RISK ALERT BULLETIN MAY 2004 **No.2\2004**

1. GENERAL MANAGER'S COLUMN

In our February Bulletin, we referred to the controversial RAF Second Amendment Bill of 2003. Parliamentary hearings on the Bill were again cancelled amid indications that the Bill would either be scrapped in its current form or held over until after the elections. It is clear that full consultation is required before the Bill is passed and we will report further in our August 2004 Bulletin.

In this issue, we have the second (and final) instalment of our 2-part article, Common Pitfalls in Business Sales and also our usual columns containing current decisions pertaining to Prescription and MVA matters. We hope you find these useful.

Policy Queries

I have allowed my client's common-law claim against the driver/ owner of the vehicle in which he was a passenger to become prescribed. What is the deductible?

As the claim arose for reasons set out in clause 8.5.2 of the Policy, (i.e. for loss/damage in respect of bodily injury caused by the driving of a motor vehicle) the higher deductible (as applied for Prescribed MVA's) will apply (see Clause 8.5.1 of the Policy). The deductible for a single practitioner will be R35 000- 00 and R63 000-00 for a two- partner firm etc.

Because the claim against the driver/owner is governed by common-law and not the RAF Act and the matter cannot be registered with *Prescription Alert*, the 15% loading will not apply.

(The Plaintiff will, *inter alia*, have to prove that the driver/owner of the vehicle would have been able to satisfy a claim instituted against them, before s/he will be entitled to compensation.)

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2. Common Pitfalls in Business Sales- Part 2

In Part 1 we dealt with the issues of VAT, the Labour Relations Act and the Competition Act as they affect the sale of businesses.

We now discuss the Insolvency Act, Warranties, the extent to which book debts, liabilities and contracts are transferred and the requirements for the transfer of contracts with third parties.

Insolvency Act

In terms of s34 of the Insolvency Act, if a trader transfers a business or a part of it, and the trader is sequestrated or liquidated, or a creditor attaches property in satisfaction of a judgment debt, the transfer is void against the trustee or liquidator, or such a creditor, for six months after the transfer unless the transfer has been advertised as prescribed.

The advertising involves two advertisements in an English and an Afrikaans newspaper circulating in the area where the business is conducted, and one in the Government Gazette (which should be on the same day as the second of the two sets of newspaper advertisements). The business may then be disposed of not less than 30 or more than 60 days after the last publication without risk of attack by a liquidator, trustee or creditor.

It is often impossible, because of time constraints, to publish the advertisements. Where this is so, it is desirable to insert a provision in the contract whereby the seller indemnifies the purchaser against the consequences of an attachment. This, however, does not protect the purchaser in the event of insolvency or liquidation, in which case the purchaser will lose the assets purchased and is left with only a concurrent claim for the purchase price.

When drafting these agreements, practitioners should warn the purchaser (their client) not to lightly forego the protection afforded by the Insolvency Act if there is any real prospect of a supervening insolvency of the seller. By failing to do so, you may be faced with a claim by a purchaser who has had to restore such assets as are in his possession or to pay the value of these assets.

Warranties

The extent of warranties to be given by a seller will vary considerably according to the particular circumstances. Obviously, the seller of a business will want to limit the warranties as much as possible, whereas the purchaser will want them to be as inclusive as possible.

The two most common reasons advanced for limitation of warranties are either that the purchaser has had the opportunity to conduct a full due diligence investigation (and therefore, so the seller will say, should have discovered all the skeletons in the cupboards), or that the sale is a management buy-out (and therefore the purchaser, who has been in control of the business, should be aware of the existence, and location, of the skeletons).

The simple point is that the things usually warranted are the basis of the sale price being fixed as it is, and the seller should take a view on warranting what is necessary to ensure that that value is vouched by proper warranties.

Book Debts, Liabilities and Third-Party Contracts

It is often best for the purchaser of a business to take over the debtors' book as it stands at the effective date. There are many different ways of dealing with this, the most common are:

1. Cession of the book, with a warranty that the book is good for, say, 90% of its nominal value and with adjustments by way of reimbursement to the purchaser if it has not been recovered after a specified period. Sometimes a converse provision is also inserted, with an adjustment in favour of the seller if the recovery exceeds the specified proportion.

2. Cession of a part only of the book (that part agreed as likely to be good) with or without a warranty.

3. In conjunction with either 1 or 2 above a resolutive condition in respect of each debt that, if it has not been recovered by a specified date, it reverts to the seller (with an appropriate price adjustment in the purchaser's favour).

It is usually best for the business to be sold free of liabilities, and this is so for the seller just as it is for the buyer, because it limits possible contention about the extent of the liabilities after the transfer has taken place.

It is often necessary for third-party contracts such as supply agreements, leases, licences and service agreements to be taken over for the continued operation of the business.

A debt can always be transferred by cession, and without the consent of the debtor (provided only that the debtor's obligation is not made more onerous). But the delegation of an obligation does need the consent of the person to whom the obligation is owed.

The purchaser *(with the assistance of his attorney)* needs to analyse carefully which third-party contracts are necessary for the business acquisition to be worthwhile. If there is one particular contract which is necessary then the transfer of the contract to the purchaser should be a condition precedent – a condition which stops the contract from coming into operation until it is fulfilled. As a rule, one simply incorporates a term which obliges the seller to use all reasonable endeavours to get the third party to agree to the transfer.

Conclusion

There are as many appropriate ways of dealing with the sale of businesses as there are business sale transactions, and no standard method of drafting an agreement for a business sale. The above is no more than the briefest of guidelines which practitioners should consider in structuring their clients' transaction and in safeguarding themselves against possible allegations of negligence at a later stage.

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With acknowledgement to Hugh Bisset of Deneys Reitz (Commercial Update- September 2001)

3. Useful tips for MVA Practitioners

Road Accident Fund v Thugwana 575\2002

This appeal (*unreported at the time of publication*) raised three questions:

(i) The meaning of regulation 2(1)(c) in terms of the Road Accident Fund Act, 56 of 1996 which requires a person injured in a "hit and run" motor vehicle accident to furnish an affidavit to the police, if reasonably possible, within 14 days after being in a position to do so;
(ii) Whether the regulation is peremptory; and if it is,
(iii) Whether it is *ultra vires*.

Facts

The respondent (Thugwana), as plaintiff, instituted an action for compensation against the appellant (RAF), as defendant, for damages for injuries sustained in a motor vehicle accident. The RAF raised a special plea alleging non-compliance by Thugwana with regulation 2(1)(c). Thugwana replicated that he had complied with the provisions of the regulation; alternatively, that he had substantially complied therewith; and further alternatively, that the provisions of the regulation were *ultra vires* the Act. The Court *a quo* (De Vos J) dismissed the special plea hence the appeal.

Held

In answering question (i) above the Court held that the purpose of the regulation is to reduce the risk of fraud in “hit and run” claims, as the RAF usually finds it impossible to find evidence to controvert the claimant’s allegations. The later the affidavit is made the greater the problems that would be faced by the RAF. The Court *a quo* reasoned that the claimant had to have been aware that such an affidavit was required, for the regulation to apply. The Appeal Court held that to interpret the regulation so as to require a subjective knowledge of the provisions on the part of the claimant, before the obligation to furnish the affidavit arises, would defeat the whole purpose thereof, -although the double qualifications contained in the regulation *i.e.*, “if reasonably possible” and “after being in position to do so” create a certain difficulty. Thugwana was in a position to submit the affidavit to the police whilst he was still in hospital, and at the latest by February 1999. The affidavit was only submitted to the police on the 29 August 2002.

With respect to question (ii) above the Court held in the affirmative as it provides a penalty for non-compliance, namely, the Fund incurs no liability to the claimant.

With respect to question (iii) the Court held that the regulation is not *ultra vires* as it is regulatory in nature, designed to eliminate fraud or facilitate proof.

In conclusion, the court held that the Fund had 60 days, in terms of Section 24(5) of the Act, to object to the validity of a claim submitted, failing which the claim shall be deemed to be valid in all respects and commented that this could provide an answer to the special plea. The appeal was accordingly upheld and leave granted to Thugwana to amend his replication.

Although each case must be assessed according to it’s own particular circumstances, practitioners are urged to ensure that the appropriate affidavit is lodged with the SAPS timeously. Should a client approach you well after being able to lodge the appropriate affidavit then he\she should be fully advised as to the dangers involved in lodging such a claim. Detailed notes of such consultation must be kept and a letter should be sent to the client, confirming the discussion. It does seem however in terms of this judgment that the RAF may only rely on this regulation if they have indeed objected to the validity of the claim in terms of section 24(5) of the Act.

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3. PRESCRIPTION MATTERS

Section 15(1) of the Prescription Act 68 of 1969

In terms of the section, “the running of Prescription shall, subject to the provisions of section 15(2) be interrupted by the service on the debtor of any process whereby the creditor claims payment of the debt.”

Blaauwberg Meat Wholesalers CC v Anglo Dutch Meats (Exports) Limited 442\2002

Here the court had to consider whether an action mistakenly instituted in the name of A as creditor served to interrupt prescription where it appeared, after the prescriptive period, that B was the true creditor and the summons was duly amended.

Facts

On 12 April 1996, summons was served on the appellant in which Anglo-Dutch Meats (UK) Limited (hereinafter referred to as “UK”) claimed payment for goods sold and delivered to the appellant, the last due date for payment being 23 August 1995.

During November 1998, the legal representatives of the plaintiff became aware that the true seller of the meat had been Anglo- Dutch Meats (Exports) Ltd (hereinafter referred to as “Exports” and the current respondent) and not UK. By then more than three years had passed since the cause of action arose.

An application was brought to amend the citation of the plaintiff which the appellant opposed.

Held

Cleaver J. in the *court a quo* granted the amendment stating that, “Prescription will not be a consideration if the amendment is granted on the basis that the plaintiff was incorrectly described or that the description of the plaintiff amounted to a misnomer, for in such event the service of the summons on the defendant will have interrupted prescription.”

The appellant raised a Special Plea of Prescription. Hodes J. in the Cape Provincial Division ruled that he was entitled to reconsider the application for the amendment of the citation of the plaintiff. He concluded that Cleaver J. had wrongly granted the amendment because the running of prescription had not been interrupted by the summons. He upheld the special plea.

The respondent appealed to a Full bench. The main question before the court was whether a summons was served on the defendant before prescription, in which the creditor who asked for judgement, viz Exports, claimed payment.

In answering this question, the court held that the fact that there was no exact compliance is beyond dispute. However, the identity of the creditor did not depend on the name only, but also place of residence or business, registered office, occupation or nature of business, details of some or all of which one would expect to find in a process, may also serve to establish identity or clarify an ambiguous or incorrectly stated name. Here, however, the only possible details were that UK "was a company with limited liability registered in accordance with the Laws of England with registered office at Arkwright Road, etc. When Exports was later introduced into the summons, exactly the same description was applied, which was insufficient to support it as the creditor. The fact remained that the summons served on the appellant failed entirely to communicate to it the intention of Exports to claim payment.

In concluding the court stated that prescription penalises negligence and inactivity. The respondent remained absent and inert for more than three years and failed to take reasonable precautions from the time of preparing the summons to the belated awakening.

While it may seem obvious, we once again urge practitioners to ensure that they issue proceedings in the name of the correct plaintiff and also to conduct the necessary research (Company searches etc.) to ensure that they have sued the correct defendant.

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6. LETTERS TO THE EDITOR

Dear Editor
Re: Bilingual Bulletin

The Management and members would like to thank you for the excellent policy decision to publish this essential magazine in Afrikaans as well.

On behalf of all the members we extend a heartfelt thanks and wish you all the best with your work in future.

Yours Faithfully

CJA Lourens
Vereniging van Regslui vir Afrikaans

Erratum

Amendment of Attorneys Act, 1979
In our February 2004 Bulletin we reported on the above amendment and provided the contact numbers of the Legal Education and Development unit. As this was a late insertion, the incorrect dialing code for the unit was given. We apologise for the inconvenience caused in this regard. The correct numbers are:

Tel: (012) 341-3091 Fax: (012) 341-1339

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