

Analyses

Security for Costs in Corporate Litigation

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1 Introduction

In *Crest Enterprises (Pty) Ltd & another v Barnett and Schlosberg NNO* 1986 (4) SA 19 (C) at 20B–C, Berman J stated every person’s right of access to the courts:

‘[N]o hurdle should be permitted to stand in the way of any person’s access to a court in seeking relief at its hands, and no court should — in the case of an impecunious litigant — by requiring him as plaintiff, or applicant, to provide security for his opponent’s costs, lend support to the canard which likens its doors to those of the Ritz Hotel.’

This principle is entrenched in the Bill of Rights. Section 34 of the Constitution of the Republic of South Africa Act 108 of 1996 provides that everyone has the right to have any dispute that can be resolved by the application of law decided in a fair public hearing before a court or, where appropriate, another independent and impartial tribunal or forum. The term ‘person’ here includes juristic persons like companies and close corporations (s 8(2) and (4) of the Constitution; see also Michele Havenga ‘Corporations and the Right to Equality’ (1999) 62 *THRHR* 495 at 495–497). There are a number of well-known common-law and statutory exceptions to the principle. Common-law exceptions include peregrine plaintiffs, persons intent on pursuing vexatious and reckless actions, and those who resort to proceedings that are an abuse of the process of the court (see, generally, *Ecker v Dean* 1938 AD 102 at 110).

Section 13 of the Companies Act 61 of 1973 provides for one of the statutory exceptions. It allows the court, at any stage, where a company or other body corporate is a plaintiff or an applicant in any legal proceedings, and if it appears by credible testimony that there is reason to believe that the company or body corporate, or, if it is being wound up, its liquidator, will be unable to pay the costs of the defendant or respondent if successful in his defence, to require sufficient security to be given for those costs. The court may stay all proceedings till the security is given. The corresponding, and very similar, provision relating to close corporations is section 8 of the Close Corporations Act 69 of 1984. The discussion that follows includes both sections, unless I indicate otherwise.

The courts have, in various judgments over the years, interpreted and

commented on these sections. In the discussion that follows I shall try to summarize the principles established in these cases.

2 Purpose of the Provision

The purpose of section 13 and its predecessor (s 216 of the Companies Act 46 of 1926) was stated in *Hudson & Son v London Trading Co Ltd* 1930 WLD 288 to be to protect the public in litigation by bankrupt companies. The bankrupt company is not excluded from the courts, but is prevented if it cannot find security from dragging its opponent from one court to another while it is not able to pay the costs if it is unsuccessful (see also *Lappeman Diamond Cutting Works (Pty) Ltd v MIB Group (Pty) Ltd (No 1)* 1997 (4) SA 908 (W) at 919G–H; *Northbank Diamonds Ltd v FTK Holland BV & others* 2003 (1) SA 189 (NmS) at 194I).

The applicant is not required to show that the company actually is insolvent. Rather, it is sufficient that there is reason to believe that the company will be unable to pay the defendant's or respondent's costs (*Henochsberg on the Companies Act* 5 ed by PM Meskin (ed) (1994) 28). That the company is in liquidation creates a rebuttable presumption that such reason exists (*Trust Bank van Afrika Bpk v Lief & another* 1963 (4) SA 752 (T) at 755; *Price Forbes (Africa) Ltd v Schwartz NO* 1966 (4) SA 118 (W)), as does the fact that the company's liabilities exceed its assets (*Ferreira v Arlinders Ltd* 1964 (1) SA 631 (O) at 632).

3 When May Security Be Required?

3.1 Entity

Section 13 applies to any company or body corporate, but it cannot be invoked against a trust — a trust is not a company or a body corporate within the meaning of the section. Nor should a court equate a trust with such a company for the purpose of ordering it to furnish security for costs (*Crest Enterprises supra* at 19; see also *Magnum Financial Holdings (in liquidation) v Summerly* 1984 (1) SA 160 (W), where it was confirmed that a trust is not a body corporate within the meaning of the Insolvency Act 24 of 1936).

3.2 Arbitration Proceedings

Section 21(1)(a) of the Arbitration Act 42 of 1965 states that for the purposes of and in relation to a reference under an arbitration agreement, the court has the same power to make orders in respect of, amongst other things, security for costs as it has for the purposes of, and in relation to, any action or matter in that court. When this provision is read with section 13, it is clear that the latter applies in respect of a company or body corporate that is a claimant in arbitration proceedings (*Henochsberg op cit* at 28; see also *Sasko Bpk v Futurus Construction (Pty) Ltd* 1988 (4) SA 170 (W) at 171; *Petz Products (Pty) Ltd v*

Commercial Electrical Contractors (Pty) Ltd 1990 (4) SA 196 (C) at 203–205).

3.3 More than One Plaintiff

Security may be required even if the company is not the only plaintiff or applicant (*Kruger Stores (Pty) Ltd v Kopman* 1957 (1) SA 645 (W) at 648; *Northbank Diamonds Ltd v FTK Holland BK & others* 2003 (1) SA 189 (NmS)). In *Northbank Diamonds*, the court exercised its discretion against ordering security on the basis that the pooled resources of the applicants were sufficient to pay the costs if Northbank were successful in its defence of the main application. Strydom CJ confirmed that the court had the discretion to make the order for costs against all the applicants jointly and severally, and considered the facts to be such that this type of order would be made.

3.4 When Claimed?

Security can be called for in terms of section 13 at any stage. Security once given may be increased later (*Montesse Township & Investment Corp (Pty) Ltd v Standard Bank* 1964 (1) SA 14 (T); *Alexander v Greenberg* 1983 (1) SA 1041 (W) at 1042; see also MS Blackman, RD Jooste & GK Everingham *Commentary on the Companies Act* (2002) 2-7). The security can be required in respect of costs already incurred and future costs (*Kruger Stores (Pty) Ltd v Kopman* supra at 648). It may be required to be given at any stage of the proceedings, as long as it is required timeously in relation to the progress of the proceedings (*Wallace NO v Rooibos Tea Control Board* 1989 (1) SA 137 (C)).

There should be as little delay as possible in bringing an application under section 13 (*Wallace v Rooibos Tea Control Board* supra at 144–145). But if the application is made too early it will be difficult to predict accurately how long the trial will take and what the costs will be (on the difficulties relating to bringing the application at the proper time, see *Croft Leisure Ltd v Gravestock & Owen* [1993] BCLC 1273 (CA) at 1279).

3.4 Liquidation

Section 13 provides that security may also be sought if it appears that a company's liquidator will be unable to pay the costs of the defendant or respondent if such party is successful in his defence. The section also applies where a liquidator enforces a statutory claim under other provisions of the Companies Act, read, where appropriate, with certain provisions of the Insolvency Act 24 of 1936 (Blackman et al op cit at 2-8; *Shepstone & Wylie & others v Geyser NO* 1998 (3) SA 1036 (SCA) at 1043A–C; contra *Trakman NO v Livschitz & others: In re Livschitz & another v Trakman NO* 1996 (2) SA 384 (W) at 391 et seq; Henochsberg op cit at 27).

The section should also apply to a company in judicial management, even though section 439 does not refer to section 13 (section 439 provides for the application of specific sections dealing with a company being wound up and its liquidator to companies in liquidation (see also Henochsberg *op cit* at 27)).

3.5 Claims in Reconvention

In *Van Zyl v Euodia Trust (Edms) Bpk* 1983 (3) SA 394 (T) and *Lister Garment Corporation (Pty) Ltd v Wallace NO* 1992 (2) SA 722 (D), the courts based their decision that claims in reconvention were not covered by section 13 on the rather narrow ground that section 13 referred to a plaintiff or applicant in any legal proceedings, and that, when an action was instituted and a counterclaim lodged, there was only one plaintiff in the proceedings. In *Compair SA (Pty) Ltd v Global Chemical Co (Pty) Ltd* 1985 (1) SA 532 (C), Aaron AJ indicated that a counterclaim was technically separate and distinct from the claim in convention, and that it might be competent in a proper case to order defendant to give security for the costs of the counterclaim. But where the issues in the actions in convention and reconvention were so closely related that if the court ordered a plaintiff in reconvention to give security for costs it might effectively be ordering it to give security for the costs brought about by its defence of the action in convention, it might exercise its discretion against ordering security (at 532–533). These three decisions were considered in *D-Jay Corporation CC v Investor Management Services (Pty) Ltd* 2000 (2) SA 755 (W). Wunsch J confirmed the persuasive value of English law regarding section 13, and held that a company that was a plaintiff in reconvention could be ordered to furnish security. Even if the court had the power, by virtue of a statute, to do so, it would not order security where the action in reconvention was essentially a defence to the action, or arose from the same transaction and went no further. He thought that the courts in *Van Zyl* and *Lister* had followed too technical an approach. Wunsch J preferred the view that a defendant who instituted a claim in reconvention, which could be entirely unrelated to the main claim, could not also be regarded as a plaintiff in the proceedings, especially if one had regard to the purpose of the legislation. He held that the defendant's claim in reconvention in the present case did not depend on the same facts but merely added a claim for damages, as had been the case in *Compair SA*. Instead, the defendant's claim in reconvention extended the enquiry beyond that arising from the main action, and the amount of the counterclaim substantially exceeded the sum claimed by the plaintiffs. The plaintiffs should not be put off the defence of the claim in reconvention for fear that the defendant would not be able to pay their costs (at 768I). So the defendant was ordered to furnish security for the costs of the claim in reconvention (at 770D). (So to my mind, the statement by Blackman and his co-authors (*op cit* at 2-7) — that

Wunsch J held that a defendant filing a claim in reconvention could not be ordered under section 13 to furnish security in respect of the costs of the counterclaim — is not correct.)

Section 8 of the Close Corporations Act 69 of 1984 clearly regulates the situation with regard to close corporations by providing that security may be sought not only when a corporation in legal proceedings is a plaintiff or applicant, but also when it brings a counterclaim or a counterapplication.

3.6 Proceedings in Magistrate's Court

Providing security in magistrate's court proceedings is regulated by rule 62 of the rules of the Magistrates' Courts. A defendant has a right to security irrespective of whether the company will be able to pay the costs. Section 13 (and section 8 of the Close Corporations Act) does not apply in these proceedings (see also Blackman et al op cit at 2-11; Henochsberg op cit at 28).

3.7 Proceedings on Appeal

In *Petz Products v Commercial Electrical Contractors* (supra) and *The Catamaran TNT: Dean Catamarans CC v Slupinsky (No 2)* 1997 (2) SA 577 (C), the courts found that an order relating to an application to provide security for costs was not an appealable judgment or order as contemplated by section 20 of the Supreme Court Act 59 of 1959, as it had been made in an interlocutory application and not in an action, and had no final or definitive effect upon the issues in the main litigation. The court held that the order for security for costs was clearly not a final order, as it could be varied by the Registrar under Uniform Rule 47(6). Also, the court that made the order could alter it at any time by increasing or reducing the amount of the security, or refer the matter to the Registrar to do so, or set aside its own order and discharge the plaintiff or claimant from its obligation to furnish security, should such security no longer be necessary (at 212B-C; see also *Montesse Township and Investment Corporation (Pty) Ltd v Standard Bank & another* 1964 (1) SA 14 (T); *Duncan NO v Minister of Law and Order* 1985 (4) SA 1 (T) at 2-3). This view was rejected by the Supreme Court of Appeal in *Shepstone & Wylie v Geyser* (supra) on the basis that a claim for security was a separate and ancillary issue between the parties, collateral to and not directly affecting the main dispute between the litigants. It was a measure of oblique relief sought by one party against the other on grounds foreign to the main issue — the financial position of one of the litigants. So the order determining this collateral dispute was definitive and final, for at no later stage in the proceedings could the applicant obtain the substance of what had been refused to him or her (see *Ecker v Dean* 1937 SWA 3 at 4). The court held that although Uniform Rule 47 allowed the Registrar to vary the order, this did not alter the position

where an order for security had been refused. A court's power to entertain a subsequent application for security did not affect the finality of the order in the previous application (at 1042H). The court did not decide whether the grant, as opposed to the refusal, of such an application was subject to appeal. In *Bookworks (Pty) Ltd v Greater Johannesburg Transitional Metropolitan Council & another* 1999 (4) SA 799 (W), the court held that it was, and that the power vested in the Registrar to increase the amount of security did not preclude an appeal against an order directing security to be furnished. But Cloete J cautioned that appeals against the exercise of the discretion conferred by section 13 should be discouraged in the absence of some demonstrable blunder or unjustifiable conclusion on the part of the trial court. If they were not so discouraged, the decision on the merits of a matter before the court would be delayed by an appeal relating to an application that marked no stage in the progress of the case, and was quite outside and incidental to it (at 808C). The court regarded the discretion given to it by the word 'may' in section 13 as narrow, which meant that the power to interfere on appeal was limited to cases in which it was found that the court vested with the discretion did not exercise it judicially. This could be done by 'showing that the court of first instance exercised the power conferred by the section capriciously or upon a wrong principle, did not bring its unbiased judgment to bear on the question, or did not act for substantial reasons' (at 804H–I; for general comments on the power to interfere on appeal in matters of discretion, see also *Benson v SA Mutual Life Assurance Society* 1986 (1) SA 776 (A) at 781–782, and the cases referred to there). In *Northbank Diamonds v FTK Holland* (supra), Strydom CJ supported this view for three reasons. In the first instance, concerns regarding costs have invariably been held to involve the exercise of a discretion in a narrow sense. Secondly, when section 13 is combined with Uniform Rule 47, as it must be to give it practical effect, the court is effectively regulating its own procedure. This is also a matter that involves a discretion in the narrow sense. Thirdly, the discretion involves the exercise of a value judgment, and there may well be a legitimate difference of opinion as to the appropriate conclusion (at 196D–I).

4 Procedure

A party who is entitled to and desires security for costs against a corporation claims such security under Uniform Rule 47. If a notice was served under Uniform Rule 47(1) and this demand was undisputed and the security for costs furnished, there is no need for an application to court for an order to furnish security (*Petz Products v Commercial Electrical Contractors* supra at 208–209; Blackman et al op cit at 2–10). Should the amount of security to be furnished be in dispute, the Registrar resolves the dispute under Uniform Rule 47(2), again without the need for a court order. Similarly, if the security to be provided has to be increased later, the Registrar determines the amount of the increase under

Uniform Rule 47(6) without the need for a court order authorizing him or her to do so. So the court is not precluded from granting an order enforcing a determination by a taxing master of an increase in security to be furnished, where the original security was furnished on an uncontested basis in compliance with a Uniform Rule 47(1) notice (*Petz Products v Commercial Electrical Contractors* (supra); Blackman et al op cit at 2-10).

If liability for payment of security is denied, the party claiming it proceeds by delivering a notice demanding security in terms of section 13 of the Companies Act or section 8 of the Close Corporations Act. The court may determine the amount and nature of the security, or authorize the Registrar to do so. Once the Registrar has determined the amount, he or she cannot increase it but the court may later do so (*Sasol Marketing Co Ltd v Allied Stationers (Pty) Ltd* 1961 (1) SA 370 at 371; *Montesse Township & Investment Corp (Pty) Ltd v Standard Bank* (supra)). When a court orders security to be provided, it may authorize the defendant or respondent to seek further security on the papers in the original application, supplemented as may be necessary (*Cometal-Mometal SARL v Corliana Enterprises (Pty) Ltd* 1981 (4) SA 662 (W)). The court may stay the proceedings until the security is furnished by a determined date and has the inherent power to dismiss the proceedings in the event of non-compliance with the order (*Excelsior Meubels Bpk v Trans Unie Ontwikkelingskorporasie Bpk* 1957 (1) SA 74 (T); see also *Gisman Mining and Engineering Co (Pty) Ltd v LTA Earthworks (Pty) Ltd* 1977 (4) SA 25 (W), where a postponement for an application for security at the request of the company was granted conditionally on a stay of the proceedings until the application had been determined).

5 Proof of Inability to Pay Costs

The phrase 'there is reason to believe' places a much lighter burden of proof on an applicant than, for example, 'the court is satisfied' (*Vumba Intertrade CC v Geometric Intertrade CC* 2001 (2) SA 1068 (W), regarding section 8 of the Close Corporations Act; on the corresponding provision in company law, see the similar views in, for example, *Trust Bank van Afrika v Lief* supra at 755D; *Agro Drip (Pty) Ltd v Fedgen Insurance Co Ltd* 1998 (1) SA 182 (W) at 186E; *Northbank Diamonds v FTK Holland* (supra)). The 'reason to believe' should, however, be founded on facts that give rise to such belief. A blind belief, surmise, speculation, or even a belief that is not supported by the necessary facts, or that is based on such information or hearsay evidence as a reasonable person ought or could not give credence to, does not suffice (*Vumba Intertrade v Geometric Intertrade* supra at 1071F-H; *Northbank Diamonds v FTK Holland* supra at 194E; see also *Native Commissioner and Union Government v Nthako* 1931 TPD 234 at 242; *London Estates (Pty) Ltd v Nair* 1957 (3) SA 591 (D) at 592F). So there should be sufficient facts before the court to enable it to conclude that there is reason to believe that a plaintiff company or

close corporation will be unable to satisfy an adverse court order. The burden of adducing such facts rests on the applicant (*Vumba Intertrade v Geometric Intertrade* supra at 1071H).

The burden to prove that there is reason to believe that the respondent (the plaintiff in the main action) will be unable to pay costs rests on the applicant (the defendant in the main action). The applicant may be assisted by material or facts put before the court by the respondent company. Where the matter is peculiarly within the knowledge of a respondent, various courts have held that less evidence would suffice to establish a prima facie case than was generally required (*Gericke v Sack* 1978 (1) SA 821 (A) at 827E–G; *Monteoli v Woolworths (Pty) Ltd* 2000 (4) SA 735 (W) at 742D–G). But less evidence did not open the door for surmise or speculation. In *Northbank Diamonds v FTK Holland* supra at 194G, Strydom CJ held that the words ‘credible testimony’ in section 13 connoted no more than evidence capable of being believed. These words do not appear in section 8 of the Close Corporations Act and I do not think that they add any additional requirement to section 13.

The usual method applied by a corporation to resist an application to furnish or to increase security is to furnish its balance sheet so that the court can see by how much the corporation’s assets exceed its liabilities (see, generally, *Milne v Sadowa Minerals (Pty) Ltd* 1956 (2) SA 89 (W); *Equitable Trust and Insurance Co of SA Ltd v Registrar of Banks* 1957 (1) SA 689 (T) at 691D–F; *Henry v RE Designs CC* 1998 (2) SA 502 (C); *Petz Products v Commercial Electrical Contractors* supra at 206E–G; *Blackman et al* op cit at 2-11). In an appropriate case, a respondent’s failure to produce its balance sheet may actually lead to the inference that, were it to do so, it would have no answer to the applicant’s claim for security for costs (*Petz Products v Commercial Electrical Contractors* supra at 206G; *Henry v RE Designs* supra at 513). But there is no rule that allows a defendant, on demand, to require a plaintiff corporation to disclose its financial statements, failing which it will be ordered to furnish security for the defendant’s costs (*Vumba Intertrade v Geometric Intertrade* supra at 1072A). The need for furnishing a balance sheet would depend on all the information put before the court (*Northbank Diamonds v FTK Holland* supra at 199A). Also, an order to provide security does not depend on the company having liquid funds ready and available to pay for the legal costs. It is sufficient for the company to show that it has free assets that can easily be liquidated, or in respect of which the necessary funds can be raised to pay an order for costs (at 199I).

6 The Discretion of the Court

Section 13 requires an investigation in two stages. In the first instance, the court must consider whether an applicant has established by credible testimony that there is reason to believe that the company or body corporate, if unsuccessful, will not be able to pay the costs of the

defendant applicant. If the court is not so satisfied, the matter rests there. But if the court is so satisfied, it must, secondly, exercise the discretion conferred on it by section 13 (*Northbank Diamonds v FTK Holland* supra at 193I; *Vumba Intertrade v Geometric Intertrade* supra at 1071E; *Henry v RE Designs* supra at 508). Prior to the decision by the Supreme Court of Appeal in *Shepstone & Wylie v Geyser* (supra), it was widely accepted that once it had been established that there was reason to believe that a company would not be able to pay a costs order if unsuccessful in its litigation, a defendant or respondent should not be deprived of the benefit to be furnished with security for costs, unless there were special circumstances (*Northbank Diamonds v FTK Holland* supra at 195A; *Petz Products v Commercial Electrical Contractors* (supra); *Cometal-Mometal SARL v Corliana Enterprises* supra at 663F–G; *Trust Bank v Lief* supra at 754H; *Fraser v Lampert* NO 1951 (4) SA 110 (T) at 115B). In *Lappeman Diamond Cutting Works v MOB Group* (supra), Joffe J held that the discretion contained in section 13 should be approached neither with a predisposition to granting security, nor with the predisposition not to grant it (at 919H). In this sense the discretion may be regarded as wide and section 13 as constitutionally sound (at 919H; Blackman et al op cit at 2-8). In *Shepstone & Wylie v Geyser* supra at 1045I, Hefer JA also preferred to approach each case upon a consideration of all the circumstances, without adopting a predisposition either in favour of or against the granting of security. The task of the court was considered to be a balancing exercise: it weighed, on the one hand, the injustice to the plaintiff if it were prevented from pursuing a proper claim by an order for security, and, on the other hand, the injustice to the defendant if no security were ordered and the defendant later found himself unable to recover costs from an unsuccessful plaintiff. (A similar approach was followed by Peter Gibson LJ in *Keary Developments Ltd v Tarmac Construction Ltd & another* [1995] 3 All ER 534 (CA) at 540a–b.) I believe that this approach is correct. It has been followed in later decisions (for example, *Commissioner, South African Revenue Service & another v East Coast Shipping (Pty) Ltd* 2000 (4) SA 533 (D) at 536–538).

In *Shepstone & Wylie v Geyser* supra at 1046G, the court also noted that the fact that an order for security would put an end to the litigation did not by itself provide sufficient reason for refusing it.

The merits of the dispute are not relevant. A court should not enquire into them or express any opinion on the prospects of success, unless it is clear that the plaintiff's action is not bona fide, or is vexatious or hopeless (*Commissioner, SARS v East Coast Shipping* supra at 540; Blackman et al op cit at 2-9).

8 Conclusion

The philosophy underpinning section 13 of the Companies Act and section 8 of the Close Corporations Act is that a company or close corporation should not enjoy the normal common-law immunity from providing security for the costs of legal proceedings. This protects the public in litigation by bankrupt corporations. The bankrupt corporation is not excluded from the court but is prevented from causing injustice to its opponent by conducting litigation while it is unable to pay its costs if it is unsuccessful.

If a court is satisfied that a corporation will, if unsuccessful in the legal proceedings, be unable to satisfy the order for costs, it may, in its discretion, order the corporation to furnish security for those costs. The constitutional right of every person, including a juristic person, to equality before the law and to equal protection of the law demands that courts should exercise their discretion to order security without any prior predisposition in favour of granting or refusing such order.

The parameters for the application of the sections and the exercise of the courts' discretion in these cases need to be defined clearly so that all parties to corporate litigation may be treated fairly. The judgments in *Lappeman Diamond Cutting Works v MOB Group* (supra), *Shepstone & Wylie v Geyser* (supra), *Northbank Diamonds v FTK Holland* (supra), and *Vumba Intertrade v Geometric Intertrade* (supra) have, to my mind, contributed substantially to legal certainty.
