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DISPUTE RESOLUTION ALERT

IN THIS **ISSUE**

DOES AN ARBITRATION AWARD CREATE A NEW DEBT?

The somewhat conceivable tension between the Arbitration Act, 1965 and the Prescription Act, 1969 has received a lot of attention from the courts recently. In the main, the issues are whether an arbitration award creates a new debt and whether a claim to make an arbitration award an order of court prescribes within three years of its publication in terms of the Prescription Act. In the recent case of *Brompton Court Body Corporate v Khumalo* (398/2017) [2018] ZASCA 27 (23 March 2018) the Supreme Court of Appeal (SCA) grappled with these questions and provided some guidance.

PREFERRED OR NOT PREFERRED – THE SUPER PREFERENT STATUS OF A BUSINESS RESCUE PRACTITIONER IN SUBSEQUENT LIQUIDATION PROCEEDINGS

The Supreme Court of Appeal provided clarity in *Diener N.O. v Minister of Justice & Others* (926/2016) regarding the ranking of the business rescue practitioner's (BRP) claim for remuneration and expenses. The SCA also clarified whether such claim was conferred a "super preference" over all creditors, secured and unsecured in subsequent liquidation proceedings.

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The respondent opposed the application in effect only on the basis that the debt in question had prescribed in terms of the Prescription Act which defence was upheld by the court a quo.

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The court found that a claim that an arbitration award be made an order of court is not a 'debt' in terms of the Prescription Act.

In this case, disputes arose between the parties, which, by agreement, were referred to arbitration. The arbitrator published the arbitration award on 21 December 2012. On 26 March 2014, the appellant applied that the arbitration award be made an order of court in terms of s31 of the Arbitration Act. The respondent opposed the application in effect only on the basis that the debt in question had prescribed in terms of the Prescription Act which defence was upheld by the court *a quo*.

As to the first issue, namely that an arbitration award creates a new debt, the SCA held that the converse will generally be true. The court opined that even a judgment of a court of law generally does not create a new debt but merely serves to affirm and/or liquidate an existing debt which was disputed. What the judgment does in relation to prescription of a debt, according to the court, is to give rise to a new period of prescription of 30 years in terms of s11(a)(ii) of the Prescription Act.

The SCA therefore held that the same principle must generally apply to an arbitration award, save that it would not attract a new prescriptive period of 30 years in terms of s11 of the Prescription Act. The decision of the SCA is silent on whether the arbitration award is subject to any other prescriptive period. As things stand, it can be interpreted to the effect that an arbitration award does not superannuate. In our view, there is no justifiable reason an arbitration award should not similarly be subjected to a 30-year prescriptive period. In conclusion, the court found that an arbitration award does not create a new debt.

As to the second issue, namely that the claim to make an arbitration award an order of court is a debt that prescribes after three years, the court held that it was unable to agree. In the main, the court found that a claim that an arbitration award be made an order of court is not a 'debt' in terms of the Prescription Act. The court endorsed the well accepted view that a debt in terms of the Prescription Act is an obligation to pay money, deliver goods or render services.

In concluding, the court found that a claim to make the arbitration award an order of court did not require the other party to perform any obligation at all, let alone

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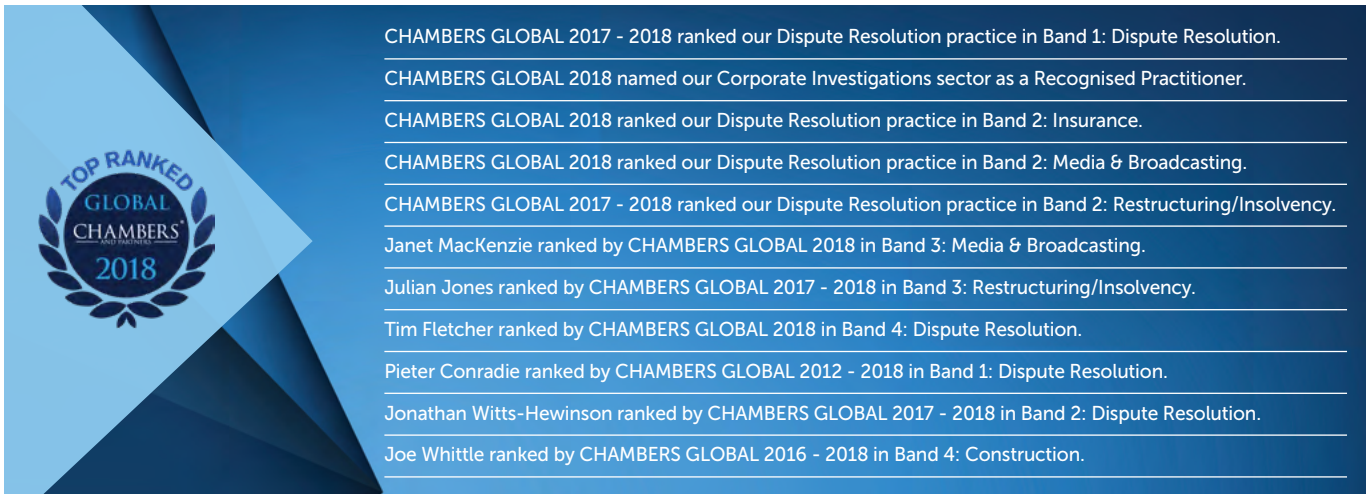
The decision further provides long awaited certainty to the effect that an arbitration award does not create a new debt and that a claim to make the arbitration award an order of court does not constitute a debt and therefore not subject to the three-year prescriptive period.

one to pay money, deliver goods or render services. The applicant would merely be utilising a statutory remedy available to it. The court was of the view that this is similar to a claim for rectification of a contract, which has been held not to constitute a debt in terms of the Prescription Act.

It is important to note that the above principles are only applicable to arbitration awards under the auspices of the Arbitration Act, the so-called domestic arbitrations and not international arbitrations governed by the International Arbitration Act, 2017.

The decision of the SCA adds to a growing body of case law where courts are generally hesitant to interfere in the enforcement of arbitration awards in the absence of a review application in accordance with s33 of the Arbitration Act. The decision further provides long awaited certainty to the effect that an arbitration award does not create a new debt and that a claim to make the arbitration award an order of court does not constitute a debt and therefore not subject to the three-year prescriptive period.

Vincent Manko



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PREFERRED OR NOT PREFERRED – THE SUPER PREFERENT STATUS OF A BUSINESS RESCUE PRACTITIONER IN SUBSEQUENT LIQUIDATION PROCEEDINGS

The BRP contended that s135(4) and s 43(5) of the Companies Act, provided that to the extent that the BRP's remuneration and expenses are not fully paid, such claim would rank in priority before the claims of all other secured and unsecured creditors.

The Supreme Court of Appeal provided clarity in *Diener N.O. v Minister of Justice & Others* (926/2016) regarding the ranking of the business rescue practitioner's (BRP) claim for remuneration and expenses. The SCA also clarified whether such claim was conferred a "super preference" over all creditors, secured and unsecured in subsequent liquidation proceedings.

Simply put, the preference only operates within a limited context and should not be interpreted to include a preference over pre-business rescue secured creditors.

In the court *a quo*, the BRP contended that s135(4) and s 43(5) of the Companies Act, No 61 of 1973 (Companies Act) provided that to the extent that the BRP's remuneration and expenses are not fully paid, such claim would rank in priority before the claims of all other secured and unsecured creditors.

Section 135 of the Companies Act deals with post-commencement finance, which includes the BRP's remuneration and expenses. The section provides that any remuneration or reimbursement for expenses which become due and payable by the company to an employee during the business rescue proceedings, but is not paid to the employee, will be regarded as post-commencement finance and will be paid in the order of preference set out in s135(3)(a).

Section 135(3)(a) provides the BRP with a preference over claims in respect of post-commencement finance irrespective of whether or not those claims are secured and a preference over all unsecured claims against the company. Should the business rescue proceedings be superseded by a liquidation order as contemplated in s135(4), the preference conferred in s135 will remain in force with the exception of any claims arising out of the cost of liquidation.

The SCA, in rejecting the BRP's argument, stated that s135(4) provides:

> To the BRP, after the conversion of business rescue proceedings into liquidation proceedings, no more than *a preference in respect of his or her remuneration to claim against the free residue after the costs of liquidation but before claims of employees for post-commencement wages, of those who have provided other post-commencement finance, whether those claims were secured or not, and of any other unsecured creditors.*

Simply put, the preference only operates within a limited context and should not be interpreted to include a preference over pre-business rescue secured creditors.

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CONTINUED

The court held that s135(4) and s143(5) of the Companies Act does not create a "super preference" as contended by the BRP.

The court held that s135(4) and s143(5) of the Companies Act does not create a "super preference" as contended by the BRP. The effect of this is that a BRP would be considered a creditor of the company within the ambit of s44 of the Insolvency Act and would be required to submit and prove their claim in respect of their remuneration and expenses. The court held that there was nothing in the Companies Act indicating that it contemplated the dilution of the rights of any secured creditors. In essence, the claim by the BRP would be treated as an unsecured claim.

This should also be a cautionary note to lenders who furnish a company in financial distress with post-commencement finance without the necessary security as contemplated by s135(2)(a) of the Company Act (post-commencement financing being secured to the lender by utilising any asset of the company to the extent that it is not otherwise encumbered). Such an unsecured lender would not be considered a preferred creditor and will be afforded no more than a preference in respect of his or her claim against the free residue after the costs of liquidation. In short, such an unsecured lender will simply have a preferential right to payment over all unsecured creditors.

Tiffany Jegels and Corné Lewis

Tim Fletcher was named the exclusive South African winner of the **ILO Client Choice Awards 2017 – 2018** in the litigation category.

Richard Marcus was named the exclusive South African winner of the **ILO Client Choice Awards 2018** in the Insolvency & Restructuring category.

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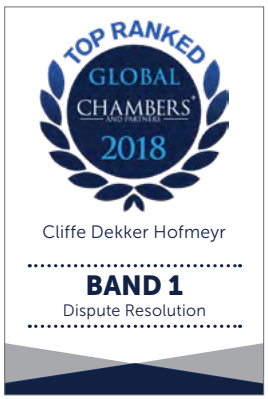

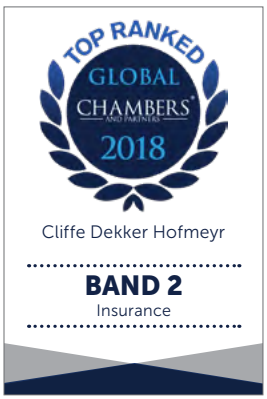

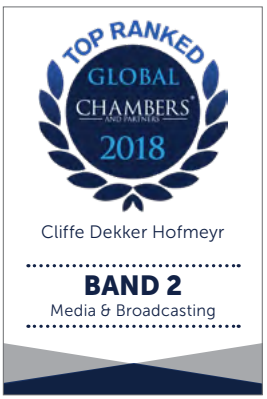

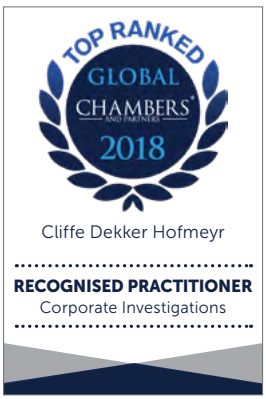

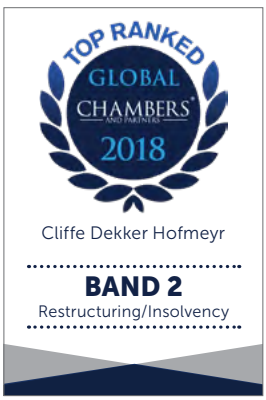

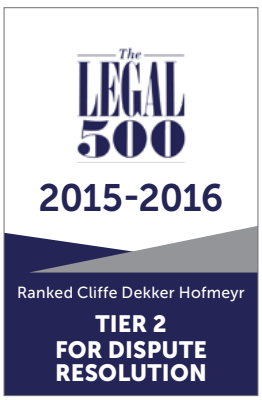

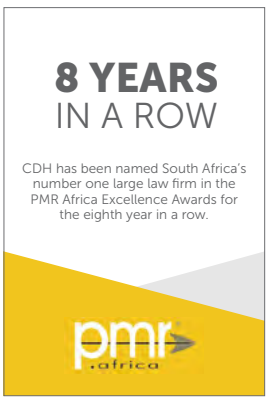

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BBBEE STATUS: LEVEL TWO CONTRIBUTOR
Cliffe Dekker Hofmeyr is very pleased to have achieved a Level 2 BBBEE verification under the new BBBEE Codes of Good Practice. Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

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