A highly effective tool for recovering creditors' claims and legal costs

By Haroon Y Laher

Creditors using amendments to the Insolvency Act to maximise the dividend payable to them in an insolvency need to be aware that the relevant amendments are superficial rather than substantive. The 1993 amendments to the Act's sections 32 (1) and 104 (3) are of relevance in this context..

Section 32 deals with proceedings that may be brought by a trustee or, failing him, a creditor, to set aside any disposition of property made by an insolvent prior to his sequestration.

Section 104 (3), on the other hand, deals with the right of creditors as a whole or in general to participate in any benefit obtained by the conduct of legal proceedings at the instance of any specific creditor.

I consider the 1993 amendments somewhat superficial rather than substantive in nature because the amendments only go so far as to provide certainty in the effect of the provisions of section 32 and 104 through clear and unambiguous wording and correct cross-referencing to sections in the Insolvency Act.

Section 32 (1) (a) allows a trustee to institute proceedings:

- to recover the value of property or a right in terms of section 25 (4);

- to set-aside a disposition of property or a penalty under sections 26, 29, 30 or 31; and
- for the recovery of compensation or a penalty under section 31.

Section 25 (4) allows a trustee to recover the value of any immovable property or a right to such immovable property, unlawfully disposed of by the insolvent.

The property or the value of the right disposed of may be recovered from the insolvent or any person who had acquired the property or the right from the insolvent, provided that where insufficient value was given, the claim shall be limited to the difference between the value of the property or the right and the actual value given in return.

Sections 26, 29, 30 and 31 deal with impeachable transactions capable of being set-aside, namely dispositions without value, voidable preferences, undue preferences and collusive dealings committed by the insolvent prior to his sequestration.

The penalty provided in section 31 (3) applies to any party involved in a collusive transaction prior to the sequestration of the insolvent. Section 31 (2) provides that the penalty shall be the benefit which would have accrued to the party engaging in the collusive transaction if such transaction had not been set aside. If such party is a creditor, he shall forfeit his claim against the estate of the insolvent.

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Section 32 (1) (b) provides that if a trustee fails to take the proceedings referred to in section 32 (1) (a), such proceedings may be taken by any creditor in the name of the trustee and against indemnification by such creditor.

To quote from Neser J [South African Board of Executors and Trust Company Limited

(in liquidation) v Gluckman 1967 (1) SA 534 (A)], the legislature "*intended that the action should be in the name of the trustee and … it is not in the name of the trustee if the creditor sues in his own name stating that he sues in the name of the trustee.*"

In practice, the trustee is the plaintiff, although in real terms, by virtue of an indemnity given by a creditor in favour of the trustee in respect of any legal costs incurred, he is only a nominal plaintiff.

The creditor becomes the driving force behind the proceedings, conducting and controlling them from beginning to end.

Note that any settlement concluded in the course of such legal proceedings must be approved by the trustee, notwithstanding any indemnity that may be given in his favour. The indemnity only goes as far as the issue of costs; it does not affect the trustee's ultimate duty and obligation, which is to administer the estate for the benefit of all the estate's creditors.

It often happens that a creditor requests the trustee to conduct an enquiry (as opposed to legal proceedings) into the affairs of the insolvent. The trustee frequently responds that the estate does not have sufficient funds in order to, for example, pay for the legal expenses incurred in the conduct of the enquiry.

Any creditor desirous of proceeding with an enquiry would in such a situation agree to indemnify the trustee from any legal costs which may be incurred.

Would a creditor providing the indemnity in favour of the trustee be entitled to recover those costs from any benefit derived to the insolvent estate from the conduct of the enquiry?

In practice, the trustee will usually allow such expenses to be recovered by the creditor

as costs of administration in terms of section 97 of the Insolvency Act; costs payable from the free residue portion of the estate.

Section 104 (3) provides a benefit in real terms to any creditor instituting legal proceedings over any of the actions mentioned in section 32 (1) (a).

In terms of this section, creditors that are not party to such legal proceedings (in the sense of co-indemnifiers of costs) cannot derive any benefit from any money or proceedings of any property recovered as a result of such legal proceedings. Such non-participating creditors may only participate in the actual recovery or benefit after the costs and the claims of the participating creditor "have been paid in full".

Section 104 (3) therefore offers a significant and distinct advantage to creditors wishing to pursue those matters referred to in section 32 (1) (a) and institute legal proceedings to achieve a desired objective in terms thereof.

Section 339 of the Companies Act, 1973, provides that in a winding-up of a company unable to pay its debts, the provisions of the law relating to insolvency shall, insofar as they are applicable, be applied *mutatis mutandis* to any matter not specifically provided for by the Companies Act.

Haroon Y Laher is a partner at corporate law firm Bowman Gilfillan