in engaging with financial institutions in rooting out all practices which are not in compliance with provisions of Section 83.
