



# DISPUTE RESOLUTION AND FINANCE & BANKING ALERT

25 AUGUST 2022



INCORPORATING  
KIETI LAW LLP, KENYA

## IN THIS ISSUE

The jury's still out on the nature of security cessions, but let's consider the effect on liquidation

In *Grobler v Oosthuizen* 2009 (5) SA 500 (SCA), the Supreme Court of Appeal (SCA) considered the nature of security cessions and found that there are two opposing theories in our law – the pledge theory and the outright cession theory. The court found it unnecessary to resolve these diverging theories and instead, found that the nature of a security cession is to be determined using the expressed intention of the parties.



FOR MORE  
INSIGHT INTO  
OUR EXPERTISE  
AND SERVICES

## The jury's still out on the nature of security cessions, but let's consider the effect on liquidation

In *Grobler v Oosthuizen 2009 (5) SA 500 (SCA)*, the Supreme Court of Appeal (SCA) considered the nature of security cessions and found that there are two opposing theories in our law – the pledge theory and the outright cession theory. The court found it unnecessary to resolve these diverging theories and instead, found that the nature of a security cession is to be determined using the expressed intention of the parties.

Thirteen years later the same question arose in *Engen Petroleum Ltd v Flotank Transport (Pty) Ltd (876/20) [2022] ZASCA 98 (21 June 2022)* with the twist that the answer would determine the legal position of a cessionary in the context of liquidation of the cedent.

In this case, Engen Petroleum Limited (Engen) sought to enforce its rights acquired in terms of a security cession concluded with Windsharp Trading Proprietary Limited (Windsharp). In terms of the cession, Windsharp ceded its book debts together with its reversionary rights to Engen. The ceded rights included debts owed to Windsharp by Flotank Transport Proprietary Limited (Flotank). After concluding the cession, Windsharp was placed under liquidation. However, prior to the order of liquidation becoming final, Engen provided Flotank with written notice of the cession, together with a notice

of intention to claim in terms of the cession. In response, Flotank required Engen to provide it with a copy of the cession. Following Engen's failure to do so, Flotank made a number of payments due by it, to Windsharp directly. On the basis that Windsharp had ceded its book debts as security, Engen applied to the High Court for an order that Flotank pay Engen the amounts it had paid to Windsharp. Flotank opposed the application on the grounds that following the liquidation of Windsharp, the ceded book debts reverted to the liquidators and Engen became a secured creditor, as such Engen's claim was against Windsharp's liquidators. In addition, Flotank contended that since Engen had failed to provide it with the cession relied upon, no proper perfection of the cession had occurred. The High Court found that the notice of cession had been sufficient to indicate Engen's rights, however, pursuant to the liquidation,

the claim to the ceded rights lay with the liquidators of Windsharp because the cession amounted to a pledge. In the SCA, Engen argued that in consequence of reversionary rights forming part of the ceded rights, the agreement constituted an outright cession as opposed to a pledge.

The SCA explained the opposing theories, noting that under the pledge theory, a debt is pledged to the cessionary and the cedent retains reversionary interests in the debt. Consequently, only the right to enforcement on non-payment by the debtor is ceded. However, an outright cession constitutes a transfer of all rights relating to the ceded debt and an undertaking (*pactum fiduciae*) that the cessionary will re-cede the debt to the cedent once the secured debt is discharged is superimposed. Consequently, the cedent will have no direct interest in the ceded right but instead have a personal claim against

## The jury's still out on the nature of security cessions, but let's consider the effect on liquidation

CONTINUED

the cessionary for the re-cession of the ceded rights upon discharge of their secured debt. It is established in our law that cession constitutes the transfer of a right, thus, the crux of the debate regarding the nature of security cessions centres on the extent of the rights transferred. Under the pledge construction, only enforcement rights are ceded and the substance of the right is retained by the cedent. Whereas under the outright cession theory, the entirety of the rights relating to the ceded debt are transferred. The court referred to its earlier decision in Grobler and held that while the pledge theory is accepted as the default position and that a security cession is deemed to resemble a pledge unless the parties intend otherwise, our law still recognises both theories. Further, it confirmed that the real nature of a security cession will be determined by the intention of the parties as recorded in the cession.

The court found that the agreement between Engen and Windsharp constituted an outright cession given that the debt and the reversionary rights were ceded. Therefore, the effect of an outright cession is that it immediately transfers the ceded rights, being the debt and the reversionary rights thereto, to the estate of the cessionary. Accordingly, the ceded rights were an asset in the estate of Engen and Flotank was obliged to make payments to Engen on receipt of the notice of cession. It follows from the order requiring Flotank to make the payments to Engen, that the ceded rights being assets in the estate of Engen would have been unaffected by the liquidation of Windsharp. In contrast, the effect of a security cession taking the pledge construction on liquidation is that it renders the cessionary a secured creditor forming part of the concursus creditorum and the ceded rights are dealt with in terms of the

legislation applicable to liquidation. The Insolvency Act 24 of 1936 provides that a secured creditor is entitled only to the proceeds of realising the ceded rights unless they have included reliance on the free residue for the balance of their claims in terms of section 89 of the Act. As such, parties to a security cession taking the pledge construction, cannot validly agree to vary the position of the cessionary or their distribution rights in respect of the insolvent estate. Accordingly, as a secured creditor, the cessionary's claim will be subject to the laws applicable to liquidation, and the total value recoverable will be limited to the value received pursuant to realisation of the ceded rights.

## The jury's still out on the nature of security cessions, but let's consider the effect on liquidation

CONTINUED

When funding a high risk borrower or in the context of limited recourse funding, it is worthwhile considering security in the form of an outright cession incorporating a pactum fiduciae in order to manage the liquidation risk. Most funding transactions are structured to incorporate the pledge construction of the security cession as lenders are ordinarily interested only in the right to enforcement on non-performance by the debtor as opposed to entirely stepping into the cedent's shoes in respect of the ceded debt. However, this case indicates that an outright security cession can be the more favourable option where there is high liquidation risk. This is so, particularly where little administrative burden would be placed on the cessionary in consequence, for instance a cession

of proceeds insurance policies. The position would be different in the context of cession of securities which would in contrast require more involvement on the part of the cessionary in its capacity as a holder of such securities.

Our law provides that the intention of the parties, as evidenced by the facts, will determine the nature of a security cession. This case illustrates the bilateral nature of security cessions in our law and highlights the disparate legal effects of the two types of security cession on liquidation of a cedent. Where parties have concluded an outright cession incorporating a pactum fiduciae, the ceded rights are immediately transferred to the estate of the cessionary and remain unaffected by liquidation of the

cedent. However, where the security cession takes the pledge construction, in the event of the liquidation of the cedent, the ceded rights form part of the liquidated estate, available for distribution by the liquidator in accordance with the applicable legislation. Evidently, the nature of the cession has significant consequences on the position of the cessionary in the event of the cedent's liquidation as it determines the extent of their protection.

**KUDA CHIMEDZA AND  
ROXANNE WEBSTER**

## OUR TEAM

For more information about our Dispute Resolution practice and services in South Africa and Kenya, please contact:



### Tim Fletcher

Chairperson  
Practice Head & Director:  
Dispute Resolution  
T +27 (0)11 562 1061  
E tim.fletcher@cdhlegal.com

### Timothy Baker

Director:  
Dispute Resolution  
T +27 (0)21 481 6308  
E timothy.baker@cdhlegal.com

### Eugene Bester

Director:  
Dispute Resolution  
T +27 (0)11 562 1173  
E eugene.bester@cdhlegal.com

### Jackwell Feris

Sector Head:  
Industrials, Manufacturing & Trade  
Director: Dispute Resolution  
T +27 (0)11 562 1825  
E jackwell.feris@cdhlegal.com

### Thabile Fuhrmann

Joint Sector Head:  
Government & State-Owned Entities  
Director: Dispute Resolution  
T +27 (0)11 562 1331  
E thabile.fuhrmann@cdhlegal.com

### Anja Hofmeyr

Director:  
Dispute Resolution  
T +27 (0)11 562 1129  
E anja.hofmeyr@cdhlegal.com

### Tiffany Jegels

Director:  
Dispute Resolution  
T +27 (0)11 562 1388  
E tiffany.jegels@cdhlegal.com

### Tobie Jordaan

Sector Head:  
Business Rescue, Restructuring & Insolvency  
Director: Dispute Resolution  
T +27 (0)11 562 1356  
E tobie.jordaan@cdhlegal.com

### Corné Lewis

Director:  
Dispute Resolution  
T +27 (0)11 562 1042  
E corne.lewis@cdhlegal.com

### Vincent Manko

Director:  
Dispute Resolution  
T +27 (0)11 562 1660  
E vincent.manko@cdhlegal.com

### Richard Marcus

Director:  
Dispute Resolution  
T +27 (0)21 481 6396  
E richard.marcus@cdhlegal.com

### Burton Meyer

Director:  
Dispute Resolution  
T +27 (0)11 562 1056  
E burton.meyer@cdhlegal.com

### Rishaban Moodley

Sector Head: Gambling & Regulatory Compliance  
Director: Dispute Resolution  
T +27 (0)11 562 1666  
E rishaban.moodley@cdhlegal.com

### Mongezi Mpahlwa

Director:  
Dispute Resolution  
T +27 (0)11 562 1476  
E mongezi.mpahlwa@cdhlegal.com

### Kgosi Nkaiseng

Director:  
Dispute Resolution  
T +27 (0)11 562 1864  
E kgosi.nkaiseng@cdhlegal.com

### Desmond Odhiambo

Partner | Kenya  
T +254 731 086 649  
+254 204 409 918  
+254 710 560 114  
E desmond.odhiambo@cdhlegal.com

### Lucinde Rhoodie

Director:  
Dispute Resolution  
T +27 (0)21 405 6080  
E lucinde.rhodie@cdhlegal.com

### Clive Rumsey

Sector Head: Construction & Engineering  
Director: Dispute Resolution  
T +27 (0)11 562 1924  
E clive.rumsey@cdhlegal.com

### Belinda Scriba

Director:  
Dispute Resolution  
T +27 (0)21 405 6139  
E belinda.scriba@cdhlegal.com

### Tim Smit

Director:  
Dispute Resolution  
T +27 (0)11 562 1085  
E tim.smit@cdhlegal.com

### Kylene Weyers

Director:  
Dispute Resolution  
T +27 (0)11 562 1118  
E kylene.weyers@cdhlegal.com

### Joe Whittle

Director:  
Dispute Resolution  
T +27 (0)11 562 1138  
E joe.whittle@cdhlegal.com

### Roy Barendse

Executive Consultant:  
Dispute Resolution  
T +27 (0)21 405 6177  
E roy.barendse@cdhlegal.com

### Jonathan Witts-Hewinson

Executive Consultant:  
Dispute Resolution  
T +27 (0)11 562 1146  
E witts@cdhlegal.com

## OUR TEAM

For more information about our Finance & Banking practice and services in South Africa and Kenya, please contact:



### **Mashudu Mphafudi**

Practice Head & Director:  
Finance & Banking  
T +27 (0)11 562 1093  
E mashudu.mphafudi@cdhlegal.com



### **Sammy Ndolo**

Managing Partner | Kenya  
T +254 731 086 649  
+254 204 409 918  
+254 710 560 114  
E sammy.ndolo@cdhlegal.com



### **Sabelo Goma**

Director:  
Finance & Banking  
T +27 (0)11 562 1602  
E sabelo.goma@cdhlegal.com



### **Adnaan Kariem**

Director:  
Finance & Banking  
T +27 (0)21 405 6102  
E adnaan.kariem@cdhlegal.com



### **Mbali Khumalo**

Director:  
Finance & Banking  
T +27 (0)11 562 1765  
E mbali.khumalo@cdhlegal.com



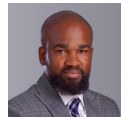
### **Jacqueline King**

Director:  
Finance & Banking  
T +27 (0)11 562 1554  
E jacqueline.king@cdhlegal.com



### **Pitso Kortjaas**

Director:  
Finance & Banking  
T +27 (0)11 562 1589  
E pitso.kortjaas@cdhlegal.com



### **Phetole Modika**

Director:  
Finance & Banking  
T +27 (0)11 562 1625  
E phetole.modika@cdhlegal.com



### **Deon Wilken**

Director:  
Finance & Banking  
T +27 (0)11 562 1096  
E deon.wilken@cdhlegal.com

### **Kuda Chimedza**

Senior Associate:  
Finance & Banking  
T +27 (0)11 562 1737  
E kuda.chimedza@cdhlegal.com

### **Koketso Maake**

Senior Associate:  
Finance & Banking  
T +27 (0)11 562 1618  
E koketso.maake@cdhlegal.com

### **Ernest Maboko**

Senior Associate  
Finance & Banking  
T +27 (0)11 562 1771  
E ernest.maboko@cdhlegal.com

### **Stephanie Goncalves**

Professional Support Lawyer:  
Finance & Banking  
T +27 (0)11 562 1448  
E stephanie.goncalves@cdhlegal.com

### **Brian Muchiri**

Associate | Kenya  
T +254 731 086 649  
+254 204 409 918  
+254 710 560 114  
E brian.muchiri@cdhlegal.com

### **Thato Sentle**

Associate:  
Finance & Banking  
T +27 (0)11 562 1844  
E thato.sentle@cdhlegal.com

**BBBEE STATUS:** LEVEL ONE CONTRIBUTOR

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.

**PLEASE NOTE**

This information is published for general information purposes and is not intended to constitute legal advice. Specialist legal advice should always be sought in relation to any particular situation. Cliffe Dekker Hofmeyr will accept no responsibility for any actions taken or not taken on the basis of this publication.

**JOHANNESBURG**

1 Protea Place, Sandton, Johannesburg, 2196. Private Bag X40, Benmore, 2010, South Africa.

Dx 154 Randburg and Dx 42 Johannesburg.

T +27 (0)11 562 1000 F +27 (0)11 562 1111 E [jhb@cdhlegal.com](mailto:jhb@cdhlegal.com)

**CAPE TOWN**

11 Buitengracht Street, Cape Town, 8001. PO Box 695, Cape Town, 8000, South Africa. Dx 5 Cape Town.

T +27 (0)21 481 6300 F +27 (0)21 481 6388 E [ctn@cdhlegal.com](mailto:ctn@cdhlegal.com)

**NAIROBI**

Merchant Square, 3<sup>rd</sup> floor, Block D, Riverside Drive, Nairobi, Kenya. P.O. Box 22602-00505, Nairobi, Kenya.

T +254 731 086 649 | +254 204 409 918 | +254 710 560 114

E [cdhkenya@cdhlegal.com](mailto:cdhkenya@cdhlegal.com)

**STELLENBOSCH**

14 Louw Street, Stellenbosch Central, Stellenbosch, 7600.

T +27 (0)21 481 6400 E [cdhstellenbosch@cdhlegal.com](mailto:cdhstellenbosch@cdhlegal.com)

©2022 11452/AUG