REPUBLIC OF SOUTH AFRICA

IN THE HIGH COURT OF SOUTH AFRICA
GAUTENG LOCAL DIVISION, JOHANNESBURG

CASE NO: 11588/2015

(1) REPORTABLE: YES / NO
(2) OF INTEREST TO OTHER JUDGES: YES/NO
(3) REVISED.

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DATE SIGNATURE

In the matter between:

DURO PRESSINGS (PTY) LTD (IN LIQUIDATION)	First Applicant
SUMAIYA ABDOOL GAFAAR KHAMMISSA N.O.	Second Applicant
CHRISTIAAN FREDERIK DE WET N.O.	Third Applicant
DESIRE JUDITH MASEGE N.O.	Fourth Applicant
BERTHUEL BILLYBOY MAHLATSI N.O.	Fifth Applicant
GURWANTRAI LAXMAN BHIKHA N.O.	Sixth Applicant

And

MERCANTILE BANK LIMITED	Respondent

J U D G M E N T

KEIGHTLEY J:

[1] There are two applications before me. The main application, which I deal with first, and then an application by the respondent for a special order of costs against the applicants in the event of the latters' application being dismissed.

THE MAIN APPLICATION

[2] The first applicant in this matter is a company called Duro Pressings (Pty) Ltd ("Duro"), which is currently in liquidation. It is common cause that Duro was placed in voluntary liquidation on 5 March 2014. On that date the special resolution placing the company in voluntary liquidation was registered, and this became the date on which the winding-up of the company commenced.

[3] Second to sixth applicants are the final liquidators who were appointed by the Master on 8 April 2014. I shall refer to them simply as "the liquidators".

[4] The respondent is Mercantile Bank Limited ("Mercantile"). Duro held a number of accounts with Mercantile, including a current account through which Duro accessed and operated an overdraft facility extended to it by Mercantile. This account was referred to in the proceedings simply as "account 59". It forms the core of the present dispute between the parties.

[5] The liquidators originally sought the following relief from this court:

[5.1] a declarator to the effect that the payments made by Mercantile out of and debited against account 59 over the period 6 March 2014 to 27 August 2014 in the aggregate sum of R155 749 722. 05 were unauthorised;

[5.2] a declarator to the effect that these payments and debits were unlawful; and

[5.3] an order directing Mercantile to credit account 59 with the sum of R155 749 722. 05, alternatively to pay such sum into Duro's estate account.

[6] After a dispute was raised by Mercantile in its answering affidavit regarding the accuracy of the amount identified in the original notice of motion, the liquidators amended their relief. They did so by substituting the lesser amount of R152 424 947. 04 for the original amount of R155 749 722. 05 cited in the Notice of Motion.

[7] Although this appears to indicate a relatively small change in respect of the monetary value attached to the relief sought by the liquidators, in substance it has greater significance for the issues in dispute in this matter.

[8] It is common cause that the amount now reflected in the notice of motion represents the sum total of three payments, or, in one case, a category of payments, made into account 59 after the commencement of Duro's winding up. These are:

[8.1] on the 18 March 2014 an amount of R58 million;

[8.2] on the same date, an amount of R78 million; and

[8.3] between 5 March 2014 and 27 August 2014, a total amount of R16 424 947.04, from “incoming debtors”.

[9] It is also common cause that these amounts were subsequently disbursed from account 59 by Mercantile. It did so without reference to or authorisation from the Master or the liquidators.

[10] The effect of the amendment to the notice of motion is that it focuses the dispute on these three payments. The question before me is whether Mercantile’s disbursement of these particular amounts from account 59 post the setting in of the *concursus creditorum* in Duro’s estate, and without authorisation, was unlawful.

[11] The liquidators’ case is a simple one, relying on the basic principles underlying the law of insolvency. In short, they submit that:

[11.1] Prior to 5 March 2014, and in terms of the banker customer relationship that existed between Mercantile and Duro, Mercantile was authorised to transact on account 59 on Duro’s behalf.

[11.2] However, on 5 March 2014 the *concursus creditorum* set in. This meant that by operation of law Mercantile’s authority to transact on account 59 was terminated.

[11.3] From that date Mercantile was not permitted to do anything in respect of account 59 without authorisation from the Master or the liquidators.

[11.4] In particular, Mercantile could not unilaterally transact on account 59. It did so in defiance of the *concursus creditorum*, and the law of insolvency.

[11.5] If Mercantile asserted an entitlement to money standing to the credit of account 59 its proper recourse was to follow the path prescribed for all creditors under insolvency law, viz. to submit and prove a claim against the estate.

[11.6] Mercantile did not do so. Instead, it resorted to unlawful self-help of funds standing to the credit of account 59.

[11.7] On this basis, Mercantile must be ordered to return the funds to account 59 so that the liquidators may properly deal with them for the benefit of all creditors in accordance with insolvency due process.

[12] There was no dispute between the parties as to the general principles relied on by the liquidators as the basis for their relief.

[13] However, what is in dispute is whether, when applied to the facts of this case, these principles support the liquidators' claim. As I will indicate in more detail below, the answer to this question depends in large measure on the events that took place between Mercantile and Duro shortly before the critical date

of 5 March 2014. These events provide the context within which the disputed amounts were paid into, and subsequently disbursed from account 59.

[14] The relevant facts in this regard are largely undisputed.

[15] The relationship between Mercantile and Duro commenced in June 2012 when Duro applied for a current account (account 59). At the same time, Mercantile granted Duro certain facilities, as recorded in successive facility letters. The final letter was granted in October 2013. It provided Dura with, among other facilities, an overdraft of R100 million, a medium term loan of R35 million, asset based finance of R20,7 million and bank guarantees of R4,2 million. These facilities were operated through account 59.

[16] The facilities came with an obligation on Duro to provide security to Mercantile. The security took the form of a deed of cession in respect of Duro's book debts as continuing covering security for the payment by Duro of all sums owing or which may have becoming owing to Mercantile. The written cession was concluded on 1 June 2012.

[17] On 31 August 2012, Duro registered a notarial special and general covering bond ("the bond") in favour of Mercantile. In terms of the bond, Duro acknowledged its indebtedness to Mercantile. It bound and hypothecated its movable assets listed in an annexure to the bond, as well as all its movable property of every description, as security for the full amount of Duro's indebtedness to Mercantile.

[18] The bond also gave Mercantile the right, on Duro's breach, forthwith, and without notice, among other things, to claim the full amount of Duro's

indebtedness to Mercantile, to take possession of and retain all Duro's movable assets, and to sell or dispose of them in such manner as Mercantile should decide, and to pass title to the relevant purchasers or transferees.

[19] In addition, and as further security under the bond, Duro ceded all its claims, rights of action and receivables to the bank. It undertook on demand by Mercantile to take all such steps as may be necessary to enable Mercantile to enforce its rights under the bond. It gave Mercantile the entitlement to notify all debtors of the cession, and to demand and receive all amounts owing by the debtors.

[20] On 20 February 2014 Duro's indebtedness to Mercantile amounted to over R144 million. From a meeting held between Duro and Mercantile, the latter learnt for the first time that Duro was in dire financial straits and that its main shareholder had sold its shareholding and withdrawn its support to the company.

[21] Mercantile concluded from this state of affairs that Duro was in default of its obligations to the bank, and it instructed its attorney (on 20 February 2014) to take steps to perfect its security in terms of the bond. This is not disputed.

[22] Mercantile also avers in its answering affidavit that on the same date it further instructed its attorney to take steps to block Duro's access to account 59. The liquidators place this in dispute. In fact, one of the main issues in dispute on the papers filed by both sides was the issue of whether Mercantile had "terminated" account 59, and the banker customer relationship with Duro, prior to 5 March 2014 or not. The liquidators contend that account 59 was

not terminated, and that Mercantile continued to operate the account and to honour amounts drawn on it. I will deal with this issue in more detail later. For reasons that will become apparent, my view is that this particular issue is not determinative of the matter before me.

[23] A number of events took place on the following day, being 21 February 2014.

[24] Mercantile hand delivered a letter to Duro giving it notice of its breach, demanding immediate re-payment of all outstanding balances due to Mercantile, and recording that Mercantile would take steps to exercise its rights to recover the amounts due.

[25] There is some dispute as to whether this letter also amounted to notice of termination of Duro's access to account 59, and of the banker customer relationship. The liquidator's say that it did not constitute such termination. As I have already indicated, ultimately this is not an issue of material importance to the question before me.

[26] On the same day, Duro's board of directors adopted a resolution in terms of which it approved "*the voluntary surrender by it of all its assets subject to the General Notarial Bond and Special Bond … in favour of (Mercantile) required for the purposes of enabling the Bank to perfect its security rights under such Bonds*."

[27] In addition, it signed an agreement with Mercantile, which the parties referred to as the "perfection agreement". The relevant parts of this agreement were as follows:

[27.1] Duro acknowledged its indebtedness to Mercantile for the outstanding amounts due;

[27.2] it acknowledged its breach of the facilities afforded to it by Mercantile, and that Mercantile had called up the facilities;

[27.3] Duro acknowledged the bond;

[27.4] Duro agreed to that in order to perfect the bond, and to give effect to its terms and conditions, it handed over, transferred and delivered all its movables to Mercantile;

[27.5] Duro further authorised Mercantile to sell the movables and to reimburse itself for all amounts in respect of which Duro was indebted to it, and to account to Duro for any balance, if any;

[27.6] in addition, it ceded all its right, title and interest in its debtors to Mercantile, and authorised Mercantile to collect them;

[27.7] Duro expressly recorded its agreement and acceptance that the bond was perfected.

[28] The liquidators do not dispute that the parties entered into the perfection agreement, or the terms thereof.

[29] The liquidators also do not dispute that on 21 February 2014 Mercantile perfected its security in terms of the bond by taking possession of Duro's movables, and that it commenced collecting Duro's book debts from this date.

[30] It is also common cause that two further, related events occurred on 21 February 2014.

[31] First, Mercantile entered into an "Offer to Purchase agreement" with an entity called Chello Trading 653 (Pty) Ltd ("Chello" and the "Chello agreement"). In terms of the Chello agreement, Chello offered to purchase "the Assets" from Mercantile for an amount of R78 million. The "*Assets"* were defined as being *"the Assets which under-lie (sic) the Securities*" held by Mercantile against Duro.

[32] It was a condition precedent to the Chello agreement that Mercantile obtain perfection of the assets purchased under the agreement. At first, the perfection was required to be by a process of court, but this was amended on 24 February 2014 to remove the reference to perfection by way of court process, and to record that perfection in terms of an agreement between Dura and Mercantile would be sufficient. A further amendment on 11 March 2014 recorded that perfection had taken place.

[33] The liquidators made something of the fact that the latter amendment took place after the effective winding-up date. In my view, this is not a material issue. The 11 March amendment simply records that there had been perfection. It does not provide that the date of perfection was the date of the amendment. In addition, the liquidators did not dispute the perfection agreement, which expressly recorded that there had been perfection, nor did they dispute that on 21 February Mercantile took possession of the movables in pursuance of the perfection of its security. In my view, the undisputed facts indicate that perfection occurred prior to 5 March 2014. On this basis,

Mercantile is correct in its assertion that this condition precedent to the Chello agreement was fulfilled.

[34] The second relevant condition precedent in the Chello agreement required an entity called Southern Palace 265 (Pty) Ltd ("Southern Palace") to obtain a facility in the amount of no less than R136 million.

[35] The second related event on 21 February 2014 was a similar agreement entered into between Mercantile and an entity call Finair Trading 612 (Pty) Ltd ("Finair" and the "Finair agreement"). In terms of this agreement, Finair offered to purchase the book debts ceded by Duro to Mercantile for an amount of R58 million.

[36] The Finair agreement was subject to the same condition precedent that applied in respect of Southern Palace being afforded a facility as recorded in the Chello agreement.

[37] The two agreements were each made conditional on the other being concluded.

[38] Mercantile points out that the amount of the facility that Southern Palace was to obtain (as a condition precedent) was the total of the purchase prices stipulated in the two agreements with Chello and Finair. Mercantile asserts that on 26 February 2014 it approved a facility to Southern Palace of R136 million. This is not disputed by the liquidators.

[39] It is common cause that the two contested amounts paid into account 59 on 18 March 2014 of R78 million and R58 million were the payments effected on

behalf of Chello and Finair in compliance with their obligations under the these two agreements.

[40] It is also common cause that the remaining amount of R16 424 947. 04 credited to account 59 from 5 March to 27 August 2014 was the sum total of the amounts collected from Duro's debtors.

[41] Finally, in this regard, it is common cause that the liquidators subsequently sought and were provided with a legal opinion to the effect that the Chello and Finair agreements were lawful. The liquidators resolved to abide by the agreements, and they agreed to ratify the perfection of Mercantile's rights under the bond. There is some dispute as to the effect of this election by the liquidators. However, I do not need resolve to that dispute.

[42] Having set out the relevant factual matrix of the dispute I turn to consider and apply the legal principles to the facts.

[43] Ordinarily, a bank has no entitlement to deal with amounts standing to the credit of its customer's account post the effective date of that customer's winding up. This is a trite principle arising out of the confluence between the legal nature of the banker customer relationship and the law of insolvency.

[44] In our law the legal nature of the banker customer relationship may be described as follows:

"*the relationship … is one of debtor and creditor. When a customer deposits money it becomes that of the bank, subject to the bank's obligation to honour cheques validly drawn by the customer*".[1]

[45] In other words, in general the customer has a personal right enforceable against the bank to demand that monies standing to the customer's credit be disbursed on the customer's instructions. This personal right forms part of the customer's general estate.

[46] The effect of a winding-up order is to establish a *concursus creditorum*. What this means is that:

"*… 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. The claim of each creditor must be dealt with as it existed as at the issue of the order.*"[2]

[47] It follows from these principles that as from the setting in of the *concursus creditorum* <u>any personal rights held by a debtor against his or her banker in relation to amounts standing to the debtor's credit</u> would be subject to the "hand of the law", and the banker would have no right to deal with those amounts without the authority of the liquidator. My reason for emphasising what I have underlined will become apparent shortly.

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1 *S v Kearney* 1964 (2) SA 495 (A) at 502H-503A, citing *Baylis' Trustee v Cape of Good Hope Bank*, 4 S.C. 439 at 422; *Duba and Others v Ketsikile and Others* 1924 EDL 332 at 341 and *R v Stanbridge* 1959 (3) SA 274 (C) at 278-9

2 *Walker v Syfret N.O.* 1911 AD 141 at 166

[48] The liquidators rely on these basic principles as the basis for their case. The initial main point of contention between the parties was on the question of whether Mercantile had actually terminated account 59, and the banker customer relationship between it and Duro on 21 February as it asserted. Mercantile contended that it had terminated the relationship on that date, as well as the facility. Furthermore, it contended that it had continued to use account 59 for its own administrative purposes.

[49] Understandably, the liquidators took issue with these contentions. They submitted that the termination of the facility did not equate to the termination of the account itself. Critical to the liquidator's case in this regard was the assertion that for so long as account 59 remained operative and received credits, Mercantile was precluded by law from dealing with those credits without the authority of the Master or the liquidators.

[50] As the hearing progressed before me, it became apparent that the issue of whether the account and/or the banker customer relationship had been terminated was something of a red herring, masking the true nature of the dispute between the parties.

[51] In Mercantile's answering affidavit, it asserted that the amounts of R78 million and R58 million paid into account 59 were payments made in settlement of the purchase prices paid under the Chello and Finair agreements. It also asserted that Duro had no right to these funds.

[52] Mercantile further averred that the amount of R16 424 947. 04 credited to account 59 from 5 March to 27 August 2014 was received from Duro's

debtors. It had received these payments on behalf of and as agent for Finair, under the Finair agreement, and that these amounts were transferred out of account 59 to Finair. Mercantile went further and averred that having ceded its book debts to the bank, Duro had no entitlement to these monies either.

[53] The liquidators did not dispute the provenance of these disputed payments. What they disputed in their replying affidavit was Mercantile's authority, or rather lack thereof, to deal with any credits standing in account 59 as from the 5 March 2014.

[54] Implicit in the liquidators' stance is the proposition that a customer may assert a claim against the bank in respect of all monies standing to the credit of his or her bank account, and, further, the related proposition that only the customer may assert that claim. However, these propositions do not find support in our jurisprudence. In *Joint Stock Company Varvarinskoye v Absa Bank Ltd*[3] and Others, the Supreme Court of Appeal held that:

> "*It is not correct, as contended for on behalf of Absa, that it is a universal and inflexible rule that only an account holder may assert a claim to money held in its account.*"[4]

[55] The court referred to the case of *McEwen N.O. v Hansa*[5] in which the Appellant Division had determined the right to claim against a credit balance of a bank account on the basis of the intention of the parties involved, rather than on the basis of whom the holder of the account was. In that case, the

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3 2008 (4) SA 287 (SCA)
4 At para 31
5 1968 (1) SA 465 (A)

AD found that there had never been any intention of the account holder acquiring these rights (to the credit balance in his account), and that they accordingly did not vest in his insolvent estate. The court in *Joint Ventures* concluded that:

> "*The funds in an account may also 'belong' to someone other than the account holder or, for that matter the bank or institution holding the money.*"[6]

[56] From this it follows that the present dispute between the parties cannot be resolved by the simple expedient of assuming that because Duro was the account holder, it had a personal claim against the bank for all credits standing to that account. The real question is whether Duro had any right, enforceable against Mercantile, to the credit amounts placed in dispute in this case. If Duro did, then those rights fell within its estate, and they were subject to the *concursus creditorum*. If, on the other hand, Duro did not have a claim to those disputed amounts standing to the credit of account 59, then they did not fall within Duro's estate on liquidation and were not subject to the *concursus creditorum*.

[57] For this reason, it is not necessary for me to resolve the issue of whether the banker customer relationship between Duro and Mercantile was terminated, or whether account 59 was terminated. It is extraneous to the dispute properly conceived.

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6 At para 33

[58] As I have already indicated, there is no dispute that the three contested amounts claimed by the liquidators related to the Chello and Finair agreements.

[59] Mercantile's case is that in the perfection agreement Duro agreed to Mercantile perfecting its rights of security in Duro's movable assets and in the cession and collection of Duro's book debts. Further, Duro specifically agreed that Mercantile was entitled to sell or otherwise transfer the assets and book debts.

[60] Acting on this, Mercantile submits that it proceeded to exercise its real rights of security by selling the movable assets underlying the notarial bond to Chello, and by ceding the book debts to Finair. This took place prior to 5 March 2014.

[61] It is so that payment of the amounts due under each agreement was only made into account 59 on 18 March 2014, and that the book debts were collected into that account until 27 August 2014. However, Mercantile contends that this does not make any difference. Duro had divested itself of all its interests in its secured assets and book debts on 21 February, and it had no further interest in the amounts received under the Chello and Finair agreements. Mercantile says that in terms of these agreements, the right to the two capital payments vested in Mercantile, and the right to the book debts collected vested in Finair.

[62] Mr Gautschi for the liquidators accepted in principle that if Duro had divested itself of its rights in these amounts prior to the winding up date, then it had no

further interest in them and they would not fall under the liquidators' control. He agreed that in the present case this depended on what the parties had intended when they entered into the perfection agreement and the Chello and Finair agreements.

[63] He submitted that the perfection agreement did not constitute an out and out divestment by Duro of its rights in its secured assets and book debts. Instead, Mr Gautschi submitted that what the parties really intended by the perfection agreement, and then by the Chello and Finair agreements was to enter into a new security arrangement. In terms of this arrangement, the parties intended that the capital amounts paid under the latter two agreements were to act as security for Duro's debt to Mercantile in place of the movables and book debts.

[64] In other words, it was submitted on behalf of the liquidators that Chello did not purchase the secured assets, and Finair did not take an out and out cession of the book debts. As such, Duro retained an interest in the contested amounts paid into account 59, as these were supposed to be held as security by Mercantile. On this basis, Mr Gautschi submitted that these amounts fell within Duro's estate, and under the control of the liquidators.

[65] There are a number of difficulties with Mr Gautschi's submissions. In the first instance, both parties accepted in their affidavits that in terms of the perfection agreement Duro gave Mercantile the unqualified right to sell the assets for its own account and to collect Duro's book debts. The liquidators did not suggest in their affidavits that the perfection agreement should be read as being in the nature of a further security arrangement, rather than

what it plainly appeared to be, viz. an acceptance by Duro that it had breached its facility obligations and that it accepted Mercantile's entitlement to act on its existing rights of security under the bond and to proceed to exercise those rights against the secured assets and book debts.

[66] Furthermore, the liquidators did not take issue in their affidavits with Mercantile's averment that in terms of the Chello agreement Chello "*purchased all of the assets secured in terms of the bond*". Nor did it dispute that in terms of the Finair agreement Mercantile "*sold the ceded book debts to Finair*" (emphases added).

[67] In their supporting affidavits the liquidators took issue with Mercantile's authority to deal with any credits in account 59, but they did not take issue with the origin of the three contested amounts. Nor did they take issue with the contested amounts being the proceeds of what were, on the face of it, sale and purchase agreements, post perfection, between Mercantile, on the one hand, and Chello and Finair on the other, in respect of the assets secured under the bond.

[68] The terms of the Chello and Finair agreements are by and large clear. The agreements were concluded between Chello and Finair as the "offerrors" under each agreement respectively, and Mercantile as the "offerree". They were expressly designated as "options to purchase" agreements. The Chello agreement records that Mercantile has taken security against Duro's assets, that it intends to perfect its security and to sell the assets. It further records that Chello is desirous of purchasing, and offers to purchase the assets from Mercantile for the sum of R78 million.

[69] The Finair agreement records that Mercantile has taken cession and pledge of Duro's debtors book, and that Finair is desirous of purchasing and taking cession of the debtors book from Mercantile. On this basis, the agreement records Finair's offer to purchase the debtors book and associated rights for the sum of R58 million.

[70] Mr Gautschi pointed to various aspects of the Chello and Finair agreements that suggested, he submitted, that the agreements were intended to be in the nature of further security arrangements rather than being in the nature of a purchase and sale of the assets and book debts. It is so that questions may be raised as to the purpose of one or two terms in the agreements, for example, the warranties given in clauses 4.1 of the Chello and Finair agreements. However, in my view these questions are not sufficient to dislodge the express and clear terms of both of these agreements, read with the perfection agreement. In terms of the latter, Duro divested itself of its rights in its assets and book debts to Mercantile. The Chello and Finair agreements in turn are characterized as being in the nature of a divestment by Mercantile of its rights in the assets and book debts to Chello and Finair.

[71] Neither party annexes any other agreement to their papers as evidence of a further security arrangement between Duro and Mercantile indicating that Duro and Mercantile intended that the amounts paid under the Chello and Finair agreements were to be held by Mercantile as a new form of security, and that Duro retained a right over the amounts so paid.

[72] For these reasons, I am unable to accept the submissions made by Mr Gautschi in oral argument before me.

[73] On the facts set out in the affidavits before me, I conclude that the effect of the perfection agreement was that Duro divested itself of its rights and interests in the assets and book debts provided as security to Mercantile. It agreed that Mercantile could alienate the assets and book debts for its own account, subject to Mercantile accounting to Duro for any excess recovered.

[74] In terms of the Chello and Finair agreements, Mercantile proceeded to sell the secured assets and book debts to these two entities for its own account. It did not do so on behalf of Duro. It acted in pursuance of the rights it acquired firstly under the bond, and secondly under the perfection agreement. These events took place prior to 5 March 2014. The effect of the perfection agreement, followed by the Chello and Finair agreements, is that Duro divested itself of any interest in the proceeds of its secured assets and book debts prior to its winding up.

[75] Accordingly, despite the fact that the two capital amounts of R78 million and R58 million were paid into account 59 after the winding up and setting in of the *concursus creditorum*, Duro no longer had any claim to the credit arising out of these payments. The interest in these credits lay with Mercantile, flowing from the Chello and Finair agreements. Similarly, Duro had no claim to the amounts paid in by debtors between 5 March and 27 August 2014. The interest in these amounts vested in Finair, which had purchased the book debts prior to 5 March 2014.

[76] Consequently, I conclude that the three contested payments into account 59 did not form part of Duro's estate, and hence fell outside the authority and

control of the liquidator. It follows that the liquidators have failed to establish their case for the relief set out in the amended Notice of Motion.

[77] I stress that the present dispute only concerns the three identified contested payments. The liquidators have reserved their rights regarding the payments and disbursements represented by the difference between the original amount claimed in the Notice of Motion, and the subsequently amended amount, that I discussed earlier. I make no finding on any other amounts paid into, or disbursed from, account 59. Whether other amounts may have been lawfully disbursed by Mercantile without the authorisation of the liquidators will depend on the facts relevant to them. I have not been asked to rule on them. The fate of any additional payments and disbursements must await further litigation, should the liquidators decide to follow that path.

THE APPLICATION FOR A SPECIAL ORDER AS TO COSTS

[78] The only question remaining is that of costs.

[79] It is trite that in our law the question of costs is a matter for determination at the discretion of the court, and that this discretion must be judicially exercised.

[80] Ordinarily costs follow the event, and the successful litigant is entitled to be indemnified by way of a costs order in its favour against the expense of having to institute or defend the proceedings in question.[7]

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7 *Texas Co (SA) Ltd v Cape Town Municipality* 1926 AD 467 at 488

[81] However, in this matter Mercantile asks for something more. It has filed an application for a special costs order against the liquidators in their personal capacities, *de bonis propriis*, and on the attorney and client scale.

[82] In terms of our common law, costs orders *de bonis propriis* may be made against trustees or liquidators in circumstances where they act negligently, unreasonably, improperly or *mala fides* in litigating or in opposing litigation on behalf of the insolvent estate.[8] Conduct falling outside of the liquidator's powers or outside of the law does not necessarily amount to unreasonable conduct.[9] A liquidator's conduct must not only be unacceptable, but must also be improper to attract a *de bonis propriis* costs order.[10]

[83] In addition to these well-established principles applying to persons litigating in a representative capacity, our courts have more recently developed the common law to extend their discretion regarding costs so as to enable them to order non-litigants to bear or share in the costs of litigation that they are funding. This follows similar trends in other Commonwealth jurisdictions,[11]

[84] In *Price Waterhouse Coopers Inc and Others v IMF (Australia) Ltd and Another*, the Gauteng Provincial Division granted an order directing the joinder of a non-party who had entered into an agreement with the plaintiff to fund the plaintiff's litigation. The joinder was purely for purposes of enabling

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8 *Caldwell's Trustee v Western Assurance Co* 1919 WLD 146; *Venter v Scott* 1980 (3) SA 988 (O); *Williams Hunt (Vereeniging) Ltd v Slomowitz* 1960 (1) SA 499 (T)

9 *Blou v Lampert & Chipkin* 1972 (2) SA 501 (T) at 507

10 *Cooper v First National Bank of SA Ltd* 2001 (3) SA 705 (SCA) at 717

11 See *Dymocks Franchise Systems (NSW) v Todd and Others* [2005] 4 All ER 195 at 2815; *Arkin v Borchard Lines Ltd* [2005] EWCA Civ 655 paras 23 and 41; *Carborundum Abrasives Ltd v Bank of New Zealand (No 2)* [1992] 3 NZLR 757 (HC)

a possible costs order to be made against the funder at the conclusion of proceedings. In so extending the common law, the court remarked that:

> "*To allow litigants like the applicants to hold funders directly liable for costs could also be considered to be one of the measures that the courts could adopt to counter any possible abuses arising from the recognition of the validity of champertous contracts*."[12]

[85] In *EP Property Projects (Pty) Ltd v Registrar of Deeds, Cape Town and Another, and Four Related Applications*[13] the Western Cape High Court distinguished between "pure funders" and those who may have acquired a personal, financial interest in the outcome of the litigation.

[86] The court took into account that pure funders may play an important role in enabling access to justice for those without their own financial means to litigate. The prospect of an adverse costs order against these types of funders may well have an adverse and unacceptable chilling effect on the right to access to courts for financially disadvantaged litigants. The court recognised the principle laid down in other common-law jurisdictions that it is in the public interest that generally the discretion will not be exercised against pure funders.[14]

[87] However, the court distinguished the case before it on the basis that the non-party in question was clearly funding the litigation with a view to gaining

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12 2013 (6) SA 216 (GNP) at 222E-H
13 2014 (1) SA 141 (WCC)
14 At para 75, citing *Carborandum Abrasives*, above

substantial financial benefit for herself.[15] She was the "real litigant" and had in effect all the rights of a party to the proceedings.[16] The court found that in those circumstances, it would be just that the funder be held jointly and severally liable for any adverse costs order against the party she was funding.

[88] A similar ruling was made in *Scholtz and Another v Merryweather and Others*[17] in which the court ordered that a father be held jointly and severally liable for costs with his son in an application for rescission. The son was the applicant in the rescission application. The basis for the court's order was that the father had funded the litigation and stood to benefit in that if the litigation succeeded, he would no longer have the financial burden of supporting his son.

[89] The case made out by Mercantile in its founding affidavit in the special costs application is based on the discretion to grant a costs order against non-parties who are funding litigation. Their case is as follows:

[89.1] Following requests made by Mercantile to the liquidators regarding the free residue of assets in the estate, and any indemnities that there might be from creditors for the costs of this application, the liquidators informed Mercantile that there was no free residue of assets, but that this situation might change. This was in May 2015.

15 At para 83
16 At para 86
17 2014 (6) SA 90 (WCC)

[89.2] The liquidators also informed Mercantile that two other legal proceedings had been instituted, and that creditors might be liable for section 89 costs.

[89.3] Mercantile says that the liquidators have not informed it of how they are funding the present application, or how they intend settling an adverse costs order.

[89.4] According to Mercantile, it has incurred substantial costs in opposing the application. On the basis of the information provided by the liquidators, it has no prospects of recovering these costs, given the current situation regarding the estate.

[89.5] Mercantile submits that the only reasonable inference from the available facts is that the liquidators or a third party are funding this application in their own capacity and for their own benefit.

[89.6] If the liquidators succeed in the application, and Mercantile is ordered to repay the amount to the estate, Mercantile undoubtedly has a secured claim against the estate. Consequently, it will be entitled to prove its claim and receive payment from the estate of a secured dividend.

[89.7] However, the liquidators stand to benefit personally in this event, in that their fees would be deducted prior to payment being made to Mercantile of its secured dividend.

[89.8] Accordingly, Mercantile submits that there would be no benefit to the general body of creditors even if the liquidators' application

succeeded. Mercantile would receive the balance of all amounts repaid, subject only to deduction of the liquidators' fees.

[89.9] From this, Mercantile says that it must be inferred that the application was not instituted for the benefit of the general body of creditors, but for the benefit of the liquidators. The liquidators are the real litigants, and are controlling the course of the litigation. Their objective is to generate fees for themselves. This is unreasonable and constitutes an abuse of process.

[89.10] Following repeated and detailed requests from Mercantile regarding the funding situation, the liquidators' attorney advised Mercantile that:

> "*I hold instructions to confirm that my clients are neither funding the litigation for their own benefit, nor is somebody else funding it for their own benefit. The application has been instituted to benefit the entire body of creditors.*"

[89.11] Mercantile submits that this response does not deal satisfactorily with the detailed queries made by it in its repeated requests to the liquidators. It says that the liquidators have failed to provide any information to demonstrate that they have the ability to meet an adverse costs order against the insolvent estate.

[90] In answer to the application, the liquidators say the following:

[90.1] Not surprisingly, they deny that they are the rougue, greedy litigators having their own interests at heart as portrayed by Mercantile in its application.

[90.2] They record that there is a large number of proven creditors in the estate.

[90.3] They point out that an inquiry under sections 417 and 418 of the 1973 Companies Act ("the inquiry") commenced in October 2014. The inquiry is funded by the insurer of 35 of Duro's proven creditors.

[90.4] The information gleaned from the inquiry to date (it is not yet completed) provided the basis for the present application against Mercantile.

[90.5] When the liquidators became aware of the facts arising from the inquiry, they felt duty bound to launch the application, as it was clear to them that a claim existed that had reasonable prospects of success. If they had failed to pursue the claim, they could later be accused of dereliction of duty.

[90.6] They aver that there are proved creditors against whom a contribution could be levied to cover Mercantile's costs. A list of proved creditors is annexed to the answering affidavit.

[90.7] The liquidators deny the correctness of Mercantile's contention that it is a foregone conclusion that no benefit will inure to the general body of creditors in the event of a successful application.

They point out that any claim that Mercantile submits against the estate would have to be scrutinised, and subject to further verification and objection processes before it could be accepted.

[90.8] The liquidators also say that the balance of the estate account fluctuates from time to time, and that this means that it is subject to various levels of liquidity, depending on a variety of factors.

[90.9] Finally, the liquidators make an averment that has caused further concern to be expressed by Mercantile. It is as follows:

> "*The process of levying contributions on proven creditors is an arduous and time-consuming one. The liquidators therefore decided to be pragmatic and to fund the interim cash flow required for this application by Christiaan Frederik De Wet, the third applicant. Should, for any reason, this application prove to be unsuccessful, the liquidators and specifically Christiaan Frederik De Wet, the third applicant will recoup the costs of this application from the proven creditors by way of levying a contribution in terms of the Insolvency laws.*" (emphasis added)

[91] In response to this averment, Mercantile submits that the liquidators have essentially admitted to funding the application in their personal capacities. This, it says, constitutes a breach of the liquidators' duties to act independently, and not for their own benefit.[18] It gives the liquidators a personal interest in the litigation, and creates a conflict of interest between

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18 *Standard Bank of SA v The Master of the High Court* 2010 (4) SA 405 (SCA)

the liquidators and the estate. Furthermore, the liquidators have no authority to fund litigation on behalf of the estate, and accordingly, they are acting outside the parameters of the law in doing so.

[92] The question is how I am to exercise my discretion in this case.

[93] I consider first Mercantile's contention that as the liquidators are funders with a personal interest in the litigation I may, and should, exercise my discretion to grant a personal costs order against them.

[94] This case is not on all fours with any of the recent cases in which funders have been held liable, or potentially liable for the costs of litigation. In the cases to which I have referred, there was substantial evidence establishing that the non-litigants were funding the litigation, and on what basis they were doing so. There was also clear evidence indicating that the funders had substantial, direct financial interests in the outcome of the litigation, and that this was the basis for their funding.

[95] The case before me is somewhat different. The liquidators have conceded that one of them is "*fund(ing) the interim cash flow required*" for the application.

[96] Mercantile submits that this is a concession by the liquidators that one of them is funding the application. It submits further that this concession shows that they misled Mercantile and the court by their earlier instructions to the effect that they were not funding the litigation for their own benefit, but for the benefit of the general body of creditors.

[97] I am not sure why the liquidators did not play open cards earlier regarding how the application was being funded. Mercantile would have it that this was because they were trying to cover up their own interest in the application. However, it must also be borne in mind that the litigation has been robust, with both sides standing to win or lose substantial sums. It is not uncommon that in this type of litigation the parties do not play open hands with each other. Was the earlier instruction an attempt to mislead the court? I am not convinced that I can reach this conclusion on what I have before me. The earlier instruction from the liquidators was that they were "not funding the application for their own benefit". They perhaps obfuscated the issue of where the funding was coming from, but what they clearly said was that the application was not for their benefit.

[98] In any event, it is not very clear what the averment in their answering affidavit means. Does it mean that Mr de Wet has put up "cash flow" to date for purposes of ensuring that the application could be prepared and heard, and that his funding is limited to this? It seems to me that this may be the case, but unfortunately the liquidators do not elaborate.

[99] What they do say is that they will recoup the costs of the application from creditor's contributions if the application is not successful. It appears from this that whatever funding Mr de Wet has put up to date, it is not unconditional, and that the intention is that ultimately the proven creditors will be levied for the costs.

[100] As regards the contention that the liquidators have no authority to fund litigation, this does not in and of itself mean that a *de bonis propriis* costs

order should follow. As I pointed out earlier, acting outside a liquidator's authority does not warrant such an order unless in doing so the liquidator acted unreasonably, or improperly, or recklessly or *mala fides*.

[101] In my view, even if I proceed on the assumption that the liquidators are funding the application, the real issue is whether they are doing so out of their personal interest in the litigation, and not in the interests of the general body of creditors. It seems to me that if this can be established, then there may be grounds for the exercise of my discretion to grant a *de bonis propriis* costs order.

[102] In this regard, the principles underlying the exercise of the extended discretion in non-party funding cases recently recognised by our courts overlap to some extent with the established common law principles regarding *de bonis propriis* orders against liquidators. What I mean by this observation is that if it can be established that a liquidator is personally funding litigation on behalf of an insolvent estate for his or her own benefit, and not for the benefit of the general body of creditors, it may well be concluded that this in any event amounts to unreasonable or improper conduct warranting a costs order under the established common-law principles.

[103] Regardless of which approach is taken (the funder-based approach, or the more established improper conduct approach), the fundamental question must be whether the applicant for the special costs order is able to establish that the liquidator in question was motivated by his or her personal interest and not that of the general body of creditors.

[104] Mercantile requests me to draw an inference that this is the case on the basis I described earlier. In their submissions, Mercantile pointed out that the decision to institute the application was made after the liquidators had ratified the perfection of the bond and the Chello and Finair agreements. In other words, according to Mercantile, the liquidators cannot honestly say that there would be any grounds to reject a claim by Mercantile (in the event of the liquidators having succeeded in the application) as they had ratified the agreements upon which the claim was based. This was one of the main bases on which Mercantile submitted that the only reasonable inference to be drawn is that the sole purpose of the application was to ensure fees for the liquidators in their personal capacities.

[105] The concern I have with this contention is that it overlooks the fact that the ratification of the perfection, Chello and Finair agreements took place in early June 2014. It was only subsequent to this (late in June 2014) that an order was granted for the inquiry, and only in October 2014 that the inquiry commenced. As I indicated earlier, the liquidators' case has always been that it was information emanating from the inquiry that led it to launch the application. That inquiry is not yet complete. What this demonstrates is that the ratification of the agreements preceded what the liquidators say was information from the inquiry that raised concerns for them about the validity of those agreements.

[106] According to the liquidators, therefore, in light of facts only known to them subsequently, they had grounds to question whether the ratification had been properly made. Consequently, on the liquidator's case, a secured creditor's

claim by Mercantile following the liquidators' success in this application would not necessarily mean that Mercantile's claim ultimately would be accepted. This is something that needed to be clarified through a court process.

[107] Clearly the liquidators were influenced in their decision to litigate by new information that came to hand as a result of the inquiry. It is important in my view to bear in mind that as liquidators they have a duty to inquire into the affairs of Duro and to recover all its assets and property.[19] This must entail the duty to initiate legal proceedings to recover assets or property, whether tangible or intangible, if there are reasonable prospects of success. To fail to do so may give rise to the criticism that a liquidator acted negligently in attempting to make good a possible claim in favour of the estate.

[108] Although the liquidators did not succeed in the main application, this is not the test. The question is whether they instituted an application that had reasonable prospects of success at that time.

[109] If they did so, then I cannot accept Mercantile's contention that the only reasonable inference to draw is that the liquidators were driven by their own personal interests in launching and following through on the application.

[110] The application was fiercely contested by both sides, with oral argument lasting for longer than one court day. The supporting papers were substantial. The issues raised were not straightforward. They raised complex questions of insolvency law and banking law. Having had to decide the matter, it is plain to me that the liquidators' application had reasonable

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[19] Section 391 of the 1973 Companies Act. See also *Bernstein and Others v Bester and Others NNO* 1996 (2) SA 751 (CC) at para 16

prospects of success when it was launched. This was clearly not a case with no prospects.

[111] Of course, Mercantile's argument is that this is not the issue. The issue is that the liquidators ought to have known (or, more accurately, they in fact knew) that even if the application succeeded, Mercantile would have a secured claim that was unassailable, and that the only persons who really stood to benefit from the application were the liquidators, through the fees they would recoup.

[112] As I have already explained, this ignores the fact that the liquidators were motivated in launching the application by new information emanating from the inquiry which raised questions about the legal validity of the agreements relied on by Mercantile and, consequently, of any claim that Mercantile might have made against the estate based on those agreements.

[113] In these circumstances, and bearing in mind the obligation on the liquidators to act to recover assets in the estate, it would be unreasonable to infer in this case that they were motivated by their own interests in instituting the application rather than the interests of the general body of creditors.

[114] For these reasons, I cannot accept Mercantile's contention that the only reasonable inference to be made from the facts is that the liquidators funded the application for their own personal interest, and that they are the real litigants in the proceedings.

[115] I also cannot conclude that the liquidators acted unreasonably, or *mala fides*, or recklessly or improperly in instituting the application. Duro's debts are

substantial, and there are a number of creditors. The liquidators obtained information indicating that Mercantile had operated account 59 after *concursus creditorum*, and that over R152 million had been received and disbursed from that account without the authority of the liquidators or the Master. In these circumstances, it would have been remiss of the liquidators not to contemplate litigation. It was not unreasonable for them to believe that the application had reasonable prospects of success, or that there were reasonable prospects (despite the earlier ratification) that the general body of creditors would benefit from the litigation. As I have already indicated, had they declined to act, they may well have been criticised for failing to act in the best interests of creditors.

[116] For these reasons, I conclude that Mercantile has not succeeded in establishing a case for the granting of a *de bonis propriis* costs order against the liquidators as requested in their notice of motion.

[117] For sake of completeness, I record that the liquidators sought leave to file a supplementary affidavit, containing new facts, in the application for a special costs order. Mercantile indicated by letter to the court that it would not agree to the affidavit being filed, and that if I was minded to grant leave, it would seek to file an affidavit in response thereto.

[118] In my view, the supplementary affidavit does not take the issue of costs any further. It is in the interests of both parties that the matter be brought to a close without any further, unnecessary time or costs being spent on the dispute. The costs associated with the liquidator's application to file the supplementary affidavit should be borne by them.

[119] I make the following order:

1. The applicant's application is dismissed with costs.

2. The respondent's application for a special costs order is dismissed with costs, save that the applicants are directed to pay the costs associated with their request for leave to file a supplementary affidavit.

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R KEIGHTLEY
JUDGE OF THE HIGH COURT OF SOUTH AFRICA
GAUTENG LOCAL DIVISION, JOHANNESBURG

Date Heard: 22nd February 2016

Date of Judgment: 21st April 2016

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