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## TO BE OR NOT TO BE? THE ROLE OF PRIVATE ENQUIRIES IN THE SOUTH AFRICAN INSOLVENCY LAW

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### 1 Introduction

It is well established that wording must be interpreted in the light of their context being "the matter of the statute, its apparent scope and purpose and, within limits, its background..." [one] must have regard to the context in which the words of the section occur even though... the words themselves appear to be clear and unambiguous... the emerging trend in statutory construction is to have regard to the context in which the words occur even where the words to be construed are clear and unambiguous. This "technique" is now required by the Constitution, in particular by section 39(2).<sup>1</sup>

It appears customary in secondary sources to initiate any discussion on section 417 of the *Companies Act* 61 of 1973<sup>2</sup> with the word "draconian".<sup>3</sup> Consulting a dictionary one is informed that "draconian" relates to, or is characteristic of, Draco or the severe code of laws held to have been framed by him.<sup>4</sup> Draco was an Athenian law scribe under whom small offences had heavy punishments, and thus the perception appears to be that the provisions of section 417 are overly harsh and that the potential scope of the provision is disproportionate to the rationale for which it was enacted. The purpose of this article is to demonstrate that section 417, although

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<sup>1</sup> Satchwell J in *Huang v Bester* 2012 5 SA 551 (GSJ) para 17. Hereafter referred to as "*Huang v Bester*".

<sup>2</sup> Hereafter refer to as the "*Companies Act*".

<sup>3</sup> See *Botha v Strydom* 1992 2 SA 155 (N) 159G-I; *Jeeva v Receiver of Revenue, Port Elizabeth* 1995 2 SA 433 (SE) A-B.

<sup>4</sup> Merriam Webster Date Unknown Draconian <http://www.merriam-webster.com/dictionary/draconian>.

wide in ambit,<sup>5</sup> does not offend our sense of justice and fairness, and that it therefore deserves to remain part of the future South African insolvency law regime.<sup>6</sup>

This article deals with the question of whether or not section 417 is adequately framed in order to fulfill its intended purposes in South African insolvency law. As stated in the quotation above, the current trend is to interpret legislation with reference to its context, ie the scope and purpose of such legislation, and thus the study is aimed at a policy evaluation. The intention is to determine whether section 417 conforms to the underlying values and interests that it was designed to serve and whether the outcome is advantageous to society.

The reason for focusing on section 417 is based on the unique and inquisitorial nature of the section, which jars with our sense of justice and seems a curious inclusion in a predominantly adversarial system. A section which allows for a witness to be summoned *ex parte*, where such person has no access to the application and cannot compel the discovery of documents, nor has access to the enquiry itself or the record of it, does indeed seem draconian in our modern age of constitutionalism and in the face of modern legislation such as the *Promotion of Access to Information Act 2 of 2000*.<sup>7</sup>

Although the scrutiny of private examinations is not novel, it is felt that further exploration of the subject is justified by virtue of the fact that robust and innovative legislative changes have been seen in the South African corporate landscape. The section has already been tested and found to be lawful and constitutional,<sup>8</sup> but the

<sup>5</sup> Reference is made to the word "any" five times in s 236(1). In *Huang v Bester* para 17 Satchwell J points out that the word "any" in s 236 "offers the most open-ended and far-reaching enumeration...which it is possible to describe".

<sup>6</sup> In the early nineties the South African Law Reform Commission embarked on an extensive study of South African insolvency law and published its *Report on the Review of the Law of Insolvency* in 2000: see SALC *Review of the Law of Insolvency* vols 1 and 2. For a more detailed discussion see Evans *Critical Analysis of Problem Areas* 430; Burdette *Framework for Corporate Insolvency Law Reform* ch 3; Boraine and van der Linde 1998 *TSAR* 621; Havenga 2001 *SA Merc LJ* 408; Loubser 2007 *SA Merc LJ* 123.

<sup>7</sup> Meskin *et al* *Insolvency Law* para 8.5.2 notes that a witness is entitled to a copy of the record of his own evidence at his own cost.

<sup>8</sup> Meskin *et al* *Insolvency Law* para 8.5.2, where it is noted that save for part of s 417(2)(b), all provisions of s 417 and 418 are not constitutionally invalid. See further *Bernstein v Bester* 1996 2 SA 751 (CC), hereafter referred to as "*Bernstein*" or "*Bernstein v Bester*". The provision of s 417(2)(b) that "any answer given to any such question may thereafter be used in evidence

aim is to ascertain whether the section serves a legitimate purpose and is necessary in a democratic society. A further impetus to this study was the judgment of *Kebble v Gainsford*,<sup>9</sup> which again brought section 417 to the fore and thus prompted a more in-depth investigation of the nature, scope and objectives of the section. The court concluded in *Kebble* that the circumstances of that matter clearly indicated the need for private investigation by the liquidators and the judgment is therefore a positive affirmation for the continued demand for investigations of this nature. The *Kebble* judgment is not critically analysed, as such an analysis would not aid a deeper understanding of section 417, but the approach taken by the court in the matter lucidly setting out the nature, scope and purpose of the section is utilized as a springboard for this investigation. In short, the question asked in this article is whether or not section 417 is adequately framed in its current format in order to fulfill its intended purpose in South African insolvency law.

In Part 2 the law applicable to South African private examinations is considered. The primary source is section 417 of the *Companies Act*. Secondary sources include academic texts and judicial interpretation, in particular the matter of *Kebble v Gainsford*.<sup>10</sup> Part 3 comprises a comparative study, albeit very brief and condensed, taking a look at a similar provision in the *Insolvency Act* of the United Kingdom, namely section 236 of the *Insolvency Act*, 1986.<sup>11</sup> England is chosen as a source of comparison because much South African insolvency law emanates from England.<sup>12</sup> Further, the decision was prompted by the *Kebble* judgment itself, which refers to English cases that are seminal in this area of the law. Part 4 provides a comparison between the two systems for the purpose of identifying areas where South African

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against him" is constitutionally invalid with effect from 27 April 1994, in relation only to criminal proceedings other than those mentioned in the text, see *Ferreira v Levin* 1996 1 SA 984 (CC), hereafter referred to as "*Ferreira v Levin*".

<sup>9</sup> *Kebble v Gainsford* 2010 1 SA 561 (GSJ). Hereafter referred to as "*Kebble*" or "*Kebble v Gainsford*".

<sup>10</sup> *Kebble v Gainsford*.

<sup>11</sup> Hereafter referred to as "*Insolvency Act*, 1986".

<sup>12</sup> Our earlier insolvency legislation also had much in common with the English bankruptcy law. Ordinance 64 of 1829 was introduced in the Cape of Good Hope and although the basis of the Ordinance was English law, it wove together English and Dutch practice and established the principles of our present insolvency practice. See Burdette *Framework for Corporate Insolvency Law Reform* Part 2 77.

law may benefit from reform, and concludes with suggestions for appropriate reform.

## 2 South African law

### 2.1 Introduction

The matter of *Kebble v Gainsford* is a useful vehicle for looking at the nature and purpose of a section 417 examination as the judgment contains extensive and constructive references to the various objectives of such an examination.<sup>13</sup> In his judgment Levenberg AJ relied heavily on the approach of the constitutional court in the matter of *Bernstein v Bester*,<sup>14</sup> where the constitutionality of section 417 and 418 was tested. Levenberg AJ finds himself in good company in his reliance on the *Bernstein* case, as this case has been embraced as a seminal decision on particularly the right to privacy, and in the approximately six years since the judgment it has been referred to in almost ninety High Court and Constitutional Court cases.<sup>15</sup> For the purposes of this article, the comments relating to sections 417 and 418 are of relevance. The court in *Bernstein* declared sections 417 and 418 to be constitutionally valid. The comments of Ackerman J relating to the objectives of a section 417 examination are of particular interest and these comments will therefore be used as a point of reference. To begin with, however, the facts of the *Kebble* matter are provided below.

### 2.2 The facts

The facts of the *Kebble* case are evident from the judgment and can be summarised as follows: The applicant, Kebble was faced with a summons compelling him to testify in a section 417 examination. He did not wish to be submitted to such an examination and brought an application for the proceedings to be set aside. Kebble was the sole surviving director of a company called BNC ("the company") prior to its liquidation. He openly admitted in an affidavit that the company had been used as a

<sup>13</sup> *Kebble v Gainsford*.

<sup>14</sup> See n 8 above.

<sup>15</sup> Lawcite Date Unknown <http://www.saflii.org/cgi-bin/LawCite?cit=1996+ZACC+2>.

vehicle to perpetrate a fraud against another company, Randgold.<sup>16</sup> Randgold launched successful winding-up proceedings against the company and subsequent to the final liquidation order, a settlement agreement was entered into whereby Kebble agreed to pay Randgold an amount of R30 million in settlement of any claims against him.<sup>17</sup> Kebble also alleged that Randgold undertook not to support the private examination at which he was summoned to give evidence. Kebble commenced payment in terms of the settlement agreement, but soon stopped due to an alleged dispute. This necessitated a second settlement agreement. The liquidators declined to be party to either of the settlement agreements due to the inherent risk they would be exposed to.<sup>18</sup> They were of the view that as no payment was made to the company itself, it was not to the benefit of all creditors. Although Randgold was the only creditor to come forward at that stage, other creditors had been identified. Randgold was not prepared to indemnify the liquidators against possible claims by other creditors. Kebble alleged that the proposed examination was an abuse for two reasons: the only proved creditor, Randgold, did not want the examination to continue as its claim had been satisfied by the settlement agreements and the liquidators were already possessed of sufficient information to effect the winding-up of the company, as well as to pursue litigation if necessary. The liquidators disputed these allegations.<sup>19</sup>

### **2.3 *The judgment***

Kebble's main contention of abuse was found to be unsubstantiated. He contended that the continuance of the examination would invalidate the settlement he had reached with Randgold, but the court found that had he wanted to rely on his bargain with Randgold he should have included the liquidators as parties to the agreement.<sup>20</sup> With regard to his second main contention, namely that the liquidators already had sufficient information to proceed with litigation, the court pointed out that even if the liquidators had a subjective intention to sue, based on the decision

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<sup>16</sup> *Kebble v Gainsford* 565D.

<sup>17</sup> *Kebble v Gainsford* 564B.

<sup>18</sup> *Kebble v Gainsford* 567E.

<sup>19</sup> *Kebble v Gainsford* 571J.

<sup>20</sup> *Kebble v Gainsford* 576A.

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in *Cloverbay Ltd (Joint Administrators) v Bank of Credit and Commerce International SA*,<sup>21</sup> that would not preclude them from going ahead with the examination.<sup>22</sup>

The court held that it was not incumbent upon the liquidators to demonstrate a need for the examination. It was the obligation of the party wishing to stop the examination to demonstrate a "clear abuse".<sup>23</sup> This Kebble had failed to do. On the contrary, this was clearly a case where an examination was warranted. The court listed nine reasons in support of this contention: 1) Kebble was the only surviving director of the company. 2) The only reason the company was formed was for fraudulent purposes. 3) The company was hopelessly insolvent and the liquidators had a duty to enquire as to the causes of the company's failure. 4) The fraud that had been committed was of a complex nature requiring further examination. 5) The fact that Kebble was prepared to pay R30 million to bring the examination to an end showed that he was not a person without knowledge of the affairs of the company. 6) It was against public policy to permit an examinee to avoid a liquidator's examination through a settlement to which the liquidators were not a party. 7) Kebble himself had conceded that there may be other legitimate claims against the company and the liquidators should be given the opportunity to investigate such claims. 8) As long as there were outstanding claims against the company, the liquidators had a duty to pursue all potential assets. 9). The fact that the liquidators had carried out their own examinations and prepared the groundwork for the examination should not be used against them. If this were not so, liquidators would be prevented from ever preparing for enquiries, lest their diligence count against them.<sup>24</sup>

The court pointed out, further, that it was the duty of the court to protect examinees at an examination. If questions were asked that were abusive, the Commissioner, as an officer of the court, should disallow them. If the Commissioner's discretion was ex

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<sup>21</sup> *Cloverbay Ltd (Joint Administrators) v Bank of Credit and Commerce International SA* 1991 Ch 90 (hereafter referred to as "Cloverbay").

<sup>22</sup> *Kebble v Gainsford* 575G.

<sup>23</sup> *Kebble v Gainsford* 579A.

<sup>24</sup> *Kebble v Gainsford* 577C- 578F.

## 2.4 *The duties of a liquidator*

As stated above, Levenberg AJ quoted extensively from the *Bernstein* matter, where Ackerman J summarised the major statutory duties of a liquidator in a winding-up. Ackerman J's summary is not provided, as it is in substance premised on the duties set out in the *Companies Act*, as discussed below.

The duties of a liquidator are found in sections 391 to 410 of the *Companies Act* 61 of 1973. The relevant sections are mandatory, thus in each case the liquidator "shall" perform the duty stipulated. The act first stipulates general duties and then lists specific duties. The general duties of the liquidator are noted to be the following: to proceed without delay to recover and take possession of all the assets and property of the company, to apply such assets and property in satisfaction of the costs of the winding-up and the claims of creditors, and to distribute the balance among those who are entitled thereto.<sup>25</sup> The specific duties of the liquidator include the duty to give information to the Master of the High Court,<sup>26</sup> to facilitate the Master's inspection of the books and documents of the company, and generally to aid the Master in the performance of his duties under the Act.<sup>27</sup> A liquidator further has a duty to expose offences and act thereon. He must examine the affairs and transactions of the company before its winding-up in order to ascertain if any of the directors and officers or past directors and officers of the company have contravened any provision of the Act or committed any offence.<sup>28</sup> Where appropriate, the liquidator must report any grounds to disqualify a director.<sup>29</sup> Before submitting his final account, the liquidator has to submit a report to the Master containing full particulars of any contraventions or offences. The Master in turn has a duty to transmit a copy of this report to the Attorney-General. The liquidator has a duty, except in the case of a member's voluntary winding-up, to present a report to

<sup>25</sup> Companies Act s 391.

<sup>26</sup> Hereafter referred to as the "Master" or "Master's office". The Master of the High Court is a public servant who is charged, *inter alia*, with control over the administration of insolvent estates. S 1 of the *Administration of Estates Act* 66 of 1965 defines "Master" in relation to any matter, property or estate, as the Master, Deputy Master or Assistant Master of the High Court who has jurisdiction in respect of the matter, property or estate.

<sup>27</sup> Companies Act s 392.

<sup>28</sup> *Companies Act* s 400(1)(a).

<sup>29</sup> *Companies Act* s 400(1)(b).

the creditors and contributories. This report has to be submitted no later than three months after the date of the liquidator's appointment to a general meeting of creditors and contributories of the company and has to set out, *inter alia*, the capital issued by the company, its estimated assets and liabilities, the causes of the failure of the company (if it had failed) and the progress and prospects of the winding-up.<sup>30</sup> Of significance is the fact that the liquidator has to note in this report whether or not further examination is in his opinion desirable in regard to any matter relating to the promotion, formation or failure of the company or the conduct of its business.<sup>31</sup>

As stated above, the duties of a liquidator summarised by Levenberg AJ in the *Kebble* matter correspond in material respects to those set out in the Act. What needs to be considered next is to whom the liquidator owes such duties.

## **2.5 To whom does the liquidator owe these duties?**

Although a company remains in existence during winding-up, it ceases from the commencement of the winding-up to carry on its business except in so far as may be required for the beneficial winding-up thereof, and its directors lose their powers except insofar as their continuance is sanctioned by the liquidator.<sup>32</sup> Whereas the business and affairs of the company up to that point are managed by or under the direction of its board,<sup>33</sup> who are accountable to the body of shareholders as a whole, the focus changes on winding-up to the benefit of creditors. It must be noted, however, that advantage to creditors is not one of the circumstances required for a company to be wound up by a Court.<sup>34</sup> Here the *Companies Act* differs from the *Insolvency Act*, which requires an advantage to creditors if a natural debtor's estate is sequestrated.<sup>35</sup>

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<sup>30</sup> Companies Act s 402.

<sup>31</sup> *Companies Act* s 402(1)(f).

<sup>32</sup> Companies Act s 353.

<sup>33</sup> *Companies Act* 71 of 2008 s 66.

<sup>34</sup> *Companies Act* s 344 (a)-(h) sets out the circumstances in which a company may be wound up by a court, with s 344 (f) (when the company is unable to pay its debts) and s 344 (h) (when it appears just and equitable that the company should be wound up) most often being referred to.

<sup>35</sup> *Insolvency Act* 24 of 1936 s6(1). See also Evans *Critical Analysis of Problem Areas* part IV for a detailed discussion.

It is trite South African law that the liquidator owes a duty to the creditors as a whole, otherwise known as the *concursus creditorum*.<sup>36</sup> The following dictum of Innes JA in the case of *Walker v Syfret*<sup>37</sup> is considered the *locus classicus* on the effect of a *concursus creditorum*, namely:

... the hand of the law is laid upon the estate, and at once the rights of the general body of creditors have to be taken into consideration. No transaction can thereafter be entered into with regard to estate matters by a single creditor to the prejudice of the general body.<sup>38</sup>

The nature of a liquidator's functions were also considered in the matter of *James v The Magistrate Wynberg*.<sup>39</sup> Before pronouncing on the fiduciary duty of a liquidator to the creditors, the court considered *obiter* whether or not a liquidator ought to be considered an officer of the court in South African law.<sup>40</sup> In doing so the court referred to the judgment of Coetze J in *Gilbert v Bekker*,<sup>41</sup> from which it is evident that Coetze J did not place much value on such a distinction:

To refer to a trustee as an officer of the Court seems to me inappropriate as he is just the holder of one of a host of offices created by various statutes such as directors, executors, mayors, town clerks, etc. But even if it is felt that he qualifies for this honour, there are no legal consequences which flow from that position, *qua* officer, nor powers to prescribe how he should perform his job. The furthest that one can take it is to feel free to censure him, when occasion demands, for conduct not becoming an officer and a gentleman, which seems to be just about the same thing, with as little legal content.<sup>42</sup>

In any event, the court in the *James* matter did not find it necessary to determine whether or not a liquidator is an officer of the court in South Africa, as the matter was decided on the basis that:

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<sup>36</sup> Swart Rol van 'n Concursus Creditorum 281; *Nel v Master of the High Court* 2002 ZASCA 4 (8 March 2002) para 6; Cf *Richter v Riverside Estates (Pty) Ltd* 1946 OPD 209 223.

<sup>37</sup> *Walker v Syfret* 1911 AD 141.

<sup>38</sup> *Walker v Syfret* 1911 AD 141 166.

<sup>39</sup> *James v Magistrate Wynberg* 1995 1 SA 1 (C), hereafter referred to as "James v Magistrate Wynberg". See also *Standard Bank of South Africa v The Master of the High Court* 2010 4 SA 405 (SCA), hereafter referred to as "Standard Bank v The Master".

<sup>40</sup> *James v Magistrate Wynberg* 13 I- J.

<sup>41</sup> *Gilbert v Bekker* 1984 3 SA 774 (W) 777 F-G, 778 A-B.

<sup>42</sup> *Gilbert v Bekker* 1984 3 SA 774 (W) 781E-F.

...whatever his status he stands in a fiduciary relationship both to the company of which he is the liquidator and to the body of its members as a whole, as well as to the body of its creditors as a whole.<sup>43</sup>

What turned out to be of greater importance in the *James* matter was the fact that the liquidator is expected to be detached, independent, impartial and even-handed in his dealings and must also be seen to be so.<sup>44</sup> This was considered to be particularly important when considering the "far-reaching machinery of interrogation" created by the *Companies Act*, giving rise to a *sui generis* procedure where the powers of the liquidator are "extraordinary and inquisitorial in nature".<sup>45</sup> The impartiality of a liquidator is a safeguard against the potential abuse of the examination procedure.

Whether a liquidator is an officer of the court in South African law still remains uncertain.<sup>46</sup> It should also be noted that as was mentioned in the *Gilbert* case our courts are not entrusted with insolvency administration as is the case in England where it is fundamentally the court's function.<sup>47</sup> With regard to the liquidator's legal position as to subsequent ethical standards, *Mars* asserts that an insolvency practitioner is not an officer of the court but does occupy a position of trust not only towards the creditors but also towards the insolvent himself.<sup>48</sup> As stated above, the court in the *Kebble* matter expressed the view that the Commissioner "as an officer of the Court" should disallow abusive questions.<sup>49</sup> It is submitted, in line with the decision in the *James* matter, that it will not advance standards in the winding-up

<sup>43</sup> *James v Magistrate Wynberg* 13I-J, 14A where the Court referred to the following matters as authority for this proposition: *Re Corporation, Gooch's Case* 1872 7 Ch App 207; *Caroline Trekkers en Implemente (Edms) Bpk v Venter* 1982 2 PH E9 (A); *Fey and Whiteford v Serfontein* 1993 2 SA 605 (A); *Ex parte Klopper: In re Sogervim SA (Pty) Ltd (in Liq) (Sogervim SA Intervening)* 1971 3 SA 791 (T); *Concorde Leasing Corporation (Rhodesia) Ltd v Pringle-Wood* 1975 4 SA 231 (R).

<sup>44</sup> *James v Magistrate Wynberg* 14D. See also *Standard Bank v The Master* 405: "In the winding-up of companies liquidators occupy a position of trust, not only towards creditors but also the companies in liquidation whose assets vests in them. Liquidators are required to act in the best interests of creditors. A liquidator should be wholly independent, should regard equally the interests of all creditors, and should carry out his or her duties without fear, favour or prejudice."

<sup>45</sup> *James v Magistrate Wynberg* 15C-D.

<sup>46</sup> English tradition and most common law jurisdictions consecutively consider an office-holder to be an officer of the court. Finch *Corporate Insolvency Law* 378. See also *Insolvency Act*, 1986 ss 117(5), 400(2) and Schedule B1.

<sup>47</sup> *Gilbert v Bekker* 777F-G.

<sup>48</sup> Bertelsmann *Mars*: Law of Insolvency 293.

<sup>49</sup> *Kebble v Gainsford* para 87.

process to make a liquidator an officer of the court. A statutory obligation on the liquidator to act in a fiduciary capacity towards the body of creditors as a whole and to carry out his duties in an independent, impartial and even-handed way will, it is submitted, be more effective in order to regulate the liquidator's conduct.<sup>50</sup>

It is noteworthy that the focus of the liquidator's duties falls squarely on his responsibility to determine assets. Whilst one must concede that this is an important duty, there are other objectives in insolvency which warrant consideration. One such duty is the need to investigate the cause of the failure of a company. Calitz<sup>51</sup> notes the following in this regard:

Another disparity that one notices when examining the functions of the Master within the context of international standards is the lack of investigative powers of the Master relating to the cause of the insolvency. In most foreign jurisdictions the examination into the cause of insolvency, which also includes the behaviour of the insolvent prior to the sequestration of his estate, represents a major objective in the justification of these regulatory institutions. Customarily, the investigative process of insolvency law is also established as a public policy measure. Although the South African system hosts a strong interrogation procedure, the investigative powers of the Master are limited to the general enquiries afforded by the Act, which generally aims to obtain information on the financial affairs of the insolvent and the whereabouts of property. Being able to determine the cause of insolvency not only has the advantage of separating the bona fide insolvent from the person abusing the system, but in the context of law reform will also have substantial scientific and empirical value.<sup>52</sup>

## **2.6 Sanctions against a liquidator**

Should the liquidator fail to perform his duties or comply with a reasonable demand by the Master for information or proof required by him in connection with the liquidation of the company, the Master or any person having an interest in the company, after giving the liquidator at least two weeks' notice, can apply to the Court for an order directing the liquidator to perform such a duty or comply with such a demand.<sup>53</sup> The liquidator runs the risk of having a costs order *de bonis propriis* against him.<sup>54</sup> The liquidator may also be removed by the Master and by the

<sup>50</sup> See Calitz *Reformatory Approach* part VII for a detailed discussion.

<sup>51</sup> Calitz 2011 *De Jure* 290.

<sup>52</sup> Calitz 2011 *De Jure* 299.

<sup>53</sup> Companies Act s 405.

<sup>54</sup> Companies Act s 405(2). See also *Thorn v The Master* 1964 3 SA 38 (N) 52-53.

Court if he has failed to perform any duty imposed upon him satisfactorily or to comply with a lawful demand by the Master or if the majority of the creditors (or members in the case of a member's voluntary winding-up) have requested him to do so.<sup>55</sup> A court may, on application by the Master or any interested person, remove a liquidator from office if the Master fails to do so in any of the circumstances mentioned in the act or for any other good cause.<sup>56</sup> It is significant that no action for damages can be brought against a liquidator for failing to do his duties. A liquidator may himself not be questioned in terms of a section 417 procedure.<sup>57</sup>

## **2.7 *The objectives of the section 417 examination***

The essence of section 417 is contained in its purpose, and the purpose of the section in turn justifies its means. Although much can be said about the *sui generis* nature and the far-reaching scope of the examination, every matter concerning section 417 returns to this crucial point, namely the weighing up of perceived injustices against the purpose of the section. In outlining the objectives of the section 417 examination, Levenberg AJ in *Kebble's* case again referred extensively to the matter of *Bernstein*, where Ackerman J summarised the objectives of a section 417 and 418 examination. In *Bernstein* it is noted that the section in particular is aimed at assisting liquidators in achieving their primary goal, namely to determine assets as quickly and cheaply as possible, and to pay the liabilities.<sup>58</sup> Ackerman J further notes that the section confers an ancillary power on liquidators to look into

<sup>55</sup> Companies Act s 379 (1)(b). See also *Standard Bank v The Master*.

<sup>56</sup> Companies Act s 379 (2). In terms of s 379 (2) the court may remove a liquidator from office where there is good cause for removal. Meskin further states that: "'Good cause', in this context, would include, it is submitted, misconduct of any kind not covered by any of the provisions of sections 373 or 379(1) of the Companies Act; but 'cause', it is submitted, should not be confined to misconduct or personal unfitness for office; it includes any conduct which is such that the Court is able to conclude that it would be to the advantage of all the persons interested in the winding-up that the removal should ensue, having regard to the true interests of the winding-up and the purpose for which the liquidator is appointed." (*In re Adam Eyton Limited; Ex parte Charlesworth* 1887 36 Ch 299 (CA) 303-304, 306; *Greenacre's Executors v Kemp* 1916 TPD 247 255; *James v Magistrate Wynberg* 14 and cases there cited; *Standard Bank v The Master* para 10). See also Meskin *et al* *Insolvency Law* para 4.34; Calitz 2011 *Obiter* 747-759.

<sup>57</sup> However, see s 152(2) of the *Insolvency Act*, where the Act also makes provision for an inquiry to be instituted by the Master, whenever he is of the opinion that the insolvent, the trustee, or any other person is able to give information which he (the Master) considers desirable to obtain concerning the insolvent, his estate, the administration of his estate, or any claim or demand made against the estate (s 152(2)). See also Bertelsmann *Mars: Law of Insolvency* 430.

<sup>58</sup> *Bernstein v Bester* para 16.

the company's affairs, to obtain clarity on claims that they wish to pursue, or to determine the general credibility of an examinee before embarking on a trial. The disadvantages faced by liquidators, their lack of knowledge of the company's affairs, their reliance on records which are often inadequately kept, and their dependence on members of the company as sources of information are noted. The list of objectives set out by Ackerman J is not novel, but is a restatement and affirmation of what previous decisions have determined the purpose of the section to be, as discussed further below.

That the purpose of the section is clear and unequivocal is substantiated by the fact that cases have consistently noted the purpose of the section in a similar manner. This was again seen in the very recent matter of *P Nyathi v M P Cloete*,<sup>59</sup> where the court had to consider the purpose of section 417, and in doing so it referred to a number of cases that pronounced on the objects of the section 417. The purpose of this section was variously noted to be the following: to assist officers of the Court in performing their duty to creditors, the Master and the court,<sup>60</sup> to determine the most advantageous course to adopt in regard to the liquidation of the company,<sup>61</sup> to assist the liquidator with the primary goal of winding-up, which is to identify the assets and liabilities and to administer them to the advantage of the creditors,<sup>62</sup> to provide the company with information about its affairs, claims and liabilities which the company's officers fail or refuse to make available,<sup>63</sup> and to piece together information in order to assist the winding-up process.<sup>64</sup> In another recent matter, *Kawie v The Master of the High Court*,<sup>65</sup> it is simply noted that the purpose of the section is to investigate the affairs of the company. The overall tenet of these decisions is that the purpose of section 417 is to obtain information. These recent interpretations of the purposes

<sup>59</sup> *P Nyathi v M P Cloete* 2012 6 SA 631 (GSJ), hereafter referred to as "*Nyathi v Cloete*".

<sup>60</sup> *Lynn v Kreuger* 1995 2 SA 940 (N) 944F.

<sup>61</sup> *Western Bank Ltd v Thorne* 1973 3 SA 661 (C) 666F.

<sup>62</sup> *Merchant Shippers SA (Pty) Ltd v Millman* 1986 1 SA 413 (C) 417D-E.

<sup>63</sup> *Ferreira v Levin; Vryenhoek v Powell* 1996 1 SA 984 (CC).

<sup>64</sup> *Leech v Farber* 2000 2 SA 444 (W) 450J, hereafter referred to as *Leech v Farber*.

<sup>65</sup> *Kawie v The Master of the High Court* unreported case number 21353/2011 WC of 3 November 2011.

of the section have not varied from those noted more than 40 years ago in the English matter of *Re Rolls Razor Ltd*<sup>66</sup> where the following was stated:

The process ... is needed because of the difficulty in which the liquidator in an insolvent company is necessarily placed. He usually comes as a stranger to the affairs of the company which has sunk to its financial doom. In that process, it may well be that some of those concerned in the management of the company, and others as well, have been guilty of some misconduct or impropriety which is of relevance to the liquidation. Even those who were wholly innocent of any wrongdoing may have motives for concealing what was done. In any case there are almost certain to be many transactions which are difficult to discover or to understand merely from the books and papers of the company. Accordingly the Legislator has provided this extra-ordinary process so as to enable the requisite information to be obtained.<sup>67</sup>

## 2.8 **Responsibility to account**

The last purpose of section 417 referred to by Ackerman J in the *Bernstein* matter comprises the responsibility of those who obtain funds from the public to account for how those funds were spent.<sup>68</sup> In another matter, *Ferreira v Levin, Vryenhoek v Powell*,<sup>69</sup> Sachs J stated as follows:

Company directors and other officials who appeal to the public for funds and engage in public commercial activity with the benefit of not being personally liable for company debts, cannot complain if they are subsequently called upon to account for their stewardship... Indeed, it would be ironical if crooked directors were more able to avoid submitting themselves to an examination than honest ones.<sup>70</sup>

Ackerman J's comments raise the question of to whom directors owe a responsibility to account.<sup>71</sup> It appears to be suggested that directors must account to the public or that directors in general must be accountable for their actions. It is trite that a director is accountable only to the shareholders of the company. This position is confirmed in the *Companies Act* 71 of 2008,<sup>72</sup> which prescribes that a director must

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<sup>66</sup> *Re Rolls Razor Ltd* (2) 1970 a Ch 576, hereafter referred to as *Re Rolls Razor Ltd*.

<sup>67</sup> *Nyathi v Cloete* para 591-592.

<sup>68</sup> *Bernstein v Bester* para 85. See also *Mitchell v Hodes* 2003 3 SA 176 (C).

<sup>69</sup> See *Ferreira v Levin*.

<sup>70</sup> *Ferreira v Levin* para 261.

<sup>71</sup> See *Bekink* 2008 *SA Merc LJ* 95; *Feinstein* 2010 *De Rebus* 43; *Du Plessis* 2010 *Acta Juridica* 263; *Van der Linde* 2008 *SA Merc LJ* 439; *Van der Linde* "South Africa".

<sup>72</sup> The new *Companies Act* 71 of 2008 (hereafter referred to as "2008 Act" or "2008 Companies Act") came into effect on 1 May 2011. The winding-up of insolvent companies continue to be regulated - Chapter 14 of the 1973 Act, incorporating provisions of the Insolvency Act, while the

act in the best interests of the company,<sup>73</sup> i.e. the body of shareholders as a whole. The interests of other stakeholders, such as creditors, employees, suppliers, the community and the environment, have received no formal recognition under the new *Companies Act* and the duties of directors are focused on maximising shareholder wealth.<sup>74</sup> Should a director fail in his duties, there are provisions in the new *Companies Act* that will call him to account.<sup>75</sup> A company in existence owes no duties to its creditors. This position naturally changes upon liquidation when the *concurrus creditorum* is established, but at that point the duties of the director have ceased, other than the duties to attend meetings.<sup>76</sup> It is exactly for this reason that the examination in terms of section 417 is of such value, as it is the only means to gain information from a director. It is therefore submitted that Ackerman J's comments on the responsibility of directors to account to the company's affairs refers to a director's duty to attend at enquiries such as the section 417 enquiries.

Furthermore, when one considers the prevailing economic situation it seems crucial to maintain a section such as section 417 in order to counterbalance the prevalence of white-collar crime and fraud in our society. In the *Bernstein* matter, Ackerman J took judicial notice of "the particularly high crime rate...currently prevalent in South Africa", as well as the collapse and liquidation of companies that were of concern to the state, and noted that this gave added weight to the argument that liquidators should act efficiently, quickly and prudently with assets to protect the interests of creditors and the public at large.<sup>77</sup>

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winding-up of solvent companies is addressed in the new Act. Chapter 14, with certain exceptions, continues to apply to the winding-up and liquidation of companies as if the 1973 Act had not been repealed (s 224(3) read with item 9(1) Schedule 5 of the 2008 Act). The chapter is to remain in effect until alternative legislation adequately providing for the winding-up and liquidation of insolvent companies has been put in operation (item 9(4)(a) Schedule 5 of the 2008 Act). However, certain provisions (ss 343, 344, 346 and 348-353) do not apply to solvent companies except to the extent necessary to give full effect to ss 79-83 of the 2008 Act (item 9(2) Schedule 5 of the 2008 Act).

<sup>73</sup> *Companies Act 2008* s 76(3)(b).

<sup>74</sup> Cassim *Contemporary Company Law* 517. See also Luiz and Taljaard 2009 *SA Merc LJ* 420.

<sup>75</sup> The fiduciary duties of directors are derived from our common law, and while the 2008 Act attempts to codify some of these common law duties, it is only a partial codification of the common law. See eg *Companies Act 2008* ss 22 (1); 20(6); 77(3)(b); 77(9) and 218(2).

<sup>76</sup> *Companies Act* s 414(1).

<sup>77</sup> *Bernstein v Bester* para 151.

Again, in the matter of *Mitchell v Hodes*<sup>78</sup> it was highlighted that the honest conduct of companies was a matter of great public concern, requiring the exposure of dishonest conduct, especially since the liquidation is frequently the result of mismanagement involving fraud on the part of the directors and other officers of the company.<sup>79</sup> These persons are often the only ones to have details of the pre-liquidation business affairs of the company. It is especially in these cases that an exa

## ***2.9 Aspects which safeguard against the abuse of the section***

### *2.9.1 Balance of rights*

Unless the court or, as the case may be, the Master, were to direct otherwise, section 417(7) operates to deny all persons access to the application and any documents accompanying it and to the examination or enquiry itself, the record of it, and to any books or papers produced at it.<sup>80</sup> In *Merchant Shippers SA v Millman*<sup>81</sup> the court stated that there was good reason for the preservation of secrecy, not only with regard to the examination, but also the application for the enquiry. The judge underlined that the motive for the enquiry was to enable the liquidator to seek and recover assets to the advantage of creditors. If the information regarding the application and the matters which were to be inquired were to be made public this would complicate the task of the liquidator considerably.<sup>82</sup>

It is submitted that the balance to be achieved between the giving of the information requested and possible hardship to the examinee goes to the heart of the purpose of section 417. Ackerman J in *Bernstein*, as quoted in the *Kebble*

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<sup>78</sup> *Mitchell v Hodes* (n 69

<sup>79</sup> *Mitchell v Hodes* 48.

<sup>80</sup> Meskin *et al* *Insolvency Law* para 8.5.2 and see *Cordiant Trading CC v Daimler Chrysler Financial Services (Pty) Ltd* 2005 4 SA 389 (D&CLD). Meskin states that "it should be noted that this position may now have changed in light of the provisions of the Promotion of Access to Information Act 2 of 2000 which obliges public and private bodies to make information available in specific circumstances. In terms of s 5 of this Act, its provisions override those of other legislation that prohibits or restricts the disclosure of a record and which is materially inconsistent with an object or specific provision of such Act." Meskin *al* *Insolvency Law* para 8.5.2.

<sup>81</sup> *Merchant Shippers SA v Millman* 1986 1 SA 413 (C).

<sup>82</sup> *Merchant Shippers SA v Millman* 414 G-H.

matter, refers to an English decision, *Cloverbay*,<sup>83</sup> where the Court of Appeal highlighted the balance between the requirements of the liquidator and possible oppression to the person to be examined.<sup>84</sup> The court pointed out that where the information requested is fundamental to the winding-up process, the balance would clearly weigh in favour of an examination, but if the liquidator wanted to merely "dot the i's and cross the t's on a fairly clear claim" the balance would lie against him.<sup>85</sup> Conceding that few cases will be this plainly weighted, it is noted that a court will have to exercise its discretion as to whether or not to order an examination. The court outlined certain guidelines for the exercise of such discretion, as follows:

The first consideration is that the purpose of the provisions is to enable the liquidator to reconstitute the state of knowledge to the company in order to make informed decisions. The purpose is not to place the company in a stronger position in civil litigation than it would have enjoyed in the absence of liquidation. Second, the appropriate strategy is not to require proof of the absolute need for information before an order of examination will be granted, but proof of a reasonable requirement of information. Third, the case for examination would be much stronger against officers or former directors of the company, who owe the company a fiduciary duty, than against third parties. Fourth, an order for oral examination is more likely to operate against an examinee than an order for the production of documents. The court is also likely to treat an application for the holding of a s 417 examination from an office holder, such as the liquidator, with more sympathy than it would treat a similar request from a contributor...<sup>86</sup>

The court concluded by stating that a clear case of abuse had to be established before a discharge from a subpoena could be ordered. As stated above, Kebble failed to establish any abuse. On the contrary, it was found that this was a clear case where an examination was patently indicated, for the reasons set out above in the discussion of the judgment.

Applicants wishing to set aside an order in terms of section 417 must prove that the statutory balance does not protect them properly. It is the Master who determines the relevance of the documents requested and not the party seeking to prevent disclosure.<sup>87</sup> In the *Gumede*<sup>88</sup> matter, where the application was for the production of

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<sup>83</sup> *Cloverbay*.

<sup>84</sup> *Cloverbay* 102a.

<sup>85</sup> *Cloverbay* 102a.

<sup>86</sup> *Kebble v Gainsford* 29.

<sup>87</sup> *Akoo v Master of the High Court* 2012 ZAKZPHC 45 (31 July 2012).

<sup>88</sup> *Gumede v Subel* 2006 3 SA 498 (SCA).

documents, the court held that the relevance of the documents requested trumped the right to privacy.<sup>89</sup> The decision was premised on the balance between the harm to a person summoned to produce books or papers in his custody and the importance of the documents sought.<sup>90</sup>

In *Mitchell's* case the court was dealing with the aspect of self-incrimination.<sup>91</sup> The following was noted regarding the balance between oppression to the examinee and the need to obtain information:

To my mind, the inevitable tension between the rights of an examinee in section 417 proceedings (in particular, the broad right to a fair trial of an examinee who is also an accused person) and the indubitable public interest in the proper examination of corporate collapses, has been adequately and fairly balanced by the Constitutional Court by the introduction of a direct use immunity, and by making the use of derivative evidence at a subsequent criminal trial subject to the discretion of the trial judge (whose duty it is to ensure compliance with fair criminal trial standards).<sup>92</sup>

Direct and derivative use immunity refers to the fact that a witness' own evidence cannot be used against himself or herself, unless such evidence is substantiated independently. This immunity differs from blanket immunity, which is an undertaking not to prosecute the witness. By allowing the use of derivative evidence, flexibility has been retained in that the trial judge may decide whether to admit the evidence or not. It also avoids immunity baths where a witness offers up evidence in order to side-step future prosecution. In terms of section 417(2)(b) any person may be required to answer any question put to him or her at the examination, notwithstanding that the answer may incriminate him or her. A person shall be obliged to answer at the instance of the Master or the Court, provided that the Master or the Court has consulted with the Director of Public Prosecutions who has jurisdiction.<sup>93</sup> Academic writers have criticized the requirement to involve the Director

<sup>89</sup> *Gumede v Subel* 2006 3 SA 498 (SCA) 505.

<sup>90</sup> Calitz 2006 *Obiter* 403- 409.

<sup>91</sup> *Mitchell v Hodes*. Also see *Parboo v Getz* 1997 4 SA 1095 (CC).

<sup>92</sup> *Mitchell v Hodes* 53.

<sup>93</sup> S 417(2)(b) of the *Companies Act* was amended in 2002.

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of Public Prosecutions, on the basis that this may unnecessarily stultify proceedings.<sup>94</sup>

### 2.9.2 Abuse of process

The court has the inherent power, both at common law and in terms of section 173 of the *Constitution*<sup>95</sup> to regulate its own process, including the right to prevent an abuse of its process in the form of frivolous or vexatious litigation.<sup>96</sup> The court can interfere and declare the exercise of power invalid only where it is shown that the repository of the power acted *mala fide* or from ulterior motive or failed to apply his mind to the matter.<sup>97</sup> In evaluating if there is an abuse the court is required to cumulatively weigh up all of the factors both for and against the holding of an examination. Whether there is an abuse or not will in all instances depend on the circumstances of the case. The court thus has the power to prevent the oppressive, vexatious and unfair use of section 417 proceedings.<sup>98</sup> In the matter of *Leech v Farber*,<sup>99</sup> Nugent J stated this unequivocally as follows:

As long as enquiries of this nature have been permitted by legislation in this country, the courts have had the power to intervene in order to supervise the manner in which they have been conducted.<sup>100</sup>

The liquidator must apply his mind in order to determine if a legitimate purpose exists and that sufficient cause is made out for the enquiry to take place. Should he not do so, he runs the risk of the court's declaring that the enquiry amounts to an abuse of process.<sup>101</sup> However, a witness does not have a right to being given a list of questions prior to a section 417 hearing.<sup>102</sup> An opportunity should be given to the witness to consult the documents and to consider a reply, but it is not necessary for

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<sup>94</sup> Meskin *et al* *Insolvency Law* para 5.8.2

<sup>95</sup> *Constitution of the Republic of South Africa*, 1996, hereafter referred to as "the *Constitution*". In terms of s 1(2) of the *Citation of Constitutional Laws Act* 5 of 2005, which came into operation on 27 June 2005, all references to the *Constitution of the Republic of South Africa* Act 108 of 1996 have been replaced by the *Constitution of the Republic of South Africa*, 1996.

<sup>96</sup> *Cassimjee v Minister of Finance* 2012 ZASCA 101 (1 June 2012) para 8.

<sup>97</sup> *Strauss v The Master* 2001 1 SA 649 (T) 657A.

<sup>98</sup> *Bernstein v Bester* 776G.

<sup>99</sup> *Leech v Farber* .

<sup>100</sup> *Leech v Farber* 451C-D.

<sup>101</sup> *Laskarides v German Tyre Centre (Pty) Ltd* 2010 1 SA 390 (W).

<sup>102</sup> *Nyathi v Cloete*.

him to prepare for an enquiry as for an academic examination.<sup>103</sup> Where applicants have averred that the subpoenas issued against them were vague in that they failed to specify the nature of the documents that were required, this was rejected by the court.<sup>104</sup> The mere fact that a variety of documents is required does not mean that the request for documents was vague.

### 2.9.3 *Oral or written interrogatories*

The Master or the Court may examine any person summoned on oath or affirmation concerning any matter referred to in subsection (1), either orally or on written interrogatories and may reduce his answers to writing and require him to sign them.<sup>105</sup> The recent *Nyathi*<sup>106</sup> matter dealt with a review of a decision not to allow the examination of the applicants in an examination in terms of section 417 and 418 by written interrogatory. The applicants further wanted an order setting aside the subpoenas issued in terms of section 417. The court pointed out that it has a discretion whether to proceed by means of an oral interrogation as opposed to a written interrogatory and that there must be good reason for having a written examination rather than an oral examination.<sup>107</sup> The court again referred to the English matter of *Re Rolls Razor Ltd*,<sup>108</sup> where it was held that one must look at the facts as a whole, without yielding to preconceptions.<sup>109</sup> In the *Nyathi* matter it was held that a written interrogatory may be indicated where the information sought is merely formal in nature. In other circumstances, a written interrogatory as a precursor to oral examination may be more suitable.<sup>110</sup> However, one should be disinclined to take the written interrogatory route when this would undermine the object and purpose of the examination, especially where the failure of the company was, on the face of it, caused by the fraudulent actions of the directors.<sup>111</sup> In such instances it would be counterproductive not to get the necessary information from

<sup>103</sup> *Lategan v Lategan* 2003 6 SA 611 (D).

<sup>104</sup> *Nyathi v Cloete*.

<sup>105</sup> S 417 (2A)(a) of the *Companies Act*.

<sup>106</sup> *Nyathi v Cloete*.

<sup>107</sup> *Nyathi v Cloete* para 7.

<sup>108</sup> *Re Rolls Razor Ltd*.

<sup>109</sup> *Re Rolls Razor Ltd* para 6.

<sup>110</sup> *Re Rolls Razor Ltd* para 6. See also *Leech v Faber* 451A-B.

<sup>111</sup> The court referred to the matter of *Lynn v Krueger* 1995 2 SA 940 944F-I.

the directors themselves, as quickly as possible, as they may be the only sources of information as to the pre-liquidation affairs of the company. In the *Nyathi* matter there was a typical absence of information, a lack of financial documents and information of the insolvent company, and a lack of co-operation from the directors. So little persuaded was the court that the application in the *Nyathi* matter was "ill conceived" that costs on a punitive scale were awarded against the applicants.

In the Draft *Insolvency Bill*,<sup>112</sup> clauses 417 and 418 have been retained in clause 65 and 66. *Van der Linde and Boraine*<sup>113</sup> note that the provisions of the draft bill are similar to sections 417 and 418 of the *Companies Act*, with certain innovations. One such novelty is found in clause 67, which empowers the liquidator to put written questions to the insolvent, creditors and other witnesses. Answers to such questions are treated as evidence given at an interrogation. The authors note that this procedure should save time and money.<sup>114</sup> In response to their viewpoint, reference is made to the *Nyathi* decision discussed above, where the court noted that written interrogatories are not appropriate in all cases and that there is a risk that necessary information which could be elicited by means of oral evidence may not be exposed.

#### 2.9.4 Conclusion

It can be seen that section 417 must be interpreted in order to give effect to the liquidator's duties, namely to determine and realize as many assets as possible and to assist the Master to expose any offences, to determine if directors are to be disqualified, and to determine the cause of failure of the company, where applicable. It is significant that the courts give the duty to collect assets more weight than any of the liquidator's other duties. In the *Kebble* matter the court raised the point that directors should have a duty to account to the public, but it is submitted that the main focus of the liquidator remains to collect and distribute assets. The wide discretion that the court has in terms of section 417 is balanced by a weighing of the interests of the parties and the fact that the court will not allow an abuse of process.

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<sup>112</sup> SALC *Review of the Law of Insolvency* (Volume 2) Draft Bill.

<sup>113</sup> Boraine and Van der Linde 1999 *TSAR* 38.

<sup>114</sup> Boraine and Van der Linde 1999 *TSAR* 45.

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It is important not to place too many checks and balances in a procedure based on discretion, as this may counter the very effectiveness of the section.

### **3 Comparison with English law**

#### **3.1 Introduction**

This part contains the comparative aspect of the study and takes a concise look at the English provision for private examinations, namely section 236 of the *Insolvency Act*, 1986.<sup>115</sup> As has been noted above, South African insolvency law has a strong link to English insolvency law, as is evidenced by the seminal English cases that are still referred to and relied on by our courts, including the Constitutional Court, in reaching their decisions.

#### **3.2 Section 236 of the *Insolvency Act* 1986**

Section 236 of the *Insolvency Act*, 1986<sup>116</sup> regulates private examinations. According to this section the court may, on the application of the office holder, summon to appear before it any officer of the company, any person known or suspected to have in his possession any property of the company or supposed to be indebted to the company or any person whom the court thinks capable of giving information concerning the promotion, formation, business, dealings, affairs or property of the company.<sup>117</sup> "Office holder" means the administrator, the administrative receiver, the liquidator or provisional liquidator,<sup>118</sup> but also has an extended meaning to include the official receiver.<sup>119</sup> For *Rajak* the most striking feature of the section is the fact

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<sup>115</sup> For the purpose of clarifying nomenclature it should be noted that English insolvency law makes provision for a number of regimes, including voluntary winding-up, winding-up by court, receivership, administration and voluntary arrangements, with the result that the insolvency practitioner may be variously referred to as an administrative receiver, administrator, nominee or supervisor, liquidator or provisional liquidator, the office holder, official receiver etc. I have not reduced these varying terms to a standard terminology such as "the practitioner", but have reproduced the nomenclature used in the act, the case or the text that I refer to without alteration.

<sup>116</sup> Hereafter referred to as the "*Insolvency Act*, 1986".

<sup>117</sup> *Insolvency Act*, 1986 s 234 (2).

<sup>118</sup> *Insolvency Act*, 1986 s 234 (1).

<sup>119</sup> *Re Pantmaenog Timber Co Ltd* 2004 1 AC 158.

that anyone can be summoned under it, provided that person is capable of giving information concerning the affairs of the company.<sup>120</sup>

The onus of proving that the information is reasonably required rests on the office holder. His burden is eased by the fact that the court regards the views of the office holder with "a good deal of weight".<sup>121</sup> Factors which are relevant are the stage of the insolvency process, the importance of the information required and the purpose for which it is required, the proximity of the relationship between the respondent and the insolvent, whether the order is for an oral examination or an order to produce documents, self-incrimination, and the entitlement of a respondent to documents.<sup>122</sup> Finch notes that the power to examine is not designed to offer liquidators special advantages in ordinary litigation and should not be used oppressively.<sup>123</sup>

### ***3.3 Scope of the application***

The scope of section 236 is premised upon the discretion of the court. *Sealy and Milman* comment that the court's discretion under section 236 is unfettered,<sup>124</sup> yet circumscribed by the overriding requirements that the examination should be necessary in the interests of winding-up, and that it should not be oppressive or unfair to the respondent.<sup>125</sup> It has been noted that, in view of the fact that the legislature saw fit to award a discretion to the court in respect of private enquiries, it would be counterproductive to classify all the occasions upon which it may be proper to make an order.<sup>126</sup> The section has been held to be very useful and as such it was unnecessary and undesirable to limit its scope.<sup>127</sup> A principal authority on the scope of section 236 is the decision of the House of Lords in *British & Commonwealth*

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<sup>120</sup> Rajak Company Liquidations 307.

<sup>121</sup> Sasea Finance Ltd v KPMG 1998 BCC 216 220. See Finch *Corporate Insolvency Law* 565.

<sup>122</sup> *Re Pantmaenog Timber Co Ltd* 2004 1 AC 158.

<sup>123</sup> Finch *Corporate Insolvency Law* 565, where reference is made to the matter of *Re Embassy Art Products Ltd* 1987 3 BCC 292.

<sup>124</sup> Possibly referring to the judgment in *In re Rolls Razor Ltd* 592, where reference was made to "the unfettered discretion of the judge brought to bear upon any exercise of this extraordinary jurisdiction". See *Sealy and Milman Annotated Guide* 258.

<sup>125</sup> *Sealy and Milman Annotated Guide* 259.

<sup>126</sup> *In re North Australian Territory Co* 1890 45 ChD 87 92.

<sup>127</sup> *In re Highgrade Trades Ltd* 1984 BCLC 151 177.

*Holdings plc v Spicer and Oppenheim.*<sup>128</sup> In this case very extensive information had been requested and the respondents objected to the wide terms of the order, claiming this to be oppressive.<sup>129</sup> The main issue for the court to decide was if the jurisdiction under section 236 was limited to make provision for such information as would have been available to the company but for its insolvency, based on the "reconstitution of knowledge" argument.<sup>130</sup> It was accepted that at least some of the information requested was information that the company would not have been entitled to. In the principal judgment it was held that there was no such limitation in jurisdiction and no rule establishing such a limitation had been held down in the decision of *Cloverbay*.<sup>131</sup> *Mayson* noted that the court has the power to order the production of books, papers and records relating to the company even if they are not in the company's property and the company itself could not have obtained them.<sup>132</sup> The scope of the section is such that it can be used even against an official receiver himself, as noted by *Rajak* with reference to the case of *Re John T. Rhodes Ltd*,<sup>133</sup> namely that the receiver is liable to be summoned to appear before the court to provide an account of his dealings as receiver.<sup>134</sup>

<sup>128</sup> British and Commonwealth Holdings plc v Spicer and Oppenheim 1993 AC 426, hereafter referred as "British and Commonwealth Holdings".

<sup>129</sup> This summary of the *British and Commonwealth Holdings* matter is included in the judgment of *Cowlishaw v O & D Building Contractors Ltd* 2009 EWHC 2445 (Ch).

<sup>130</sup> It was also held in the case of *Cowlishaw and Wong v O & D Building Contractors Ltd* 2009 EWHC 2445 (Ch) that the court's power of private examination is wide and can include any person the court thinks is capable of providing information regarding the company's promotion, formation, business, dealings, affairs and property. In *In re Highgrade Trades Ltd* 1984 BCAC 151, Oliver LJ in relation to s 268 said, at para 177: "the jurisdiction is a most useful one, and I certainly do not wish to say, and it is unnecessary to say, anything which would limit its scope". In *In re John T Rhodes Ltd* 1986 2 BCC 99,284, 286, Hoffmann J again emphasised the discretionary nature of an order made under s 561 of the *Companies Act*, 1985, the successor of s 268 of the Act of 1948.

<sup>131</sup> *Cloverbay*.

<sup>132</sup> French, Mayson and Ryan *Company Law* 747 referring to *Re Trading Partners Ltd* 2002 1 BCAC 655.

<sup>133</sup> *In re John T Rhodes Ltd* 1986 2 BCC 99.

<sup>134</sup> *Rajak Company Liquidations* 338.

### **3.4 Purpose of the examination**

The case of *British and Commonwealth Holdings*<sup>135</sup> addressed the purpose of the section 236 examination.<sup>136</sup> The court approved the dictum of Buckley J in *In Re Rolls Razor Ltd*<sup>137</sup> to the effect that the purpose of the section is to obtain information that the liquidator, as a stranger to the company, may not be privy to.<sup>138</sup> The dictum of Buckley J was also referred to in the *Kebble* matter and is quoted above and will therefore not be repeated here. In summary, the purposes of the section as set out in the *In re Rolls* matter are as follows: to assist the office holder to "discover the truth", so that he complete his function as effectively and with little expense as possible, to put the affairs of the insolvent estate in order, to identify and recover assets and to discover facts surrounding potential claims, including claims against the potential respondent to the application. In the *British & Commonwealth*<sup>139</sup> matter counsel for the appellants summarized the purpose of the section as follows:

The office holder faces the obvious difficulty or disadvantage that he is a stranger to the company's affairs. This is the "mischief" at which section 236 is aimed: the section overcomes the difficulty or disadvantage by allowing the office holder to acquire (cheaply and, if appropriate, quickly) the knowledge that the company over which is he is appointed should possess. The section remedies disadvantage rather than confers advantage.<sup>140</sup>

The above quotation is included here, as it is submitted that the formulation by counsel to the effect that section 236 does not confer additional advantages to a liquidator but rather redresses an imbalance that exists due to the fact that the liquidator is a stranger to the company aids our understanding of the true purpose of section 236.

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<sup>135</sup> British and Commonwealth Holdings.

<sup>136</sup> Fletcher *Law of Insolvency* 575.

<sup>137</sup> *In re Rolls Razor Ltd*.

<sup>138</sup> Fletcher *Law of Insolvency* 575.

<sup>139</sup> British and Commonwealth Holdings.

<sup>140</sup> British and Commonwealth Holdings 428.

*Goode* identifies the objectives of English corporate insolvency law as restoring the company to profitable trading, maximising returns to creditors, providing a fair and equitable system for the ranking of claims, identifying the causes of the company's failure, and imposing sanctions for culpable management by its directors and officers.<sup>141</sup> What can thus be added to the purposes of section 236 discussed above is the aim of obtaining evidence for use in directors' disqualification proceedings. This aspect is addressed more fully below under the discussion of the duties of the official receiver.

### ***3.5 Duties of the official receiver***

An official receiver's duties are not confined to the determination of the assets of the company, but include an investigation of the affairs of the company.<sup>142</sup> Mayson notes that a person who is appointed as a practitioner in a company insolvency is usually unfamiliar with the company but must take charge of it very quickly, and the legislation therefore makes several provisions for information about the company to be provided to the practitioner.<sup>143</sup> One such provision is section 131 of the *Insolvency Act*. In terms of this provision the official receiver may require a person to submit a statement as to the affairs of the company.<sup>144</sup> The official receiver has the duty to investigate if the company has failed and also to investigate more generally the promotion, formation, business, dealings and affairs of the company and to make such a report as he thinks fit.<sup>145</sup> The official receiver has a discretion as to whether to submit a report or not, and if his investigation reveals no misconduct a report may be dispensed with.<sup>146</sup> However, if he does submit a report, it may play a significant part in proceedings under the *Company Directors Disqualification Act, 1986*,<sup>147</sup> alternatively proceedings in terms of the *Insolvency Act, 1986* concerning wrongful

<sup>141</sup> *Goode Principles of Corporate Insolvency Law* 59-63.

<sup>142</sup> *Insolvency Act, 1986* s 132. See Fletcher *Law of Insolvency* 707.

<sup>143</sup> French, Mayson and Ryan *Company Law* 744.

<sup>144</sup> *Insolvency Act, 1986* s 131. Such a person can be an officer, employee or former employee of the company. The particulars that can be requested include particulars of the company's assets and liabilities, the names and addresses of the company's creditors, the securities held by the creditors and such further information as the official receiver may require.

<sup>145</sup> *Insolvency Act, 1986* s 132.

<sup>146</sup> Fletcher *Law of Insolvency* 452.

<sup>147</sup> Hereafter referred to as "Company Directors Disqualification Act".

trading, dispositions without value, voidable preferences, extortionate credit transactions or proceedings for remedies against delinquent directors.<sup>148</sup> *Goode* points out that the insolvency of a company affects creditors, employees and the Government, which loses out on taxes and, accordingly, insolvency law imposes an obligation on liquidators to investigate the cause of failure of a company and the imposition of applicable sanctions.<sup>149</sup>

### **3.6 *Section 235 of the Insolvency Act 1986***

The official receiver is assisted in his duty by section 235 of the *Insolvency Act*, 1986, which creates a duty to co-operate with the office-holder.<sup>150</sup> This section notes that each person mentioned in section 236 shall give to the office holder such information concerning the company and its affairs or property as the office holder may reasonably require, failing which a fine may be imposed.<sup>151</sup> No prescribed procedure is required in terms of section 235 and the office holder may merely contact the relevant person requesting his attendance or the information that he requires.<sup>152</sup>

In the matter of *RGB Resources plc*<sup>153</sup> it was held that section 236 should be read together with section 235, but it noted that section 235 contained a mandatory obligation on an officer to give the information reasonably required, whereas the court retained a discretion to order a private examination under section 236.<sup>154</sup> Section 236 is wider reaching in scope than section 235 as it can be used to obtain

<sup>148</sup> Fletcher Law of Insolvency 716.

<sup>149</sup> Goode Principles of Corporate Insolvency Law 62.

<sup>150</sup> Fletcher Law of Insolvency 712.

<sup>151</sup> *Insolvency Act*, 1986 s 235 (2). S 235 (3) notes that the persons referred to are those who are or have at any time been officers of the company, those who have taken part in the formation of the company at any time within one year before the date on which the company entered administration, those who are in the employment of the company (or another company), or have been in its employment (including employment under a contract for services) within that year, and are in the office holder's opinion capable of giving information which he requires and in the case of a company being wound up by the court, any person who has acted as the administrator, administrative receiver or liquidator of the company.

<sup>152</sup> Robinson Date Unknown <http://www.practicallaw.com/5-521-0528>.

<sup>153</sup> *Re RGB Resources plc* 2002 EWHC 1612 (Ch).

<sup>154</sup> *Re RGB Resources plc* 2002 EWHC 1612 (Ch). See also *Official Receiver (Appellant) v Wadge Rapps and Hunt (a Firm) and Two Other Actions* 2003 UKHL 49 paras 36- 38.

documents and information from persons outside the company, such as bank officials. Office holders are encouraged to make use of section 235. For example, in the *Re Embassy Art Products Ltd*<sup>155</sup> matter it was held oppressive to seek the production of documents in wide terms without having made any attempt to obtain the information by letter or by any other means in the first place.<sup>156</sup>

### **3.7 The Insolvency Service**

The insolvency practitioner does not act alone in the execution of his duties, but is regulated by The Insolvency Service, which is an executive agency within the Department for Business, Innovation and Skills.<sup>157</sup> The Insolvency Service's functions include the authorisation and regulation of the insolvency profession, dealing with the disqualification of unfit directors, and providing information to the public when necessary.<sup>158</sup> There is also a Companies Investigations Branch which conducts confidential investigations into companies where it is in the public interest to do so.

### **3.8 The Company Directors Disqualification Act**

Although no mention is made of the *Directors Disqualification Act* in section 236 of the *Insolvency Act*, 1986, these two measures should be read together.<sup>159</sup> In the *Pantmaenog*<sup>160</sup> matter the court pointed out that there is a close and important link between section 236(3) of the *Insolvency Act*, 1986 and section 7(3) of the *Companies Directors Disqualification Act* and referred to the matter of *Re Polly Peck International plc*,<sup>161</sup> where it was stated that the purposes of the liquidation, administration or receivership, as the case may be, must include the gathering of information as to the conduct of the affairs of the company and those responsible for it in order that the office-holder can report to the Secretary of State as he is

<sup>155</sup> *Re Embassy Art Products Ltd* 1987 3 BCC 292.

<sup>156</sup> *Re Embassy Art Products Ltd* 1987 3 BCC 299.

<sup>157</sup> The Insolvency Service, an executive agency of the Department for Business, Innovation and Skills, mainly acts as the interface between government and the various stakeholders in insolvency law, and although the decisive responsibility rests with the Secretary of State for the Department for Business, Innovation and Skills, the routine responsibility for the supervision and control of the insolvency system is delegated to the Insolvency Service.

<sup>158</sup> Goode Principles of Corporate Insolvency Law 27.

<sup>159</sup> *Re Pantmaenog Timber Co Ltd* 49.

<sup>160</sup> *Re Pantmaenog Timber Co Ltd* 49.

<sup>161</sup> *Re Polly Peck International plc* 1994 BCC 15, 16 A-B.

required to do by section 7(3) of the *Companies Directors Disqualification Act*.<sup>162</sup> The court concludes that these provisions are complementary to each other. Information obtained under section 236 may be of use for more than one purpose and the section should therefore not be interpreted narrowly.

### **3.9 Protection of the public interest and balancing interests**

The case of *Re Pantmaenog Timber Co Ltd*<sup>163</sup> introduces a further issue relevant to section 236, namely the public interest aspect of insolvencies. The court emphasized that the liquidator serves a public interest and not merely the financial interest of the creditors and contributors. The court referred to the report of the Cork Committee,<sup>164</sup> which observed that "The law of insolvency takes the form of a compact to which there are three parties: the debtor, his creditors and society".<sup>165</sup> As a result, the court pointed out, insolvency proceedings are not treated in English law as an exclusively private matter between the debtor and his creditor, as the interest of the community must be taken into account.<sup>166</sup>

Keay defines public interest as those interests which society has a regard for and which are wider than the interests of those parties directly involved in an insolvent matter.<sup>167</sup> He submits, however, that it is difficult to define the concept of the public interest and that there is no general consensus as to what the public interest involves. He concludes that it should not be assumed that the interests of the debtor and the creditors take preference over the public interest, nor should one say that the public interest is paramount. The correct approach is to consider all interests in each case, and to engage in a careful balancing exercise to determine which interests, based on the facts, should be preferred.<sup>168</sup> Keay highlights the basic issues relating to interaction between the public interest and insolvency law and states the following:

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<sup>162</sup> Fletcher *The Law of Insolvency* 716.

<sup>163</sup> *Re Pantmaenog Timber Co Ltd*.

<sup>164</sup> Review Committee, *Insolvency Law and Practice*, Cmnd 8558 (1982) - the "Cork Report".

<sup>165</sup> Review Committee para 192.

<sup>166</sup> *Pantmaenog Timber Co Ltd* para 52.

<sup>167</sup> Keay 2000 *NILQ* 509.

<sup>168</sup> Keay 2000 *NILQ* 580.

It is possible to divide instances where the public interest is a factor in insolvency law into three very broad categories. First, it is in the public interest that insolvencies are resolved in an orderly and expeditious way. Second, it is in the public interest to ensure that commercial morality is enforced, so as, *inter alia*, to prevent fraud and improper practices.<sup>169</sup>

This balance of interests is necessary to counter the wide discretion of the court in matters arising from section 236.<sup>170</sup> It has been held that the court must be astute to prevent any oppressive, vexatious or unfair use of the section.<sup>171</sup> The court must balance the needs of the liquidators with the potential oppression to the individuals.

In *Re Castle New Homes Ltd*<sup>172</sup> the court put it thus:

The court will always be concerned to avoid vexation, oppression or injustice in making an order under section 236. If the evidence shows that the purpose of a litigator in seeking the examination is to achieve an advantage beyond that available to the ordinary litigant, in litigation which he has already commenced or which he has definitely decided to commence, the predisposition of the court may well be to refuse an immediate order for examination, unless the liquidator can show special grounds to the contrary. If, however, it appears from the evidence that the object of the liquidator is simply to elicit information that will enable or assist him to decide whether or not his company has a valid claim against a third party, the court will approach the liquidator's application with no such predisposition. While it will still be anxious in such a case to avoid oppression, it will also bear in mind that one of the very purposes of section [236] is to enable the liquidator 'as effectively as possible and...with as little expense as possible and with as much expedition as possible... to complete his function as liquidator...; and that to assist him in this may inevitably involve giving him a degree of advantage which would not be available to an ordinary potential litigant.<sup>173</sup>

The above passage was quoted with approval in the matter of *Cloverbay*.<sup>174</sup> The court in *Re British and Commonwealth Holdings* also listed certain factors to be borne in mind when exercising the discretion.<sup>175</sup> However, the court expressly excluded the factor that the purpose of section 236 was for the office holder to get sufficient knowledge and information to reconstitute the state of knowledge that the company should possess. The court was of the opinion that no limitation to the reconstitution of the company's state of knowledge exists, as was envisaged in

<sup>169</sup> Keay 2000 *NILQ* 509. See also Keay 2001 *Anglo-American LR* 209.

<sup>170</sup> Fletcher *Law of Insolvency* 709.

<sup>171</sup> *In re Rolls Razor Ltd* 700.

<sup>172</sup> *Re Castle New Homes Ltd* 1979 1 WLR 1075.

<sup>173</sup> *Re Castle New Homes Ltd* 1979 1 WLR 1090.

<sup>174</sup> *Cloverbay* 102.

<sup>175</sup> Fletcher *Law of Insolvency* 710.

*Cloverbay*.<sup>176</sup> In *Cowlishaw v O & D Building Contractors Ltd* the court's discretion under section 236 was restrained, as the unfairness to the respondent in producing the documents outweighed the benefit to the liquidator of obtaining the documents.<sup>177</sup>

### **3.10 Conclusion**

It is evident that insolvencies in England are strictly regulated. The Insolvency Service, a governmental agency created by statute, oversees the process. Although rooted in statute, the process is scaffolded by recognized professional bodies, rules, regulations, codes of ethics, statements of insolvency practice and insolvency guidance papers. The *Insolvency Act*, 1986 and the *Disqualification Act* are intended to work together and this shows that the focus of insolvencies in English law is wider than the determination of assets. The liquidator serves a public interest and does not represent only the creditors and contributories. Public interest is a nebulous concept which is better left undefined. The directors are under a statutory duty to assist the process by providing such information as the office holder may require. The private examination procedure is seen as a procedure of last resort and the office holder is expected to attempt to obtain information by any other means in the first instance. The court prevents oppressive, vexatious and unfair use of the section by balancing the needs of the office holder against the rights of the respondent.

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<sup>176</sup> Fletcher *Law of Insolvency* 711.

<sup>177</sup> *Cowlishaw v O & D Building Contractors Ltd* 2009 EWHC 2445 (Ch). In this matter the respondents were concerned that the administrator's true purpose was to obtain the documents so that they could be sold to a buyer as a part of a package to sell the development. It was submitted on their behalf that it was an abuse of the procedure under s 236 to seek from them the "fruits of their labours". The court found this to be a valid objection.

## 4 Summary and recommendations

### 4.1 Comparison between the South African and the English procedures

The scope of application of a private examination is very wide.<sup>178</sup> In both South Africa and England the procedure is unavailable in voluntary insolvency. In England the procedure is available in all other forms of insolvency, whereas the South African section refers to cases where a company is unable to pay its debts. This restriction is being eroded by our courts and has been made applicable to a company which was wound up on the basis that it was just and equitable to do so.<sup>179</sup> The interpretation of the court in doing so is commended and it is submitted that future legislation should do away with the requirement of a company's being "unable to pay its debts". As stated by the court in *Huang*, liquidators in all cases of winding-up face similar problems, and there appears to be no rational basis to make a procedure available to only certain types of winding-up. This interpretation is not an extension of the section beyond its original intention and as such should be countenanced.

The Master or the Court can instigate the procedure in South Africa on the assumption that there are instances where a secret examination without recourse to the court would benefit the winding-up process.<sup>180</sup> In terms of English law, the procedure can be instigated only by the court, and the office holder applies to the court to commence a private enquiry. In the interests of certainty, some thought needs to be given to the personae that are empowered to instigate a private examination in South African law. This matter is addressed below under the heading of "Reform". It is submitted that the private examination, premised as it is on discretion and balance, is one that is best confined to the court's examination.

Both the English and the South African systems view the private examination as an extraordinary procedure of a *sui generis* nature, where the examination is

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<sup>178</sup> See *Botha v Strydom* 1992 2 SA 155 (N) 159G-I; *Jeeva v Receiver of Revenue, Port Elizabeth* 1995 2 SA 433 (SE) A-B.

<sup>179</sup> Also see O'Brien 2002 *TSAR* 736, where it is envisaged that the restriction of s 236 to instances where company is "unable to pay its debts" should be revisited.

<sup>180</sup> Section 417 of the *Companies Act* notes that the Master or the court may summon a person for an examination.

inquisitorial and the ordinary standards of trial procedure are not applicable. Both systems make use of discretion in order to balance the rights of examinees against the need for information.

In South African law the private examination is part of the administration process. In English law it is held to be oppressive to proceed with a statutory examination if information or documentation has not been requested informally by letter or other means. English law therefore envisages that a statutory examination be seen as a last resort. Furthermore, although the procedure under section 236 is sometimes referred to as a "private examination" the court may make a range of other orders, including the production of witness statements or documents. It is submitted that the insolvency process in South Africa will be enhanced by an adoption of the English approach. This is discussed more fully under "Reform" below.

The general duties of the liquidator in South African law and an office holder under English law coincide in that both of them have the duty of recovering the assets of the company, paying the creditors, and distributing the surplus (if any) to the persons entitled to it. In English law the duties of an office holder are wider, including the duty to investigate the causes of a company's failure, to expose offences and to report on the grounds for recommending the disqualification of a director. This is an area where South African law is deficient, as discussed more fully below.

The liquidator is probably not an officer of the court in South African law, but what is more important is that the liquidator is seen to be independent and impartial in his dealings.<sup>181</sup> It is submitted that a statutory obligation on the liquidator to act in a fiduciary capacity towards the body of creditors as a whole will give clarity and credence to his position. This matter is therefore discussed under "Reform" below. The insolvency practitioner is an officer of the court in the England, but there no evident benefit in following this practice in South African law.

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<sup>181</sup> See para 2.5 above.

Sanctions against the liquidator include an order by the Court for the liquidator to comply with a reasonable demand by the Master. The liquidator may also be removed by the Master and by the court, or by a majority of creditors, if he has not performed his duties satisfactorily. No action for damages can be brought against a liquidator for failing to do his duties. In English law, insolvency practitioners belong to one of the regulated bodies and these bodies may issue disciplinary orders against their members. These bodies can also withdraw a practitioner's insolvency licence on the basis that the practitioner is no longer a fit and proper person to perform the functions of a liquidator.

#### **4.2 *Recommendations***

From the above discussion it can be seen that certain aspects pertaining to private examinations are ideal and should not be altered, such as the wide discretion of the court and the balance to be achieved between the rights of examinees and the needs of liquidators. Others are adequate, such as the provision for legal representation and access to information. Suggestions for reform are related to the following aspects of the private examination: who may instigate a private examination, using a public examination as a last resort, putting supportive measures and structures into place in order to scaffold the statutory foundation, encoding the fiduciary duties of liquidators, and extending the focus of a private examination.

##### *4.2.1 Who may instigate a private examination?*

In South Africa a private examination may be commenced by the Master or the Court. The Master's office is overburdened with duties. With particular reference to private examinations, the delegation of functions to a commissioner recognizes that the Master and the court are in need of assistance. It is submitted that delegation to a commissioner is treating the symptoms rather than eradicating the root of the problem. Instead of extending the power to instigate a private examination to the Master, and then attempting to ease his burden by making provision for delegation, it is submitted that a more realistic solution would be to limit the involvement of the Master altogether. In order to expand on this point of view, it is necessary to briefly

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consider reform to insolvency law in general, with reference to recent corporate reform in South Africa.

As already stated, insolvency law in South Africa has long been waiting its turn for reformative legislation. Recent years have seen the creation of a new corporate dispensation with the coming into being of the new *Companies Act* 71 of 2008, which also introduced a new business rescue regime. With the development of company law, policy considerations have come into play, such as providing a "clear, facilitating, predictable and consistently enforced law" and "a protective and fertile environment for economic activity".<sup>182</sup> Five points of economic growth were identified, namely enterprise development, promoting investment, making companies more efficient, encouraging transparency and high standards of governance, and following best practice jurisdictions internationally.<sup>183</sup> Goal statements in reviewing corporate law included simplification, flexibility, efficiency, transparency and predictability. It is submitted that the same policy considerations and goals are applicable to corporate insolvency law and should similarly be adopted.

In accordance with the policy of emulating best practice jurisdictions, one may look to English insolvency law, which has close links with South African insolvency law and which has seen extensive reform, for guidance. In England insolvency is regulated by an organ of state, namely the Insolvency Service. It is submitted that the appointment of an independent body to regulate insolvency law is required in South Africa as well required.<sup>184</sup> A local example of such a regulatory body is the National Credit Regulator,<sup>185</sup> which is responsible for the regulation of the South African credit industry. The National Credit Regulator has the task of education, research, policy development, the registration of industry participants, the investigation of complaints, and ensuring the enforcement of the *National Credit Act*.<sup>186</sup> The establishment of a statutory regulatory body tasked with the supervision

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<sup>182</sup> Memorandum on the objects of the *Companies Bill*, 2008 para 1.

<sup>183</sup> Memorandum on the objects of the *Companies Bill*, 2008 para 1.

<sup>184</sup> See Calitz *Reformatory Approach* ch 7.

<sup>185</sup> Established by the *National Credit Act* 34 of 2005.

<sup>186</sup> [www.ncr.org.za](http://www.ncr.org.za).

of the insolvency industry, with the duties of education, research, policy development, the registration of insolvency practitioners, investigation and enforcement would result in increased clarity, predictability, and confidence in the system. With particular reference to private examinations, the insolvency practitioner, an appropriately qualified individual, should in applicable instances be empowered to apply to court to instigate a private examination. It is important, though, that this should occur only at the point where all else has failed.

#### *4.2.2 The public examination as a last resort*

The English interpretation of the private examination as an expedient to be adopted as a last resort is commendable, and South African law may benefit from incorporating a similar approach. Emphasis should be placed on the informal examination of persons who may assist in the liquidation process and the statutory duties of directors to assist in the liquidation process should be underscored. A leaning towards this approach is found in the Johannesburg bar practice manual, which notes that when an application is made to examine a particular witness, it must be shown that the witness in question has refused to furnish the information required of him or is otherwise unwilling to cooperate with the liquidator.<sup>187</sup>

#### *4.2.3 Supportive measures*

Sufficient supportive measures should be included in the new insolvency regime to bolster the insolvency practitioner in his duties. This is another instance where English law may assist reform in the South African context. Augmenting strategies employed by the English system include complementary legislation such as the *Director's Disqualification Act*, 1986, which has its own body of investigation and enforcement. The procedure in terms of English law appears to be more a more effective way of policing the behaviour of directors. In English law, further, the Insolvency Service appoints official receivers to investigate the affairs of companies in compulsory liquidation to establish the reasons for the insolvency and report on

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<sup>187</sup> Johannesburg Bar practice manual of the South Gauteng High Court 10.8.

misconduct.<sup>188</sup> Furthermore, for grave offences there is the Serious Fraud Office, that investigates and prosecutes serious or complex fraud or corruption.

#### *4.2.4 Statutory statement of the fiduciary duties of a liquidator*

Our courts have highlighted the need for a liquidator to be independent and impartial and to act in a fiduciary capacity towards creditors and the company.<sup>189</sup> Again, it is useful to have regard to the recent innovations in company law in this regard. One of the novel aspects introduced by the act is the fact that it includes a statutory statement of the fiduciary duties of directors. The act includes "standards of directors' conduct"<sup>190</sup> in terms of which a director must exercise his powers and functions in good faith and for a proper purpose,<sup>191</sup> in the bests interests of the company,<sup>192</sup> and with the degree of care, skill and diligence that may reasonably be expected of him.<sup>193</sup> If a director breaches his fiduciary duties, he can be held liable in accordance with the principles of the common law<sup>194</sup> or in terms of delict for any loss, damages or costs as a consequence of a breach of care, skill and diligence. These duties are mandatory, prescriptive and unalterable. They apply to all companies, and directors cannot contract out of these duties.<sup>195</sup> Cassim notes that their object is to raise the standards of corporate and directorial behaviour.<sup>196</sup>

It is submitted that a similar approach may be adopted in order to regulate the duties of a liquidator, namely a statutory statement of duties that will make these duties more clear and accessible. A codification or statutory statement of duties

<sup>188</sup> The Insolvency Service also investigates persons in bankruptcy.

<sup>189</sup> See paras 2.4.-2.5 above.

<sup>190</sup> *Companies Act, 2008* s 76.

<sup>191</sup> *Companies Act, 2008* s 76(3)(a).

<sup>192</sup> *Companies Act, 2008* s 76(3)(b).

<sup>193</sup> *Companies Act, 2008* s 76(3)(c).

<sup>194</sup> *Companies Act, 2008* s 77.

<sup>195</sup> Cassim Contemporary Company Law 507.

<sup>196</sup> The statutory fiduciary duties are extended to a business rescue practitioner in terms of the business rescue proceedings contained in Ch 6 of the new *Companies Act*, by virtue of the fact that a business rescue practitioner, during rescue proceedings, has the responsibilities, duties and liabilities of a director of the company, as set out in ss 75 to 77 of the *Companies Act, 2008*. In addition, the business rescue practitioner may be held liable in accordance with any relevant law for the consequences of any act or omission amounting to gross negligence in the exercise of the powers and performance of the functions of practitioner, although he is not liable for any act or omission made in good faith in the course of the exercise of his powers and the performance of his functions (s 140(3)(c)).

would likewise have the object of raising the standard of behaviour of insolvency practitioners and would provide a predictable and effective environment for the efficient discharge of a practitioner's duties. These duties should be mandatory and unalterable. In the English system there is a structure of interwoven rules, regulations, codes and guidelines which augment the statutory basis of the insolvency law. This system of certainty, transparency, accessibility and predictability is one that should be emulated in our law.

#### *4.2.5 Extending the focus of the liquidator's duties*

A significant difference in focus between the South African and English systems is the fact that the official receiver is tasked with the duty not only to determine and realize the assets of the insolvent company, but also to investigate and report on the cause of the failure of the company. In South Africa the overarching purpose of the section has consistently been interpreted by our courts as being for the acquisition of information. South African insolvency law would be enhanced if the focus of the examination were to be extended to include an investigation into the cause of the failure of the company. There is a greater awareness of the interdependence between companies and the society in which they function, and there should be an increased responsibility in the insolvency process on the reasons why companies have failed.

### **4.3 Conclusion**

In conclusion, it is submitted that far from being draconian, it is vital that section 417 be retained in a new insolvency regime. The accessibility of the section to liquidators, the inquisitorial nature of the proceedings, the wide scope of the section and the effective sanctions should examinees not comply together combine to make a formula that has over the years proved impervious to circumvention. The sheer regularity with which private examinations are sought to be challenged in our courts is indicative of the effectiveness of the section. It is hard not to draw the inference

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that it is particularly those with something to hide that are mostly desirous to evade the examination. The court in *Podlas*<sup>197</sup> put it thus:

It is difficult to see why an insolvent who has made a clean breast and has nothing to hide should shirk an interrogation such as the one the applicant objects to... A person who is sequestered effectively sacrifices his or her right to privacy in regard to, at the least, pre-sequestration patrimonial matters. The rights of a creditor enjoy preference over those of an insolvent...<sup>198</sup>

It is submitted that this section must remain part of our future insolvency legislation as it fulfills its function with prudent efficiency. This submission is strengthened by the fact that the Constitutional Court, after careful consideration, has kept sections 417 and 418 wholly intact,<sup>199</sup> with the exception of those parts that infringed on the rule of self-incrimination. Recommendations have been made in this article on aspects where the section may be enhanced by reform. In part, these recommendations rely on the premise that South African insolvency law *in toto* is desperately in need of an overhaul. Meaningful reform will include a re-evaluation of the Master's role, widening the scope of the liquidator's duties, and making it obligatory for liquidators to act honestly and impartially. Such measures will bring certainty and credibility which will hopefully help to counterbalance the resistance to the "draconian" private enquiry.

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<sup>197</sup> *Podlas v Bryden* 1994 4 SA 662 (T).

<sup>198</sup> *Podlas v Bryden* 1994 4 SA 662 (T), which dealt with a private examination in terms of s 152 of the *Insolvency Act*.

<sup>199</sup> See fn 113, 114.

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**LIST OF ABBREVIATIONS**

Anglo-American LR	Anglo-American Law Review
NILQ	North Ireland Legal Quarterly
SALC	South African Law Commission
SA Merc LJ	South African Mercantile Law Journal
TSAR	Tydskrif vir die Suid-Afrikaanse Reg

## TO BE OR NOT TO BE? THE ROLE OF PRIVATE ENQUIRIES IN THE SOUTH AFRICAN INSOLVENCY LAW

**Y Joubert\***

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### SUMMARY

This article analyses the role of the so-called private examinations in our South African insolvency law and deals with the question of whether or not section 417 of the Insolvency Act (Act 24 of 1936) is adequately and effectively framed in order to fulfil its intended purpose in South African law. The contribution also points out that although the scrutiny of private examinations is not novel; it is argued that further exploration of the subject is justified by virtue of the fact that robust and innovative legislative changes have been experienced in the South African corporate landscape. Although the section has already passed the test of lawfulness and constitutionality, the aim is to ascertain whether the section serves a legitimate purpose and is essential and relevant in a democratic society. This is done by considering the South African law relating to South African private examinations and includes academic texts and judicial interpretation. Both section 417 of the Companies Act (Act 61 of 1973) and the matter of *Kebble v Gainsford* in particular are discussed. A brief comparative analysis of a similar provision in the Insolvency Act of the United Kingdom (UK), namely section 236 of the Insolvency Act 1986 is also included.

Finally recommendations are made on aspects where the section may be enhanced by reform which in part relies on the premise that South African insolvency law *in toto* is desperately in need of an overhaul. The article concludes that it is vital that section 417 be retained in a new insolvency regime as there is a greater awareness of the interdependence between companies and the society in which they function, and it is submitted that there should be an increased responsibility in the insolvency

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process on the reasons why companies have failed. The accessibility of the section to practitioners, the inquisitorial nature of the proceedings, the wide scope of the section and the effective sanctions should examinees not comply together combine to make a formula that has over the years proved impervious to circumvention and it therefore fulfils its function with prudent efficiency.

**KEYWORDS:** Insolvency law; liquidation; section 417 of Companies Act 61 of 1973; private examinations; constitutional; constitutional court cases; balance of rights; abuse of process; *concursus creditorum*; oral or written interrogatories; Insolvency Act 1986; official receiver.