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DISPUTE RESOLUTION ALERT

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If satisfied that it is reasonable and just to do so, a court may set aside a dissenting vote on a business rescue plan. In *Collard v Jatara Connect (Pty) Ltd & Others* [2017] ZAWCHC 45, the court did exactly that. Explaining his decision, Judge Dlodlo stated that there should be no reason to prefer a winding up application over a business rescue plan that will pay the employees of the company in full and result in a better return for creditors.

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BANKING: CONTINUING COVERING SECURITY: HOW GOOD IS YOUR COVER?

In the recent matter of Thomani And Another V Seboka No And Others 2017 (1) SA 51 (GP) the court had to determine the extent of sureties' liability and whether such liability was adequately secured.

Volatile economic circumstances forced banks and other financial institutions to become more reliant on security held by them, securing debts of customers with securities ranging from suretyships to covering mortgage bonds.

Sometimes a creditor thinks it holds sufficient security only to find out it was mistaken. In the recent matter of *Thomani And Another V Seboka No And Others* 2017 (1) SA 51 (GP) the court had to determine the extent of sureties' liability and whether such liability was adequately secured.

In this matter the applicants, Mr and Mrs Thomani, bound themselves as sureties and co-principal debtors in favour of a company called Abrina 1591 (Pty) Ltd (Abrina). Abrina was at all relevant times indebted to ABSA Bank Limited (ABSA), the fourth respondent. Abrina defaulted on its payment obligations to ABSA.

The applicants, unrelated to the suretyship signed in favour of ABSA, had a personal home loan with ABSA. As security for the repayment of this home loan, ABSA registered what is commonly known as a sectional mortgage bond hypothecating a unit (Bond) over the applicants' sectional title property.

Clause 4 of this bond provided as follows:

> Continuing covering bond
>
> The bond shall remain in force as continuing covering security for the capital amount, the interest thereon and the additional amount, notwithstanding any intermediate settlement, the bond shall be and remain of full force, virtue and effect as a continuing covering security and covering bond for each and every sum in which the mortgagor may now or hereafter become indebted to the bank from any cause whatsoever to the amount of the capital amount, interest thereon and the additional amount.

ABSA issued summons against the sureties pursuant to the suretyship and obtained default judgment. Relying on the bond, it attached the applicants' property and caused it to be sold in execution.

The applicants applied for rescission of the default judgment and for an order setting aside the sale of their property. The main defence raised by the applicants was that they stood surety for Abrina, whereas the bond on which ABSA relied was a normal housing bond over the applicants' sectional unit and not a surety bond.

The court had to determine whether the phrase "for each and every sum in which the mortgager may now or hereafter become indebted to the Bank from any cause whatsoever", could be construed to cover the applicants' liability to ABSA in terms of the suretyship.

The court considered case law and made a distinction between amounts payable under the bond and amounts secured by the bond, the first referred to as the obligatory part of the bond.

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This finding highlights the importance for all lenders, not limited to banks, to ensure that proper security is obtained for the liabilities of debtors.

The court found that it was clear from the wording of the clause in the bond, which was registered in respect of the applicants' home loan, that it related to the obligatory part of the bond — namely the capital amount, the interest thereon and the additional amount payable in respect of the home loan.

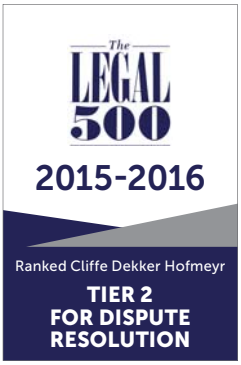
The phrase "any cause whatsoever", so the court found, was also limited to the amount of the capital amount, interest thereon and the additional amount, and could not be relied on by ABSA for payment of any of the applicants' obligations in terms of the suretyship.

The court in its judgment noted that clause 5 of the suretyship referred to the "obligations of the principal debtor" and that the security which ABSA obtained for the payment of Abrina's debt was the suretyship and not the bond.

The court held, after consideration, that the bond which was registered as security for the applicants' home loan, could not be used as security for a loan to Abrina, which was one of the reasons the court rescinded the judgment granted against the applicants and set aside the sale in execution.

This finding highlights the importance for all lenders, not limited to banks, to ensure that proper security is obtained for the liabilities of debtors, to avoid the proverbial unscrambling of the egg, when challenged.

Lucinde Rhoodie



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BUSINESS RESCUE, RESTRUCTURING AND INSOLVENCY

THE COURT'S POWER TO SET ASIDE THE DISSENTING VOTE OF A CREDITOR IN BUSINESS RESCUE PROCEEDINGS

Judge Dlodlo stated that there should be no reason to prefer a winding up application over a business rescue plan that will pay the employees of the company in full and result in a better return for creditors.

If satisfied that it is reasonable and just to do so, a court may set aside a dissenting vote on a business rescue plan. In *Collard v Jatara Connect (Pty) Ltd & Others* [2017] ZAWCHC 45, the court did exactly that. Explaining his decision, Judge Dlodlo stated that there should be no reason to prefer a winding up application over a business rescue plan that will pay the employees of the company in full and result in a better return for creditors. This judgment has subsequently been confirmed by the Supreme Court of Appeal (SCA) in *First Rand Bank Ltd v KJ Foods CC (in business rescue)* (734/2015) [2015] ZASCA 50 on 26 April 2017.

Judge Dlodlo was therefore called upon to decide whether or not Edcon's dissenting vote should be set aside.

In the *Collard* case, it was common cause that the business of the company in distress, Jatara Connect (Pty) Ltd (Jatara) was incapable of financial rescue. The fact that a company is incapable of rescue does not preclude it from business rescue because a legitimate, alternate objective of business rescue is to ensure a better dividend for creditors in instances where the company cannot be rescued. In this instance, Jatara had commenced arbitration proceedings against its major client, Edcon Limited (Edcon). If Jatara are successful in the arbitration, they would receive a substantial award for damages resulting from an alleged breach of contract by Edcon. This sum would be sufficient to ensure that each of Jatara's 140 staff would be paid in full and sufficient to provide a more favourable dividend to Jatara's remaining creditors. It is noteworthy that upon winding up, Edcon would not receive a dividend, whereas in terms of the business rescue plan, Edcon would likely receive a sizeable dividend.

Collard, a director and creditor of Jatara, brought an application to wind up Jatara. In response, the employees brought an application for an order placing Jatara into business rescue. The order was granted and the essence of the business rescue plan was to allow for the continuation of the arbitration proceedings.

Edcon, as a proven creditor holding 49.8% of the company's debt and consequently a substantial voting interest, voted against the business rescue plan while all other creditors, including SARS, voted in favour of the plan. The plan was therefore rejected. The employees of Jatara then brought an application to set aside Edcon's vote in terms of s153(7) of the Companies Act, No 71 of 2008 (Act). This section provides that a court may order that a vote on a business rescue plan be set aside if it is satisfied that it is reasonable and just to do so taking various factors into account. Judge Dlodlo was therefore called upon to decide whether or not Edcon's dissenting vote should be set aside.

The Judge cited with approval the judgment of *Koen & Another v Wedgewood Village Golf & Country Estate (Pty) Ltd & Others* 2012 (2) SA 378 (WCC) in which the court acknowledged the significant collateral damage, economic and social, brought about by the liquidation of companies, specifically, the

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The judge found that Edcon's vote was inappropriate and that it was reasonable and just to set it aside, which it duly did.

destruction of wealth and of livelihoods. The court stated that it is in the public interest that the incidence of such adverse socio-economic consequences should be avoided where reasonably possible.

Upon examination of the business rescue plan, the Judge noted that, pursuant to success in the arbitration proceedings, all of the concurrent creditors of the company, including Edcon, would receive a better dividend under the business rescue and, significantly, that the employees would be paid in full. The only inference the Judge could thus draw from Edcon's dissenting vote was that it did so with the sole intention of frustrating the arbitration proceedings against it.

Edcon's vote was found to be mala fide, and therefore it could not be considered appropriate. The judge found that Edcon's vote was inappropriate and that it was reasonable and just to set it aside, which it duly did. In the result, the business rescue plan was adopted at the intervention of the employees of Jatara with the assistance of the court.

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BBBEE STATUS: LEVEL THREE CONTRIBUTOR
Cliffe Dekker Hofmeyr is very pleased to have achieved a Level 3 BBBEE verification under the new BBBEE Codes of Good Practice. Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

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