REPUBLIC OF SOUTH AFRICA

SOUTH GAUTENG HIGH COURT, JOHANNESBURG

CASE NO: 2009/45807

In the matter between:

FREIDLEIN COMPANY (PTY) LTD	Plaintiff
and	
ANDREW WILLIAM SIMAAN	First Defendant
TREVOR ALLAN THOMPSON	Second Defendant
BRISS MATABATHE	Third Defendant

JUDGMENT

KATHREE-SETILOANE, J

[1] The plaintiff, Freidland Company (Pty) Ltd, instituted an action, on 29 October 2009, in which it sought an order that the defendants, in their capacities as directors of Furnex Stores (Pty) Ltd ("Furnex"), be held personally liable for the debts of Furnex to the plaintiff, in terms of section 424 of the Companies Act, No. 61 of 1973 ("the Companies Act"), on the basis that the business of Furnex was being carried on recklessly and/or with intent

to defraud creditors of Furnex, in particular the plaintiff, and/or for fraudulent purposes.

[2] The defendants raised a special plea challenging the *locus standi* of the plaintiff to institute an action against them, in terms of section 424 of the Companies Act. The special plea reads as follows:

"(1) On or about 11 September 2009, an arrangement between Furnex and its creditors, having been sanctioned by the Court on 1 September 2009, was registered in terms of section 311(6)(a) of the Companies Act 61 of 1973 as amended.

(2) In terms of clause 6 of the arrangement all creditors of Furnex, including the plaintiff, were deemed to have ceded their claims against Furnex to the proposer or its nominee with effect from the date of registration of the court order sanctioning the arrangement concerned.

(3) The arrangement was binding on all the creditors of Furnex, including the plaintiff.

(4) In the premises, with effect from 11 September 2009 the plaintiff ceased to have locus standi in respect of any claim it had against Furnex and accordingly against the defendants in respect thereof."

[3] The parties have agreed, in terms of Rule 33(4) to a separation of the issues and, that the defendants' special plea be determined separately and prior to the remaining issues. There is also agreement that in the event of the special plea being upheld, it will dispose of the action in its entirety.

[4] It is common cause that the offer of compromise and scheme of arrangement was sanctioned by the Court on 11 September 2009. Clause 6 of the scheme of arrangement reads as follows:

*"**6. Proposed Arrangement between the Company and its Creditors and Cession of Claims***

6.1 The capital sum payable by the Proposer in terms 4.1 above of this arrangement for the benefit of the creditors shall be deemed to have been paid to the creditors as the consideration for the cession by them to the Proposer of their claims ("ceded claims"), and each creditor will be deemed to have ceded its claims against the Company to the Proposer or its nominee.

6.2 A cession of the claims referred to in 6.1 shall be deemed to take effect upon the registration of the order sanctioning this arrangement in terms of Section 311(6) of the Companies Act, save in terms of 3.3."

[5] It is common cause that the word "deemed" used in relation to the cession of the creditors' claims to the proposer in clause 6 of the scheme of arrangement bears its general or usual meaning, which was expressed as follows in *R v Norfok County Council* 65 LT 222, and cited in *Ex Parte Strydom NO: In Re Central Plumbing Works (Natal) (Pty) Ltd* 1988 (1) SA 616 (D&CLD) at 620E-G:

"Generally speaking when you talk of a thing being deemed something you do not mean to say that it is that which it is deemed to be. It is rather an admission that it is not what it is deemed to be and that, notwithstanding it is not that particular thing, nevertheless...it is deemed to be that thing."

In the earlier case of *Steel v Shanta Construction (Pty) Ltd and Others* 1973 (2) SA 537 (T) at 541, Coetzee (at 541I-J) stated that:

"When "deemed" is used as meaning "considered" or "regarded" and not in one of its other meanings (such as, for instance, "to think") it is a very strong

word to denote, frequently exhaustively, that something is a fact regardless of the objective truth of the matter. It is an indispensable word, in legal parlance, to convey that enquiry into this truth is irrelevant for purposes of the particular instrument."

[6] Section 311 of the Companies Act provides:

*"**Compromise and arrangement between company, its members and creditors***

(1) *Where any compromise or arrangement is proposed between a company and its creditors or any class of them or between a company and its members and any class of them, the Court may, on application of the company or any creditor or member of the company or, in the case of a company being wound up, of the liquidator, or if the company is subject to a judicial management order, of the judicial manager, order a meeting of the creditors or class of creditors, or of the members of the company or class of members (as the case may be), to be summoned in such manner as the Court may direct.*

(2) *If the compromise or arrangement is agreed to by —*

(a) *a majority in number representing three-fourths in value of the creditors; or*

(b) *a majority representing three-fourths of the votes exercisable by the members or class of members,*

(as the case maybe) present and voting either in person or by proxy at the meeting, such compromise or arrangement shall, if sanctioned by the Court, be binding on all creditors or the class of creditors, or on the members or class of members (as the case maybe) and also on the company or on the liquidator if the company is being wound up or on the judicial manager if the company is subject to a judicial management order.

(3) No such compromise or arrangement shall affect the liability of any person who is a surety for the company.

(4) *If the compromise or arrangement is in respect of a company being wound up and provides for the discharge of the winding-up order or for the dissolution of the company without winding up, the liquidator of the company shall lodge with the Master a report in terms of section 400(2) and a report as to whether or not any director or officer or past director or officer of the company is or appears to be personally liable for damages or compensation to the company or for any debts or liabilities of the company under any provision of this Act, and the Master shall report thereon to the Court.*

(5) *The Court, in determining whether the compromise or arrangement should be sanctioned or not, shall have regard to the number of members or members of a class present or represented at the meeting referred to in subsection (2) voting in favour of the compromise or arrangement and to the report of the Master referred to in subsection (4).*

(6) (a) An order by the Court sanctioning a compromise or arrangement shall have no effect until a certified copy thereof has been lodged with the Registrar under cover of the prescribed form and registered by him.

(b)A copy of such order of court shall be annexed to every copy of the memorandum of the company issued after the date of the order.

(7) *If a company fails to comply with the provisions of subsection (6) (b), the company and every director and officer of the company who is a party to the failure, shall be guilty of an offence.*

(8) *In this section 'company' means any company liable to be wound up under this Act and the expression 'arrangement' includes a reorganization of the share capital of the company by the consolidation of shares of different classes or by the division of shares into shares of different classes or by both these methods."*

[7] The question for determination is therefore whether the right conferred upon creditors by section 424(1) of the Companies Act is extinguished upon the sanctioning and implementation of a compromise in terms of section 311 of the Companies Act. In other words, do creditors, upon a sanctioning and implementation of a compromise, retain any rights they might have against representatives of the company, having ceded or surrendered their claims against the company.

[8] Section 424(1) of the Companies Act provides:

"When it appears, whether it be in a winding-up, judicial management or otherwise, that any business of the company was or is being carried on recklessly or with intent to defraud creditors of the company or creditors of any other person or for any fraudulent purpose, the Court may, on application of the member or contributory of the company, declare that any person who was knowingly a party to the carrying on of the business in the manner aforesaid, shall be personally responsible, without limitation of liability, for all or any of the debts or other liabilities of the company as the Court may direct."

In *Ex Parte De Villiers and Another NNO: In re Carbon Developments (Pty) Ltd (In Liquidation)*1992(2) SA 95 (WLD), Stegmann J had to decide whether creditors, in an application in terms of s 311 of the Companies Act for an order that meetings be held of classes of creditors of a company in liquidation to consider a proposed compromise or arrangement, could both surrender their claims against the company and retain any rights that they might have against its representatives under s 424(1) of the Companies Act. He outlined the purpose of a s 424(1) application (at 107F-107G) as follows:

"*What is aimed at by an application in terms of s 424(1) is that a person contemplated by the subsection (often a director or officer of an insolvent company, and whom I shall call a 'wrongdoing company representative') should be declared personally responsible for 'the debts or other liabilities of the company', or at least for such of them as the Court may conclude that he should be held personally responsible for."*

[9] Stegmann J held that the existence of 'debts and liabilities' are a prerequisite for the operation and functioning of s 424(1) of the Companies Act:

"For s 424(1) to be operable at all, the company must have 'debts or other liabilities'. If the company has no' debts and liabilities 'an essential requirement is missing and s424(1) cannot provide a remedy. In a case in which the creditors have all agreed in terms of s 311 to a compromise which specifically provides for the extinction of all the company's debts and liabilities, it seems to me to be obvious that s 424(1) cannot possibly function after the extinction of such debts and liabilities by the agreement of the creditors and sanction of the Court.

...

To my mind the words of s 424(1) make it quite clear that a debt or other liability of the company is the very foundation upon which any declaration of personal liability on the part of a wrongdoing company representative must stand as an ancillary liability, and that when that foundation ceases to exist (eg by the discharge or extinction of the company's debts) the wrongdoing company representatives which otherwise might have been declared personally responsible in terms of s 424(1) cease to be amenable to any such declaration. The liability of the wrongdoing company representatives to be declared personally liable for a company's debts or other liabilities in terms of s 424(1) is a liability ancillary to the company's own debts or other liabilities and it cannot exist without them." (at 107G-108B)

[10] Stegmann J in *Ex Parte De Villiers* accordingly concluded (at 108J to 109A-B) that when a creditor of an insolvent company in liquidation is faced with a proposal under s 311 of the Companies Act, which involves an offer of compromise inviting him to agree to cede his claims against the company in liquidation, in return for the right to a payment in terms of the compromise, such creditor should recognise the implication that, if and when he ceases to be a creditor of the company by virtue of a Court order sanctioning the compromise, he will also cease to qualify to enjoy the benefits of such rights as s 424(1) may have afforded him, had he approached the Court at a time when the company owed him a debt or other liability, for a declaration that a wrongdoing representative of the company was personally responsible for the full amount of such debt or other liability of the company.

[11] Although the judgment of Stegmann J in *Ex Parte De Villiers* was reversed on appeal in *Ex Parte De Villiers and Another NNO: In Re Carbon Developments (Pty) Ltd (In Liquidation)* 1993 (1) SA 493 (A), the Appellate Division left open the question of whether a creditor who has ceded its claim against the company retained its *locus standi* to approach a court for declaratory relief against a representative of a company under s 424(1) of the Companies Act. Goldstone JA adopted the following view:

"In the view I take in this matter, it is not necessary to decide this interesting and difficult question. I shall assume that the effect of the offer of compromise, on sanction by the Court, would be to preclude relief under s 424(1) at the instance of the creditor."

[12] However, Mr Hollander, for the plaintiff, contends that the decision of Stegmann J in *Ex Parte De Villiers* is wrong as it fails to properly take into account, the true intention of the Legislature in relation to the meaning of the words *"creditor of the company"* and, the primary objects of s 424(1 of the Companies Act. He finds support for this contention in *Pressma Services (Pty)(Ltd) v Schuttler and Another* 1990 (2) SA 411 (CPD), in which Van Schalkwyk AJ (at 417B-H), construed the meaning of the words "*creditors of the company*" in s 424(1) of the Companies Act, in light of what he viewed the primary objects of the Legislature to be. He stated as follows:

*"The words could mean either a person who is a creditor of a company at the time when he approaches the Court in terms of s424(1), in the sense that there is an existing indebtedness, or they could mean, in addition, a person in respect of whom there was an indebtedness which ceased to exist upon the sanctioning and implementation of the compromise. The first, more restricted meaning, is the more obvious and ordinary one which, in the absence of an indication to the contrary, would be the meaning to be ascribed to the words (*Steyn Die Uitleg van Wette *5th ed at 6-7 and the authorities there cited). The second, extended meaning, would be permissible only upon the basis that it is consistent with the true intention of the Legislature while the first, more restricted meaning, is not. (Steyn (op cit at 2-4) and the authorities there cited).*

The true intention of the Legislature in this regard must, in my view, be determined with reference to the primary objects of s424(1). These, as I have mentioned, are twofold. The first is to render personally liable all persons who knowingly participate in the fraudulent or reckless conduct of the business of a company. The second is to provide a meaningful remedy against the

abuses at which the subsection is directed. The first of these objects would be attained if, upon the sanctioning and implementation of a compromise, the personal liability of the persons concerned was maintained. This would be the
case even if the right conferred on a creditor by s424(1) were to pass to the offeror upon sanctioning and implementation of the compromise. The second object, however, would in my view not be attained if the remedy provided by the subsection were to be lost to creditors for, in the final analysis , it is to them that the debts of the company in respect of which personal liability is created by the subsection are owed."

[13] Van Schalkwyk AJ's suggestion (above at 417 E-H) that "creditor" may there have been confined to existing creditors, or may have been extended to include former creditors who have ceased to be creditors by virtue of a compromise in terms of s311 of the Companies Act, was sharply criticized by Stegmann J in *Ex Parte De Villiers* (at 106B-D) for its ambiguity as follows:

"This is, I must respectfully observe, a curious choice to have postulated, for if the creditors contemplated by s 424(1) are to be understood as including not only existing creditors, but also former creditors who had disposed of their
claims to existing creditors in terms of a compromise, the Legislature would have created an unlikely situation in which the company's debts (or some of them) would have to be paid twice over: once to the existing creditors and once to the former creditors. Such a result would be an absurdity which the Legislature cannot have contemplated, and I have no doubt that the implication was not brought to the attention of Van Schalkwyk AJ, and certainly not intended by him."

[14] Stegmann J went on to criticise Van Schalkwyk AJ's reasoning as

follows (at 106H-107E):

" The entire argument in the judgment is, I respectfully suggest, conducted on too narrow a footing. It seems to me that it overlooks a fundamental and decisive factor. There is no reason to doubt that, in making provision in s 311 for a compromise between a company and its creditors, the Legislature intended to leave the creditors free to agree to deal with their rights as they saw fit, ie to agree to compromise their rights, to alienate them, to extinguish them, as they chose. There is nothing in s424(1), or its context, which abridges a creditor's freedom to agree in terms of s 311 to compromise any rights he may derive from s424(1), or alienate such rights, or to extinguish them.

The conclusion reached by Van Schalkwyk AJ in Pressma Services *appears to accept that the Legislature, when providing the rights created by s 424(1) in the circumstances defined therein, intended to create a species of incorporeal property which was to be different from virtually all other incorporeal property in that the holder thereof was to have no power to agree to cede it, or to compromise it, or to extinguish it. This new species of incorporeal property is evidently thought to be both inalienable and indestructible. The consequence thereof is said to be that creditors are placed in the remarkably advantageous position of being free to compromise, alienate or extinguish their claims against a company in terms of s 311, secure in the knowledge that nothing they may agree to in terms of such compromise can affect their inalienable and indestructible rights guaranteed by the Legislature in all circumstances in terms of s 424(1). It is suggested that to that extent creditors are free to have their cake and eat it.*

No doubt the Legislature has power to devise and enact such an anomalous scheme of things. However, I am respectfully unable to accept that the Legislature has in fact done so in terms of s 424(1). Certainly it has not done so in express terms, and I remain unpersuaded by the argument that it has done so by implication. To the extent that the decision in Pressma Services *suggests otherwise, I express my respectful disagreement with it."*

[15] Having considered the judgement of Stegmann J in *Ex Parte De Villiers*,I am unable to find that either his conclusion or reasoning is wrong. I therefore endorse his judgment in all respects in relation to the question of whether creditors can both surrender their claims against the company, in an offer of compromise and retain any rights they may have against its representatives under s424(1) of the Companies Act. I am thus of the view that the judgment of Van Schalkwyk AJ is clearly wrong as it fails to have regard to the following essential factors:

(a) The freedom conferred upon creditors in an offer of compromise between a company and the creditors, in terms of s 311 of the Companies Act, to agree to deal with their rights as they see fit — by agreeing to either compromise, alienate or extinguish their rights;

(b) for s 424(1) of the Companies Act to be of application, the company must have *"debts or liabilities".*

[16] In a case, such as this, where the creditors have all agreed in terms of s 311 to a compromise which specifically provides for the extinction of all the companies debts and liabilities, s 424(1) cannot possibly function after the extinction of such debts and liabilities by the agreement of the creditors and the sanction of the Court. Despite the decisiveness of this factor to the question for determination in *Pressma Services*, it was not considered by Van Scalkwyk AJ.

[17] The fact that the Legislature has preserved the rights of a cedent to

proceed against the surety in s 311(3) of the Companies Act, the purpose of which is to ensure that a creditor's rights as against third parties (sureties) should not be affected by the sanctioning and implementation of an offer of compromise or scheme of arrangement, does not mean that the Legislature intended, either expressly or by implication, that the rights conferred upon creditors by s 424(1) are not extinguished upon the sanctioning and implementation of an offer of compromise or scheme of arrangement. I am therefore unable to agree with the view of Van Schalkwyk AJ in *Pressma Services* (at 418 A-D) that s 311(3) of the Companies Act supports the view that creditors retain the rights conferred upon them by s 424(1) upon the sanctioning and implementation of a compromise by virtue of the fact that the Legislature has seen fit to preserve the rights of creditors against sureties in such circumstances.

[18] Claassen J in *Kalinko v Nisbet and Others* 2002 (5) SA 766 (W) at 776B-F, (as did Horn J, in *Lordan NO v Dusky Dawn Investments (Pty) Ltd (In Liquidation) (Pearmain and Another Intervening)*1998 (4) SA 519 (SE) at 529E-H)) expressed his preference for the conclusion reached in *Pressma Services* that an offer of compromise in terms of s 311 of the Companies Act does not affect creditors rights in terms of s 424 thereof. He, in particular, subscribed to the following comment of Van Schalkwyk AJ in *Pressma Services* (at 416J-417A):

"It is, in my view, unthinkable that the Legislature could have intended that the aforestated purpose could be frustrated and the remedy provided for in

the subsection lost merely because of the sanctioning and implementation of a compromise in terms of s 311, especially in view of the fact that creditors who have voted against the sanctioning of the compromise may, in certain instances, be bound thereby."

[19] I am, with all due respect, not bound by the views expressed by Claassen J in *Kalinko v Nisbeth* as he was not called upon to deal with, and nor did he deal with, the question of whether or not creditors' rights in terms of s424(1) of the Companies Act are extinguished upon the sanctioning and implementation of a compromise in terms of s 311 of the Companies Act where, as in this case, the creditors have ceded or surrendered their claims against the company.

[20] The plaintiff, however, contends that upon the sanctioning and implementation of a compromise in terms of s 311 of the Companies Act, a creditor's rights under s 424(1) of the Companies Act can only be extinguished if it in actual fact cedes its claims against the company to the proposer. It is the plaintiff's contention, in this regard, that a creditor's s 424 rights can never be extinguished by operation of a deeming provision in terms of which a creditor is deemed to have ceded its claims against the company to the proposer.

[21] I do not agree with this contention. It is clear, in my view, that in the scheme of arrangement, in this case, the word "deemed" when used in relation to the cession of creditors claims bears it usual meaning ─ i.e. "deemed" is used as meaning "considered" or "regarded". This much is

common cause. Therefore, the proposal made by the proposer (Trans Africa Investment Holdings (Pty) Ltd), and accepted by the creditors is that the capital sum payable by the proposer in terms of clause 4.1 of the offer of compromise and scheme of arrangement for the benefit of the creditors shall be regarded as having been paid to the creditors, as the consideration for the cession by them to the proposer of their claims ("ceded claims"), and each creditor will be regarded as having ceded its claims against the company (Furnex), to the proposer or its nominee. Simply put, the proposal made by the proposer is, *inter alia*, that all the claims of creditors of Furnex including the plaintiff, should be regarded as if they had been ceded to the proposer.

[19] In *Ex Parte Strydom,* (above), the Court had to give consideration to the question of whether three standard schemes of arrangement amounted to "arrangements" within the ambit of s 311 of the Companies Act. In each of these schemes of arrangement the offeror proposed to make available a sum of money for distribution among all the creditors of the companies in (provisional) liquidation, in such a way that upon sanctioning of the schemes of arrangement under s 311 of the Companies Act, and upon receipt of the dividend due to them, each creditor would be deemed to have ceded to the offeror its claim against the respective companies. In considering the concept of a "deemed cession" as contemplated in the three standard schemes of arrangement under consideration, Friedman J and Wilson J stated as follows (at 621A-622D):

"It is clear in our view that in the scheme of arrangement in this case and in the Robin *case the word "deemed", when used in relation to the cession of*

creditors claims to the offeror, bears its general meaning. The proposal made by the offeror is, inter alia*, that all the claims of creditors of the company should be regarded as if they had been ceded to him, irrespective of whether or not creditors cede those claims to him, including the claims of those creditors who may not wish to cede their claims to him, and including those creditors of whose identity he is unaware or who may be unaware of the proposal which he is making. The scheme of arrangement which is proposed, therefore, is not one whereby the offeror in fact acquires the claims of creditors; it is one whereby it is proposed that he should be regarded as having acquired them regardless of the objective truth of the matter."*

...

In our view, therefore, there is no difficulty in conceptualising within the framework of a scheme of arrangement a 'deemed cession', that a cession shall be regarded as having taken place even although in truth and in fact it has not. Such a concept, to have any effect, however, requires the active participation of the debtor, ie the company. In the first place, what is required to bring about this situation is agreement on the part of the company to regard a third party as its creditor in place of its actual creditor, as if the actual creditor had ceded its claims to the third party. This concept can only be given any legal effect by the actions of the company in recognising a state of affairs as existing which does not in fact exist. The contract is not one which, as Coetzee DJP says, exists purely between cedent and cessionary. Where there has in fact been a cession, the company is obliged to recognise the cessionary as its new creditor; where the cession is 'deemed', there is obviously no obligation on the company to recognise a state of affairs which does not, in fact, exist. And it would seem to follow that the Court could not, in that event, make an order affecting the company without the company being a party thereto. The arrangement, therefore, whereby the company will recognise the offeror as its new creditor in place of its old seems to us to be not only notionally and linguistically, but also in its basic content, an arrangement between it and its creditors.

...

Finally, it should perhaps be mentioned in passing that a cession can be

deemed to have occurred in the manner we have described even although the instrument of debt has not been transferred to the offeror."

[20] Accordingly, I am of the view that the "deemed cession" of the creditors claims against Furnex to the proposer, as provided for in the scheme of arrangement, has been given legal effect to by Furnex having agreed, by way of an arrangement between it and its creditors (which arrangement has been sanctioned by the Court) that it regards the proposer as its creditor in place of its actual creditors ─ as if the actual creditors ceded their claims to the proposer. The "deemed cession" thus has the legal effect of a cession.

[21] In the circumstances, I am of the view that upon the sanctioning and implementation of an offer of compromise and scheme of arrangement, in terms of which creditors are deemed to have ceded their claims against the company to the proposer, any rights which they might have against representatives of the company, in terms of s 424(1) of the Companies Act, are extinguished. Whether creditors' claims against the company are deemed to be ceded, or actually ceded is accordingly of little moment.

[22] In the premises, I am of the view that the effect of an offer of compromise and scheme of arrangement, on sanction by the Court, would be to preclude relief under s 424(1) of the Companies Act at the instance of a creditor. Accordingly, with effect from 11 September 2009 the plaintiff ceased to have *locus standi* in respect of any claim it had against Furnex, or the defendants, by virtue of the scheme of arrangement between

Furnex and its creditors, which was sanctioned by the Court on 1 September 2009, and registered in terms of s 311(6)(a) of the Companies Act.

The defendants' special plea must accordingly succeed.

[23] In the result, I make the following order:

(a) The special plea is upheld with costs.

(b) The plaintiff's claim is dismissed with costs.

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F. KATHREE-SETILOANE
JUDGE OF THE SOUTH GAUTENG
HIGH COURT, JOHANNESBURG

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Date of Hearing:	26 August 2011
Date of Judgement:	8 February 2012

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