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An extension of the Parate Executie principle in the liquidation context

5 March 2024 *6 min read*

Emontic Investments (Pty) Ltd v Bothomley and Others[1]

Introduction

A *Parate Executie* clause is generally regarded as an impermissible contractual provision which envisages a secured creditor disposing a secured asset through a private sale when the debtor defaults, without recourse to a court – a so-called "self help" or "summary execution" clause. Such a clause is generally recognised as being *contra bonos mores* and unenforceable absent the debtor's consent to the seizure and sale of the asset in question[2].

In an insolvent situation, a secured creditor is often in possession of an asset belonging to the insolvent which serves as security, by virtue of for instance pledge or a landlord's hypothec which makes the realisation of the asset by the creditor more practically achievable. This much is recognised by the provisions of section 83 of the Insolvency Act 24 of 1936 ("the Insolvency Act"), with the proviso at section 83(10) that requires the net proceeds of the sale by a secured creditor of its secured asset to be made to the liquidator so that the liquidator may account for those proceeds in the insolvent estate's liquidation and distribution account, to be approved in due course by the Master, before the creditor can be paid out of the proceeds of that asset.

In other words, a process of court-driven oversight is required with respect to the allocation of proceeds from such a sale (regardless of whether the asset is movable or immovable).

In January 2024, the Supreme Court of Appeal handed down judgment on consideration of section 83(10) of the Insolvency Act.

Facts of the Case

- The appellant, Emontic Investments (Pty) Ltd ("Emontic") is the owner of immovable property, a farm situated in Heidelberg where Montic Dairy Proprietary Limited (in liquidation) ("Montic") conducted its business prior to its liquidation.
- In June 2016, Montic was placed in final liquidation. At the time of its liquidation Montic was indebted to Emontic in excess of R5,000,000.00 in respect of unpaid rental ("the historical rental claim").
- In November 2016, 5 months after Montic was placed in liquidation its liquidators notified Emontic of the termination of the lease agreement effective from the end of November 2016.
- Emontic lodged and proved its claim, which was for the historical rental, but also for the post-liquidation rental amount owed to it by Montic from date of liquidation until termination of the lease ("the administration rental"), and as security for its claim it relied on the common law landlord's lien over the movables which were situated on the farm.
- Prior to the second meeting of creditors Emontic notified Montic's liquidators that it would be selling the movable property over which it held as security in accordance with the provisions of section 83 of the Insolvency Act.

- Pursuant to the sale of the movable property, Emontic refused to pay over the net proceeds received from the sale of the movable property despite demand. It paid some of the proceeds, but only after it had exercised set off of its claims against the proceeds.

Legal Issue

The court had to determine whether a creditor who had relied on and realised its security in terms of section 83(3) of the Insolvency Act could apply post-liquidation set-off against the net proceeds which are to be paid to the liquidator pursuant to the realisation of the security. Could they in effect retain the proceeds of the sale, even though they had valid claims and security for them?

Emontic's Argument

1. Emontic argued that administrative rental ought to be classified as an expense incurred in the realisation of the property and must therefore be subtracted from the gross proceeds of the secured assets sold by it in determining the net proceeds.
2. Emontic further argued that it had the right to set off the administration rental from the net proceeds of the sale before making payment to the liquidators.

The Court's Decision

The court was having none of it and held that:

the wording of s 83(10) was explicit and unambiguous and required payment to the liquidator "*promptly*", and "*whenever a creditor has realised his security*", and did not permit set off to operate against a liquidators claim for payment under that section (for any part of the claim in question).

1. the obligation imposed on a creditor under s83(10) to pay over the net proceeds of the realised asset and the obligation of the trustee to pay the creditor his preferent claim out of such proceeds are not reciprocal obligations.
2. Emontic's argument of set-off was legally unsustainable as section 83(10) makes it clear that a creditor who has realised assets must promptly pay the net proceeds of the realisation to the liquidator and consequently does not permit set off to operate against a liquidator's claim for payment of the net proceeds.
3. the claim of each creditor had to be dealt with as it existed at the issue of the order placing the company in liquidation.
4. common law set-off could not operate because the condition that both debts were payable by and to the same persons was absent – the administration rental had to be paid out of the free residue of the estate, whereas the historical rental had to be paid from the proceeds of the assets securing the claim.
5. the liquidators were obliged to recover the proceeds from the sale of the assets by Emontic, and it was legally impermissible for them to agree to Emontic retaining any portion of the proceeds of its realised security.
6. a creditor who refuses to pay over the net proceeds to the liquidator even after demand, shall be guilty of an offence.

Conclusion

The SCA has thus reaffirmed the position that once a *concursus creditorum* has been established no single creditor can enter into a transaction in respect of the estate to the prejudice of the general body of creditors.

A creditor who chooses to rely on, and realise its security is obliged to pay over all the net proceeds of the sale to the liquidator, who shall then account for the asset and the creditor's claims. All claims and assets must be properly accounted for in a liquidation.

From the aforegoing it is apparent that the principal that a party, however secure their claim, cannot simply avail themselves of their due without a measure of appropriate oversight. The avoidance of any self help/*parate executie* behaviour is securely entrenched embedded in our insolvency law.

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[1] [2024] ZASCA.

[2] Juglal NO & another v Shoprite Checkers (Pty) Ltd t/a OK Franchise Division 2004 (5) SA 248 (SCA); SA Bank of Athens Ltd v Van Zyl 2005 (5) SA 93 (SCA)



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