DLA CLIFFE DEKKER HOFMEYR

DISPUTE RESOLUTION

MATTERS

JUNE 2014

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INTEREST ON UNLIQUIDATED DEBTS

Interest often has a material effect on the amount owed by a debtor. This is also true in the case of unliquidated debts, such as damages of which the amount is only ascertainable after an investigation.

In a claim for an unliquidated debt, a debtor was traditionally not held liable for interest in the absence of an agreement as to quantum or until such time as the amount had finally been assessed by a court or arbitrator.

In 1997 the legislature stepped in by means of an amendment to the Prescribed Rate of Interest Act, No 55 of 1975 (Act), when it inserted s2A into the Act. Section 2A provides for interest on unliquidated debts.

Such interest shall run from the date on which payment of the debt is claimed by service on the debtor of a demand or summons (or, in the case of arbitration proceedings, the date on which the creditor takes steps to commence the proceedings), whichever date is the earlier.

'Demand' means a written demand, setting out the creditor's claim in such a manner as to enable the debtor reasonably to assess the quantum thereof.

Interest shall be calculated at the rate prescribed by the Minister of Justice by notice in the Government Gazette as at the time when such interest begins to run (ie the date of service of a demand or summons or the date of commencement of arbitration proceedings, whichever date is the earlier). Currently the prescribed rate is 15.5% per annum. There are, however, indications that this rate will shortly be amended by the Minister.

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Interest on that part of a debt which consists of the present value of a loss which will occur in the future, shall not commence to run until the date upon which the quantum of that part is determined by judgment, arbitration or agreement.

Notwithstanding the provisions of the Act, but subject to any other law or an agreement between the parties, a court of law, or an arbitrator or arbitration tribunal may however make such order as appears just in respect of the payment of interest on an unliquidated debt, the rate at which interest shall accrue and the date from which interest shall run.

Marius Potgieter

THE PROTECTION OF INVESTMENT BILL – A POSSIBLE DEATH KNELL FOR FOREIGN INVESTMENT

The Draft Promotion and Protection of Investment Bill, 2013 (Bill) will have foreign investors thinking twice before looking at South Africa as a favourable investment destination as it deprives them of the opportunity to independently refer a dispute to an international arbitration forum without the consent of the South African government.

Foreign investors favour international forums as they remove disputes from the host nation's political and legal systems and believe they offer the prospect of a neutral, and perhaps more favourable hearing, amongst other concerns.

As the Bill presently stands, foreign investors would only be able to directly refer disputes to mediation which would be facilitated by the Department of Trade and Industry (DTI) or arbitrations in accordance with the Arbitration Act, No 42 of 1965 (Arbitration Act) .

The current state of the law governing arbitrations in South Africa provides even less comfort to foreign investors. There is no distinction between domestic and international arbitration, and it is not based on the United Nations Commission on International Trade Law (UNCITRAL model law).

The Law Commission has in the past made extensive recommendations for its reform, but to date government has made no progress in revising the arbitration legislation.

Recently the DTI submitted that a draft Bill governing domestic and international arbitration is to be presented to Cabinet (New Arbitration Bill).

The DTI's director for International Trade and Investment, Mustaqeem de Gama, told BDlive that:

"*The bill will replace the current Arbitration Act which dates back to 1960. It will aim to expedite arbitration proceedings and ensure local and foreign investors have modern and efficient alternative dispute-resolution mechanisms.*"

Accordingly, the Arbitration Act will be updated and harmonised with international laws to provide investors with a firm dispute-resolution mechanism that is recognised internationally.

This would to a large degree ease the concerns of foreign investors who prefer international arbitrations as opposed to domestic dispute resolution forums to resolve disputes.

Conclusion

Although the Bill does not expressly prohibit investors from refering disputes to international arbitration, some commentators believe that this will sound the death knell for any prospect of direct foreign investment in South Africa. However, we can all be hopeful that if the Arbitration Bill is eventually assented to, and the internationally recognised UNICITRAL model law is incorporated, it will increase confidence in foreign investors and settle any doubts.

Rishaban Moodley

BUSINESS RESCUE AND ITS EFFECT ON SURETYSHIPS

Suretyships are accessory in nature and are normally provided to creditors as additional security for their claims against their debtors. If the principal obligation is discharged, released, compromised or invalid, there is a corresponding effect on the accessory obligation. Whilst creditors' claims enjoy specific statutory protection in some parts of the Companies Act, No 71 of 2008 (Companies Act), the business rescue chapter is silent on the aspect.

If a creditor consents or votes in favour of a business rescue plan (where its debtor is the entity under business rescue), the creditor may compromise or jeopardise its claim against a surety to such principal debtor.

The Companies Act does not contain specific provisions whereby creditors' rights as against sureties are safeguarded from any compromise of the principal debt in a business rescue situation. Creditors are cautioned to peruse and consider

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business rescue plans carefully and to build in safeguards to protect their claims against sureties where appropriate.

Effect of business rescue on sureties

In the decision of *Investec Bank Limited v A Bruyns 2012 (5) SA (WCC)*(Bruyns), Rogers AJ (as he then was) held in passing that:

"*a business rescue plan may provide for the company to be released in whole or in part from its debts [and that]... a surety for the company would not be liable to the creditor for more than so much of the claim as survives the implementation of the business rescue plan.*"

At the time judgment was handed down in that case no business rescue plan had been adopted or implemented. The court therefore left open the question of whether lenders could lose their rights against sureties in circumstances where there was a compromise of the principal debt in terms of a business rescue plan.

Subsequently, and in the case of *Absa Bank Limited v Du Toit and Others (7311/13) [2013] ZAWCHC 194 (13 December 2013)* the court was faced with a situation where a defendant surety was defending summary judgment proceedings and argued that the principal debt had been, or would be, discharged as envisaged in the business rescue plan adopted in respect of the principal debtor. Consequently his argument was that this discharge should afford him a sustainable defence in his capacity as surety. The matter did to some extent turn on the wording of the business rescue plan which provided for 'the full and final settlement' of the creditor's claims against the principal debtor. Mindful that the court was dealing with summary judgment proceedings where only prima facie evidence of a defence needs to be established, the court found that the surety might be able to rely on such defence and summary judgment was refused.

In the most recent decision of *Tuning Fork (Pty) Ltd T/A Balanced Audio v Greeff and Another (18136/13) [2014] ZAWCHC 78 (28 May 2014)* (Tuning Fork), Rogers J had to decide inter alia whether the adoption and implementation of a business rescue plan resulted in the discharge of a surety's obligation to a creditor, arising from the compromise of the principal debt owed by the company under business rescue to the said creditor.

Rogers J found briefly the following:

i. One cannot imply a term, in the business rescue provisions of the Companies Act, to the effect that creditors' rights against sureties are or are not unaffected by the adoption of business rescue plans. The Companies Act is silent on the matter.

ii. The general common-law principles of our law of suretyship must therefore be applied to determine what effect the provisions contained in any business rescue plan may have on sureties (if any).

iii. One of the general principles that applies is that once the principal debt is discharged by a compromise with or release of the principal debtor, then the surety is similarly released, unless the deed of suretyship provides otherwise.

iv. Furthermore, if a business rescue plan provides for the discharge of the principal debt by way of a release of the principal debtor, and the claim against the surety is not specifically preserved by such stipulations in the plan (as may legally be permissible or unless any other arrangement is made with the surety), the surety will be discharged.

The terms of the business rescue plan in the Tuning Fork case provided for the discharge of a principal debt and it was consequently held that because the business rescue plan did not specifically address the position of sureties, and absent the evidence of any other agreement, the defendant sureties were also deemed to be discharged from their accessory obligations. This case is obviously distinguishable from the Bruyns case, where no business rescue plan had yet been adopted or implemented and absent any compromise or settlement, the creditor was entitled to proceed against the surety.

As a result, the likelihood (depending on the terms of the suretyship) exists that creditors' rights as against sureties can be extinguished in circumstances where the principal debt is compromised and/or altered in a business rescue plan.

Precautionary measures

The above-mentioned decisions warrant a creditor approaching business rescue creditors meetings and the consideration of proposed business rescue plans

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with a substantial measure of caution. Creditors should, as a minimum, consider the following:

i. safeguarding themselves against the effect that the terms of a business rescue plan may have on their securities in the form of relevant suretyships by negotiating or insisting on appropriate terminology in the plan which reserves their rights against the sureties;

ii. where possible, ensuring that sureties are party to the business rescue plan or agree to the creditors' rights against them being retained; and/or

iii. obtaining suitable alternative security to replace the suretyship and mitigate against the risk of such security being lost or diminished.

Guarantee – an alternative to suretyships

From a commercial perspective, as an alternative to seeking security in the form of suretyships containing traditional undertakings and contractual obligations, a creditor or lender could consider using guarantees. The obligations of a guarantor who provides a guarantee to a creditor are principal in nature and a guarantee can only be discharged by the fulfilment of the obligations that are so guaranteed unless otherwise agreed. In a business rescue scenario a creditor would therefore be entitled to proceed against a guarantor notwithstanding any discharge or compromise of a debt with that entity under business rescue.

Conclusion

Business rescue proceedings have, given their fairly new status and ongoing developments, created some uncertainly for creditors and lenders. Consequently creditors and lenders are encouraged to:

1 approach business rescue proceedings with suitable insight and caution; and

2 consider whether the terminology and obligations incorporated in their standard suretyship documents are sufficient to protect them in a scenario where the principal debtor has been placed under the umbrella protection of business rescue in terms of the Companies Act.

Grant Ford

REPUDIATION: A "THING WRIT IN WATER"?

Our law recognises that, where a party to a contract has repudiated that contract, the innocent party may elect to cancel or keep the contract alive. In the latter case, its own obligations continue to exist but it may refrain from performing them as long as the repudiating party maintains its position.

This principle was recently explored by the Supreme Court of Appeal in *Comwezi Security Services (Pty) Ltd & Another v Cape Empowerment Trust Ltd*. A settlement agreement was concluded between the first appellant, Comwezi Security Services (Pty) Ltd (Comwezi), and the respondent, Cape Empowerment Trust Ltd (CET), in terms of which CET was entitled to take up shares in Comwezi in settlement of monies due to it, after conducting a comprehensive due diligence investigation into Comwezi's affairs. Comwezi undertook to co-operate with CET and to make all relevant documentation available for inspection. CET was obliged to complete its investigation within a three-month period, failing which the settlement agreement would lapse. It was expressly recorded that CET would be entitled to extend that period prior to its lapsing.

Following Comwezi's failure to co-operate with the due diligence investigation and provide necessary documentation, CET successfully obtained a court order compelling Comwezi to do so, prior to the expiry of the three-month investigation period, as extended by CET from time to time. Such order was upheld on appeal. CET was, however, unable to execute the court order as Comwezi argued that the time period in which CET was to conduct its investigation had lapsed in the time it took to finalise the court application and appeal and accordingly the settlement agreement had lapsed.

In a further high court application, CET obtained an order declaring that the agreement remained valid. In an appeal against the said decision, Comwezi conceded its own repudiation by refusing to co-operate with the investigation and by insisting without justification that the agreement had lapsed. However, it contended that, having elected not to accept the repudiation, CET was obliged to continue extending the time period in order to keep the agreement alive, which it had failed to do. Can a party who repudiates a contract avail itself to a provision of the very contract it has repudiated?

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The Supreme Court of Appeal (SCA) held that, provided the innocent party is willing and able to perform its obligations, repudiation may excuse the innocent party from performing – or at least suspend its obligation to perform – until the repudiating party indicates its willingness to give effect to the contract.

Dismissing the appeal, the court found that it would be inequitable to allow Comwezi to rely on its own unaccepted repudiation to take advantage of CET's alleged failure to comply with the agreement's terms, where such failure was attributable to Comwezi's own repudiation. CET was clearly willing and able to comply with its obligations, but Comwezi's refusal to co-operate prevented it from completing its investigation within the requisite time period. It would have been futile for CET to continue to extend the time period in light of Comwezi's repudiatory conduct and CET's contractual obligation had been suspended as a result.

Liuba Stansfield

I KNOW I SIGNED THE CONTRACT, BUT IT'S NOT FAIR!

Legal professionals have been reminded that all law, including the law of contract, derives its power from the Constitution and is subject to constitutional control. When drafting cancellation clauses and other contractual provisions, due consideration must now be given to any disproportionate burden that a cancellation remedy may have on an opposing party.

Contracting parties could previously assume (in situations involving breach of contract) that an aggrieved party would be protected by the law of contract and entitled to invoke a cancellation clause and enforce the contracted/specified and/or common law remedies flowing therefrom. After all, the Constitutional Court itself held - "public policy requires that parties should comply with contractual obligations that have been freely and voluntarily undertaken."

However, the Constitutional Court recently came to the aid of a party who was more than seven years in arrears on instalments in terms of an instalment sale agreement for immovable property and had, in terms of a cancellation clause, forfeited instalments paid previously to the seller.

In *Botha & Another v Rich N.O. & Others [2014] ZACC 11*, Ms Botha (purchaser) on 19 November 2003, entered into an instalment sale agreement for immovable property owned by the respondent, JJW Hendriks Trust (seller). The purchaser owned and operated a laundry service on the immovable property in question.

The purchaser duly paid instalments from November 2003 until November 2007, where after she failed to pay instalments despite demand from the seller.

On 3 April 2008, the seller successfully prosecuted a claim in the magistrates' court for eviction and in terms of a cancellation clause, forfeiture of the instalments paid by the purchaser.

The purchaser sent a letter to the seller on 21 May 2008, demanding transfer of the property in terms of s27(1) of the Alienation of Land Act, No 68 of 1981 - which provides that a purchaser in an instalment sale agreement for immovable property may demand transfer of a property if they had paid at least half of the purchase price (provided a mortgage bond is registered in the name of the seller as security for the remainder of the purchase price). It is worth noting that the purchaser made no mention of her failure to pay instalments for over six months at that stage, nor did she tender payment thereof.

The purchaser obtained an interdict which suspended the eviction. However, on application to the Northern Cape High Court by the seller, the court held that the enforcement of the cancellation clause was not in bad faith, unreasonable, unfair, nor contrary to public policy. The Full Bench agreed and an application for leave to appeal to the Supreme Court of Appeal was dismissed with costs.

The purchaser argued before the Constitutional Court that the Northern Cape High Court and the Full Bench over emphasised the right to freedom of contract and had not sufficiently emphasised the injustice caused by the enforcement of the cancellation clause.

The Constitutional Court agreed and held that in instances where the rigid application of contractual principles would lead to an injustice - the contractual principle of good faith was flexible enough to ensure fairness between the parties.

The Constitutional Court held that where a contract has been lawfully cancelled, mutual obligations arise to restore respective performances. Relying on the forfeiture clause in the agreement, the seller made no tender of repayment of what it had received from the purchaser (despite this not being a contractual requirement). Enforcement

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of the forfeiture clause was found to be unfair, unconstitutional and a disproportionate penalty in circumstances where half of the purchase price had been paid by the purchaser (this was found despite the fact that the agreement had been lawfully cancelled by virtue of the purchaser's default).

The Constitutional Court upheld the appeal and ordered transfer of the property subject to the purchaser paying the outstanding rental owed to the seller.

The case is a sobering reminder to legal professionals to take cognisance of the fact that contracting parties will not necessarily be bound by contractual provisions to which they have agreed if those provisions are found to be unfair or, when enforced, place a disproportionate burden on one of them.

Kelvin Buchanan

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