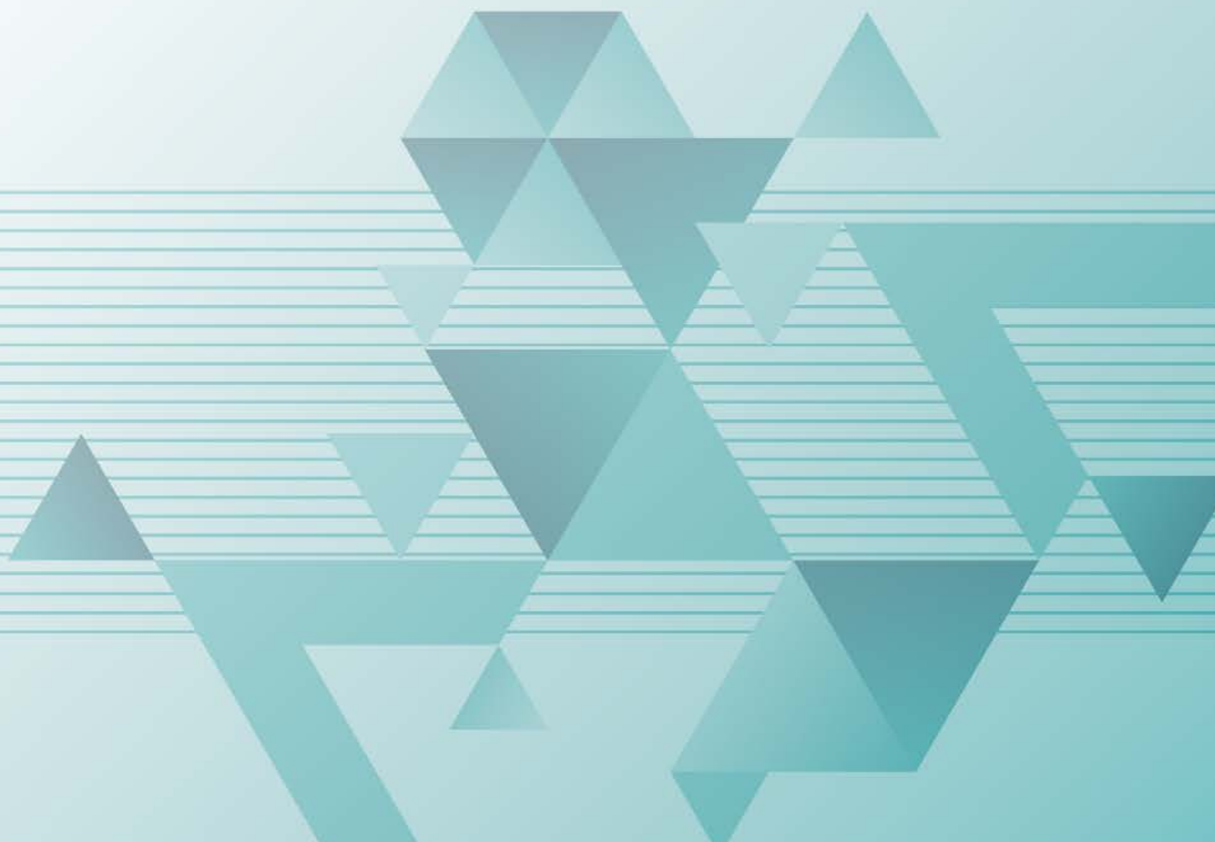
PROGRAMME IN SOUTH AFRICAN BUSINESS RESCUE

COURSE NOTES 2023



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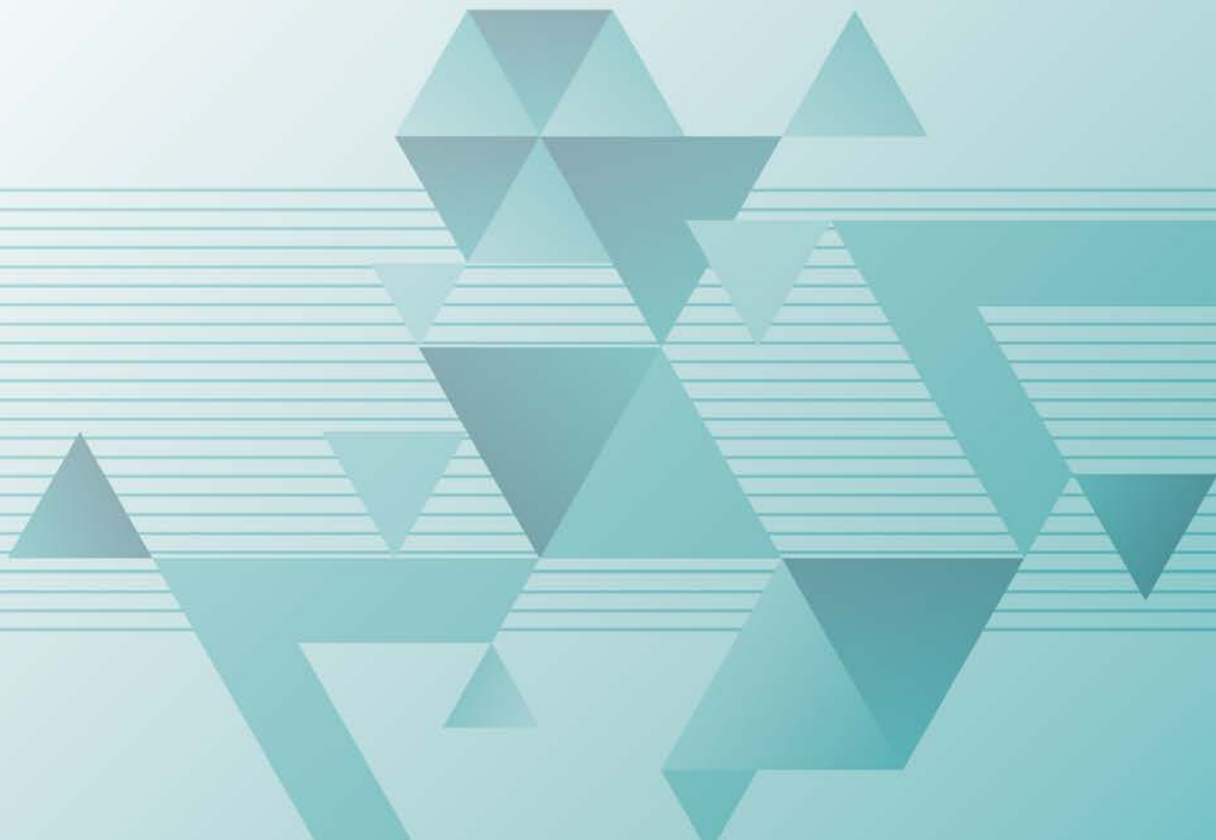

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CHAPTER 1

INTRODUCTION TO BUSINESS RESCUE

1.1 Introduction to the Programme in South African Business Rescue

For more than 25 years, SARIPA (and its predecessor organisation, AIPSA) have presented a course on South African insolvency law and practice (the insolvency course). The course evolved over a long period of time, but has for the most part always dealt with all aspects of South African insolvency law.

With the introduction of a new procedure called "business rescue" in 2011 (consisting of Chapter 6 of the Companies Act 71 of 2008),[1] the insolvency course had to be adjusted to make provision for this new procedure. This was done by introducing a new chapter to the existing course notes. Being a new procedure, it was not long before a plethora of new case law, books and articles dealing with this new procedure came to the fore. Adding all this new precedent and literature to the course notes soon resulted in the course notes becoming unwieldy. With the new business rescue procedure having created a new profession of business rescue practitioners (as opposed to insolvency practitioners who are appointed to do the insolvency work), it soon became clear that SARIPA should look at presenting two separate courses for its members, one dealing with insolvency law and practice and one dealing with business rescue.

The notes contained within these pages are the result of the decision to present a separate, discrete course on the business rescue procedure. However, despite the legislation creating a new profession, both insolvency and business rescue are in principle insolvency procedures and the two cannot be entirely separated from each other. An insolvency practitioner should have a good working knowledge of business rescue, and a business rescue practitioner should have a good working knowledge of insolvency. There is also a degree of overlap between the two procedures. It is for this reason that the course in insolvency law and practice contains a brief overview of the most important principles of business rescue, and why the business rescue course contains a section dealing with insolvency (See Chapter 14 in this regard). It is within this context that the two courses are presented by SARIPA.

In this course, we will examine the (pertinent) provisions of Chapter 6 of the Companies Act 2008 and the practical implementation of the business rescue process with reference to the various rulings and judgements by our courts in respect of business rescue. Once the course has been completed, candidates will have a sound grasp of the Chapter 6 mechanism, in particular the practical and intricate workings of the provisions.

Business rescue is a process that is dynamic and remains a developing area of South African law. The course will take into account ongoing development of the law, changes in practical approaches to the relevant provisions of the Companies Act 2008 and having regard to the manner in which practitioners apply the restructuring process in practice.

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[1] Hereinafter referred to as the Companies Act 2008.

1.2 Aims / objectives of the course

The programme focuses on providing a sound theoretical understanding of the basic principles of the South African business rescue procedure. While the emphasis is on providing a sound theoretical understanding of the principles, the course will also provide candidates with a sound practical understanding of the business rescue process.

While the course is presented entirely online, where necessary support and guidance will be provided to candidates registered on the course.

The aims and objectives of the course can be set out as follows:

Aims

After having completed the course, candidates should have a good understanding of the following:

- background to the development of the business rescue process in South Africa, as contained in Chapter 6 of the Companies Act 2008;
- application of the various pieces of primary and secondary legislation, as well as case law, governing corporate rescue in South Africa;
- understanding basic financial statements and information required to propose a business rescue plan and the approval of such plan;
- effective engagement with stakeholders;
- ethical conduct of business rescue practitioners;
- understanding the various legislation and rules for bringing a company under supervision as well as the various legislation and rules bringing the process to an end.

Objectives

After having completed the course, candidates on the course should be able to:

- answer direct and multiple-choice type questions relating to the content of the course;
- write an essay on any aspect of business rescue in South Africa;
- answer questions based on a set of facts relating to business rescue in South Africa;
- draft a business rescue plan based on a predetermined set of facts.

1.3 Scope of the course

Business rescue is interesting, but can also be an extremely challenging subject. It is obviously not possible to deal with all the legal problems that may be experienced by a business rescue practitioner in practice. It is also not expected of a business rescue practitioner to deal with all legal problems personally, as a practitioner is entitled to employ external professionals to deal with the problems they encounter.

1.4 Recommended textbooks for further reference

Candidates who require more information on the issues covered in these notes are referred to the textbooks below. Please note that in places in the notes, reference is made to some of these publications. **Students are NOT required to purchase these books for the purposes of this course**.

- *Henochsberg on the Companies Act 71 of 2008 Vol II*, P Delport and Q Vorster (LexisNexis, loose-leaf publication) (referred to as Henochsberg in these notes);
- *Levenstein, South African Business Rescue Procedure,* E Levenstein (LexisNexis loose-leaf publication) (referred to as Levenstein in these notes); and
- *Meskin, Insolvency Law and its operation in winding-up*, J Kunst, A Boraine and D Burdette (LexisNexis loose-leaf publication) (Chapter 18).

However, students are expected to have access to the following statutes (which can be downloaded for free from the Internet):

- Chapter 2, part G (sections 79-83) and Chapter 6 of the Companies Act 2008;
- Chapters 1 and 14 of the Companies Act 1973; and
- Insolvency Act of 1936.[2]

1.5 General introduction and a bird's eye view of the business rescue procedure

The restructuring of companies in financial distress is on the increase globally. The worldwide trend is to attempt to rehabilitate distressed companies, instead of simply liquidating them. In line with this global trend, Chapter 6 of the Companies Act 2008 has introduced business rescue to the South African legal landscape. Business rescue is a fairly new process aimed at the restructuring of companies in financial distress, which fundamentally rewrites South African company law from a restructuring perspective and has far-reaching effects on the rescue of companies.[3] South African companies that are financially distressed now have an opportunity to

[2] Hereinafter referred to as the Insolvency Act.
[3] See Levenstein 7-1 – 7-6. See also Henochsberg 449 - 450.

reorganise and restructure, which accords with the "corporate rescue culture" and other international standards of corporate rescue that exist in established restructuring regimes in several overseas jurisdictions, such as Chapter 11 of the US Bankruptcy Code, administration under the Insolvency Act 1986 (England and Wales) and voluntary administration under the Australian Corporations Act 2001.[4]

Prior to the introduction of business rescue on 1 May 2011, judicial management, as provided for in Chapter 15 of the Companies Act 61 of 1973,[5] was the sole means by which companies experiencing financial difficulties could avoid being wound-up. However, judicial management was not a success in South Africa and was never really accepted as an effective corporate restructuring mechanism and a viable alternative to liquidation. The "dismal failure" of judicial management in South Africa has been attributed to the fact that the judicial management legislation was outdated, highly formalistic and creditor-oriented.[6]

Business rescue has now replaced judicial management.[7] At the outset it must be emphasised that business rescue is materially different from the old judicial management procedure. The general philosophy permeating through the business rescue provisions is the recognition of the value of the business as a going concern rather than the juristic person itself. Hence the name "business rescue" and not "company rescue". This is in line with the modern trend in rescue regimes.

Business rescue attempts to secure and balance the opposing interests of creditors, shareholders and employees. It encapsulates a shift from creditors' interests to a broader range of interests, that is, a shift from a creditor-focused culture of liquidation to a rescue-oriented approach.[8] The objective of business rescue is to preserve the business, coupled with the experience and skill of its employees, which may in the end prove to be a better option for creditors in securing the full recovery of the debt.[9]

It is clear that the legislature has recognised that the liquidation of companies more frequently than not occasions significant collateral damage, both economically and socially, and is often value destructive.[10] Therefore, the focus is now on saving companies rather than destroying them. This has, amongst others, the effect of:

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4 *Koen and Another v Wedgewood Village Golf & Country Estate (Pty) Ltd* (24850/11) [2011] ZAWCHC 464 (9 December 2011); [2012] JOL 29024 (WCC); 2012 (2) SA 378 (WCC), at *para 13.* See also Levenstein 6-10.

5 Hereinafter referred to as the Companies Act 1973.

6 See Levenstein 3-5 – 3-11.

7 *Merchant West Working Capital Solutions (Pty) Ltd v Advanced Technologies and Engineering Company (Pty) Ltd and Another* (13/12406) [2013] ZAGPJHC 109 (10 May 2013 at para 12); and *MFV "Polaris": Southern African Shipyards (Pty) Ltd v MFV "Polaris" and Others* [2018] 3 All SA 2019 (WCC).

8 *The Employees of Solar Spectrum Trading 83 (Pty) Limited v Afgri Operations Limited* (Case No 6418/2011, High Court Pretoria, 8 May 2012 at 9).

9 *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* 2012 (3) SA 273 (GSJ) at 12.

10 *Collard v Jatara Connect (Pty) Ltd* 2018 (5) SA (WCC), at para 16; *Van Niekerk v Seriso 321 CC* (Case Number 2011135199, High Court Johannesburg, 20 March 2012); and *Cardinet (Proprietary) Limited v Wedgewood Golf and Country Estate (Pty) Limited (in liquidation)* (Case No 19599/2012) WCHCC (30 January 2013) at 53.

(i) maximising returns for creditors;

(ii) avoiding the piece meal sale of assets at "fire-sale" values;

(iii) retaining and preserving the goodwill of the business of the company; and

(iv) keeping businesses afloat in order to preserve employment.

This chapter seeks to provide a bird's eye view of the business rescue process, and further sets out:

(a) the important definitions in business rescue;

(b) the debtor-focused approach of Chapter 6 of the Companies Act 2008 (as opposed to the creditor-focused approach seen in traditional insolvency law);

(c) the two objectives of business rescue; and

(d) when business rescue may be most appropriate. Lastly, a broad overview of the course will be discussed.

1.6 Important definitions

Having some knowledge of the new restructuring dispensation introduced by Chapter 6 of the Companies Act 2008 is essential in this day and age, as most companies may be exposed to business rescue at various levels. Chapter 6 of the Companies Act 2008 specifically constitutes a set of carefully crafted rules to provide for the efficient rescue of financially distressed companies. In order to fully comprehend the business rescue procedure, it is necessary to understand the terminology used by the legislature. Accordingly, the following definitions must be noted.

1.6.1 "Affected person"

Section 128(1)(*a*) of the Companies Act 2008 defines "affected person" as follows:

"'Affected person', in relation to a company, means -

(a) a shareholder or creditor of the company;

(b) any registered trade union representing employees of the company; and

(c) if any of the employees of the company are not represented by a registered trade union, each of those employees or their respective representatives;"

The term "affected person" refers to all persons who are stakeholders within the business rescue context. It must be noted that the various stakeholders, including employees and trade unions, play significant roles in business rescue proceedings, which is in contrast to the position in a company's liquidation.

1.6.2 "Business rescue"

"'Business rescue' means proceedings to facilitate the rehabilitation of a company that is financially distressed by providing for -

(a) the temporary supervision of the company, and of the management of its affairs, business and property;

(b) a temporary moratorium on the rights of claimants against the company or in respect of property in its possession; and

(c) the development and implementation, if approved, of a plan to rescue the company by restructuring its affairs, business, property, debt and other liabilities, and equity in a manner that maximises the likelihood of the company continuing in existence on a solvent basis or, if it is not possible for the company to so continue in existence, results in a better return for the company's creditors or shareholders than would result from the immediate liquidation of the company."[11]

1.6.3 "Business rescue practitioner"

"Business rescue practitioner" means a person appointed, or two or more persons appointed jointly, in terms of Chapter 6 of the Companies Act 2008 to oversee a company during business rescue proceedings and "practitioner" has a corresponding meaning.

1.6.4 "Court"

"Court", depending on the context, means either-

(a) the High Court that has jurisdiction over the matter; or

(b) either-

[11] *Griessel and Another v Lizemore and Others* 2016 (6) SA 236 (GJ), at para 80.

(i) a designated judge of the High Court that has jurisdiction over the matter, if the Judge President has designated any judges in terms of section 128(3) of the Companies Act 2008; or[12]

(ii) a judge of the High Court that has jurisdiction over the matter, as assigned by the Judge President to hear the particular matter, if the Judge President has not designated any judges in terms of section 128(3) of the Companies Act 2008.

The definition of "court" makes clear that the supervision of business rescue proceedings falls within the jurisdiction of the High Court. Business rescue proceedings affect the rights of several stakeholders and creditors. The High Court is therefore best placed to balance the rights and interests of all the relevant parties. It is submitted that the role of courts and their involvement in business rescue matters is an important and key rescue theme.[13]

1.6.5 "Financially distressed"

"Financially distressed", in reference to a particular company at any particular time, means that -

(a) it appears to be reasonably unlikely that the company will be able to pay all of its debts as they become due and payable within the immediately ensuing six months; or

(b) it appears to be reasonably likely that the company will become insolvent within the immediately ensuing six months.

The test for financial distress is, accordingly, forward-looking and is intended to allow directors of companies to look into the future to determine whether the company is reasonably likely to run into cash-flow problems in the immediate ensuing six-month period. This six-month period was determined to be a sufficient period of time to allow directors to consider business rescue before it is too late.

The definition of "financial distress" envisages both a cash-flow and a balance sheet test to determine whether a company is financially distressed. Accordingly, in order to determine the eligibility of a company to enter into business rescue, one must consider whether a company will be either:

(a) factually insolvent (that its liabilities will exceed its assets); or

(b) commercially insolvent (unable to pay its debts as they become due and payable) in the next six-month period.

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[12] See the *Commercial Court Practice Directive* for the Gauteng and Gauteng Local Divisions of the High Court issued by the Judge President of the Gauteng Divisions of the High Court of South Africa on 3 October 2018. If a case is allocated as a Commercial Court case, the Judge President or Deputy Judge President allocates a judge or two judges to case manage the matter. The "Commercial Court aims to promote efficient conduct of litigation in the High Court and resolve disputes quickly, cheaply, fairly and with legal acuity".

[13] See Levenstein 7-18.

It must be noted that there is a clear distinction between "insolvent" and "financial distress". Only companies that are financially distressed should be allowed to file for business rescue.[14]

1.7 Overview of the business rescue procedure

1.7.1 The creditor-focused versus the debtor-focused approach

Traditionally, South African insolvency law (including the legislation governing the winding-up of companies) could be regarded as a "pro-creditor" regime. However, in contrast, the business rescue process is characterised by an emphasis on the balancing of the rights and interests of all relevant stakeholders, in a manner that promotes value preservation and avoids the negative consequences of liquidation. Accordingly, there has been a marked shift away from the traditional pro-creditor manner of thinking to a corporate rescue culture where the needs of the debtor are considered and where the debtor may potentially obtain a fresh start.[15]

The objective is to provide distressed companies with a "breathing space" where the interests of the "debtor" become paramount. Prior to 2011, South Africa's focus was far more weighted to the rights and interests of the creditor, as opposed to the struggling company and which was in dire need of a compromise of its debt. In the case of a company that cannot pay its debts (commercial insolvency) or where it is insolvent on its "balance sheet" (factual insolvency), there will be a need for an independent supervisor to be appointed so as to take control of the debtor's affairs with the aim of restructuring the company's debt, contracts, shareholding, employees and business. The ultimate objective is to publish and have approved a business rescue plan that, once implemented, takes the company into a position where it can continue to trade into the future on a solvent basis. If this is not possible, the business rescue plan must provide a better distribution to creditors than would be available if the company was to be immediately liquidated.

The process is aimed at balancing the rights and interests of all stakeholders (affected persons), but certainly with the aim of allowing the survival of the debtor company going forward.

1.7.2 Two objectives of business rescue

Business rescue proceedings are proceedings that are aimed at facilitating the rehabilitation of a company that is financially distressed by providing for:

(a) the temporary supervision of the company and the management of its affairs by a business rescue practitioner;

(b) a temporary moratorium (stay) on the rights of claimants against the company; and

(c) the development and implementation, if approved, of a business rescue plan to rescue the company by restructuring, amongst other things its business, property and debt.

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[14] See Levenstein 7-26 – 7-27. See also Henochsberg 457.
[15] See Levenstein 2-1.

The business rescue process is essentially aimed at restructuring the affairs of a financially distressed company in a way that either maximises the likelihood of such company continuing in existence on a solvent basis or, alternatively, results in a better return for creditors or shareholders of the company than would ordinarily result from the immediate liquidation of the company.

As set out above, the definition of "business rescue" envisages two goals, the first being the development and implementation of a plan to rescue the company, which plan has the aim of allowing the company to continue in existence on a solvent basis. This is referred to as the first part of the business rescue definition, which centres around the idea that there will be some form of restructuring and revival of the company's business, which will allow the company to continue on a solvent and viable basis into the future.

The second goal of business rescue has very little to do with the rehabilitation of the company, but instead contemplates what has become known as a "quasi-liquidation" or a "controlled wind-down" whereby the assets or business of the company are sold and in terms of which a better return (dividend) for creditors, in comparison to that which they would have received from the immediate liquidation of the company, results.

Thus, the definition of business rescue contemplates two objects or goals: a primary goal which is to facilitate the continued existence of the company in a state of solvency and a secondary goal, which is provided for as an alternative, in the event that the achievement of the primary goal does not prove to be viable, namely to facilitate a better return for creditors or shareholders than would result from immediate liquidation.[16]

1.7.3 Entry routes into business rescue

There are two entry routes into the business rescue process. The first route is a company resolution (voluntary commencement) and the second is a formal court application by an affected person (compulsory commencement). In terms of section 129(1) of the Companies Act 2008, a company's board of directors can pass a resolution in terms of which the company resolves to commence the business rescue process. In order for a company to commence business rescue proceedings on a voluntary basis, the board must have reasonable grounds to believe that the company is financially distressed and that there appears to be a reasonable prospect of rescuing the company.[17]

Compulsory business rescue, on the other hand, begins with an affected person (creditor, shareholder, registered trade union, employee or employee representative) applying to the High Court to place the company concerned in business rescue. In this regard, section 131 of the Companies Act 2008 provides that unless a company has adopted a resolution to begin

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[16] See Levenstein 7-8 – 7-15. See also Henochsberg 450 – 451.

[17] The board of a company may file a resolution with the CIPC that the company begins business rescue proceedings and must appoint a business rescue practitioner who satisfies the requirements of the Companies Act 2008. The board must have reasonable grounds to believe that the company is financially distressed and that there appears to be a reasonable prospect of rescuing the company.

business rescue proceedings, an affected person may apply to a court at any time with notice to each affected party "in the prescribed manner" for an order placing a company under supervision and commencing business rescue proceedings. It is important to note that the company and its directors (in their capacities as such) are not authorised to apply for a business rescue order under section 131.

In order to succeed with an application in terms of section 131, any one of the following jurisdictional requirements must be demonstrated, namely:

(a) that the company is financially distressed; or

(b) the company has failed to pay over any amount in respect of an obligation under or in terms of a public regulation, or contract, with respect to employment-related matters; or

(c) it is otherwise just and equitable to do so for financial reasons.

Irrespective of which jurisdictional requirement is present, in each instance there must also be a reasonable prospect for rescuing the company.

The entry routes into business rescue are dealt with in detail in Chapter 2 below.

1.7.4 The business rescue practitioner

Once business rescue proceedings have commenced, whether by a company resolution or court application, the commencement process leads to the appointment of a business rescue practitioner who is tasked with supervising the company during its business rescue proceedings.[18]

In the case of voluntary business rescue, a business rescue practitioner (who satisfies the requirements of the Companies Act 2008 and who has consented in writing to accept the appointment) is appointed by the company. However, in instances where the business rescue proceedings commence on a compulsory basis, the applicant seeking an order commencing business rescue must nominate a business rescue practitioner for appointment in its application.

During a company's business rescue proceedings, the business rescue practitioner plays a critical role and, accordingly, in addition to any other powers and duties set out in Chapter 6, the business rescue practitioner has full management control of the company in substitution for its board and pre-existing management. The business rescue practitioner is focused on developing a business rescue plan in consultation with all affected persons and to have that plan published for approval by all affected persons. Once approved, the plan must be implemented (at least to substantial implementation stage), allowing the business rescue practitioner to exit from the process.

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[18] See Levenstein 8-1. See also Henochsberg 462.

The business rescue practitioner is dealt with in more detail in Chapter 8 below.

1.7.5 *The moratorium*

A primary aim of business rescue proceedings is to offer a distressed company some breathing space to allow its affairs to be restructured in such a way as to allow it to continue to operate as a going concern. This is achieved through a general moratorium (stay) on claims. The moratorium on claims is a fundamental aspect of any successful rescue mechanism, aimed at the restructuring of the debt of a company that is financially distressed.[19]

Section 133 of the Companies Act 2008 provides that during business rescue proceedings,[20] no legal proceeding, including enforcement action, against the company, or in relation to any property belonging to the company, or lawfully in its possession, may be commenced or proceeded with in any forum, except with the written consent of the practitioner or with the leave of the court and in accordance with any terms the court considers suitable.

The moratorium is dealt with in more detail in Chapter 3 below.

1.7.6 *Post-commencement finance*

After being placed into business rescue, the financially distressed company will require ongoing finance to keep it operating and trading in the marketplace. Accordingly, post-commencement finance has been referred to as the life-blood of the company while it is under business rescue.

Post-commencement finance is funding that is provided to the company after the date of commencement of business rescue proceedings. In view of the importance of securing some level of ongoing finance in order to continue functioning in the marketplace, the Companies Act 2008 provides statutory protection and elevates the status of such funding above the claims of the company's pre-business rescue creditors.

Post-commencement finance is dealt with in more detail in Chapter 5 below.

1.7.7 *The business rescue plan*

The proposal and implementation of the business rescue plan is a critical aspect of the business rescue process. In terms of section 150(1) of the Companies Act 2008, the business rescue practitioner has a duty to prepare a business rescue plan for consideration and possible adoption, after consulting with creditors, other affected persons, and the management of the company. The business rescue plan is the road map which must be followed if the company is to be rescued and, as such, it must contain all the information reasonably required to facilitate affected persons in deciding whether or not to accept or reject the plan. An adopted plan is

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[19] See Levenstein 9-3 – 9-29. See also Henochsberg 522.

[20] In *Investec Bank Ltd v Bruyns* 2012 (5) SA 430 (WCC), at para 12, the court left open the question as to whether the business rescue proceedings commence on the launching of the application or only retrospectively after the making of a court order.

binding on the company in business rescue and all the creditors and holders of the company's securities. A business rescue plan is adopted by creditors (subject to approval by holders of securities if their interests are affected) if it is supported by 75% of creditors' voting interests and 50% of independent creditors' voting interest.

The business rescue plan is dealt with in more detail in Chapter 10 below.

1.7.8 Creditors

South Africa, at least in theory, has moved away from a creditor-driven rescue regime to a more debtor-oriented approach. However, despite this, the participation of creditors during the business rescue process remains paramount, especially in relation to the voting process in approving and a business rescue plan.[21] Section 145 of the Companies Act 2008 allows creditors to participate in court proceedings (generally by intervening in the court application brought in terms of section 131) and to participate both formally and informally in various aspects of the company's business rescue proceedings. Creditors are also entitled to be consulted by the business rescue practitioner during the development of the business rescue plan and may form a creditors' committee.

The role of creditors in the business rescue process is dealt with in more detail in Chapter 9 below.

1.7.9 Directors

Section 137(2) of the Companies Act 2008 provides that during the course of a company's business rescue proceedings, each director of the company must continue to exercise the functions of director but subject to the authority of the business rescue practitioner. The Companies Act 2008 further provides that the directors of the company have a duty to continue to exercise management functions within the company in accordance with the express instructions or direction of the business rescue practitioner, to the extent that it is possible to do so. Lastly, directors are required to attend to the requests of the business rescue practitioner at all times and provide any information about the company's affairs as may be reasonably required by the practitioner. It is important to note that if during a company's business rescue proceedings the board, or one or more directors of the company, purports to take any action on behalf of the company that requires the approval of the business rescue practitioner, that action is void unless ii is in fact approved by the business rescue practitioner.

The role of directors and their participation in the business rescue process is dealt with in more detail in Chapter 7 below.

[21] See Levenstein 9-62 – 9-63.

1.7.10 Employees

Employees are specifically catered for in the business rescue context in that they are not only afforded preferences in the ranking of claims, but are also given the opportunity to participate in the business rescue proceedings themselves.[22] It is therefore evident that employees stand to gain substantial benefits from business rescue proceedings in comparison with a liquidation scenario. It must be noted that, during a company's business rescue proceedings, employees of the company immediately before the beginning of those proceedings continue to be so employed on the same terms and conditions, and employment agreements can only be amended to the extent that changes occur in the ordinary course of attrition; or where the employees and the company, in accordance with applicable labour laws, agree different terms and conditions. It is also important to note that employees' salaries that become due and payable by the company during the business rescue proceedings, are regarded as post-commencement finance and thus have preferential status over other claims.

The role of employees in the business rescue process is dealt with in more detail in Chapter 6 below.

1.7.11 Shareholders

The business rescue practitioner must engage with and manage the expectations of shareholders and the holders of company's securities in order to properly manage the restructuring process. Section 137(1) provides that during business rescue proceedings, an alteration in the classification or status of any issued securities of a company, other than by way of a transfer of securities in the ordinary course of business, is invalid except to the extent

(a) that the court otherwise directs; or

(b) contemplated in an approved business rescue plan.

Shareholders are also given the opportunity to participate in court proceedings and the business rescue proceedings, and must be notified of court proceedings, decisions and meetings, pursuant to section 146 of the Companies Act 2008.

The role of shareholders in the business rescue process is set out in more detail in Chapter 7 below.

1.8 When is business rescue most appropriate?

In *Antonie Welman v Marcelle Props 193 CC*,[23] it was held that business rescue proceedings are not for terminally ill corporations, but are rather for ailing entities which, if given time, may be

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[22] See Levenstein 9-73. See also Henochsberg 526(68). The Companies Act 2008, s 144, sets out the rights of employees during a company's business rescue proceedings.

[23] 2012 JDR 0408 (GSJ) 12, at para 28. See also Levenstein 7-9.

rescued and become solvent. Accordingly, not all companies are suitable for business rescue, and much will depend on the specific cause of the company's financial distress.[24]

Most companies experiencing financial distress will consider business rescue for the benefit of the moratorium on claims. However, companies without a realistic hope of survival will inevitably end up in liquidation. There is therefore no merit in placing such companies into business rescue and, as such, a reasoned and factual basis for the belief that a company can be rescued is required.[25] In instances where there is no reasonable prospect of rescuing a company and where such company is clearly hopelessly insolvent, it would be manifestly wrong to place such company into business rescue. Instead, such company should rather be placed into liquidation. However, the converse is also true in that it would be equally inappropriate to liquidate a company in circumstances where such company may be successfully turned around if given the requisite breathing space and opportunity to restructure its affairs. Therefore, it goes without saying that when determining whether business rescue is most appropriate, one must assess each candidate for business rescue on the basis of the unique circumstances applicable to it.

1.9 Case study for the purposes of this course

In order to make the course as practical as possible, and in order to demonstrate the principles and procedures involved in the business rescue process, the case study set out below is provided to candidates on the course. As candidates progress through the various chapters of the course notes, self-assessment questions based on the case study will need to be completed. The self-assessment questions are designed to test candidates' knowledge of the work as they progress through the notes. In some instances, the facts of the case study may be supplemented or altered in order to address different scenarios that may arise in the context of the business recue process. In this way, candidates will be taken on a journey through the business rescue process from commencement to termination.

Candidates will be required to regularly refer back to the facts of this case study when addressing the self-assessment questions.

CASE STUDY

Fast Flights Airlines Limited

Fast Flights Airlines Limited (Fast Flights) is a public company duly incorporated and registered as such under the applicable company laws of South Africa. For the past 20 years, Fast Flights has operated a very successful low-cost airline, which made its mark by catering for the sector of the South African airline market that sought economical and efficient domestic air travel without unnecessary frills and expenses. Up until the year 2019, Fast Flights ran a profitable business, and was viewed as one of the "highfliers" of the African airline industry.

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24 See Levenstein 7-3.

25 *Kovacs Investments 571 (Pty) Ltd v Investec Bank Ltd and Another; Investec Bank Ltd v 14lso Holdings (Pty) Ltd* (25051/11, 18112/2011) [2012] ZAWCHC 110 (22 February 2012).

Towards the end of 2019, Fast Flights experienced a sharp decline in the demand for its airline tickets. This was primarily due to increasing economic constraints experienced by South African consumers, which were predicated by a stalling South African economy and the start of a global recession. New entrants into the South African airline industry also introduced a novel set of challenges for Fast Flights, in the form of increased competition for market share.

Fast Flights has a large staff complement, which includes pilots, cabin crew, engineers, maintenance and service support personnel, as well as financial and general support staff. A vast majority of Fast Flights' employees are represented by Fair-Labour-For-All, a South African registered trade union that seeks to advance the interests of employees engaged in the aviation industry.

Prior to the year 2019, Fast Flights aggressively expanded its operations by: (i) acquiring an airline catering company, (ii) increasing its workforce by almost 300 employees (increasing its wage bill by an additional R50 million per month) and (iii) acquiring five aircraft and entering into lease agreements for three additional airplanes to add to its fully owned fleet of 15 aircraft. Following the expansion, the airline operated 23 airplanes in total, had a somewhat successful catering subsidiary business and a large workforce.

Given that the acquisition of aircraft and the catering business required substantial financing and considering that all of the new aircraft were acquired offshore, Fast Flights required and obtained significant loan capital from Big Money Bank, which loans were all based in EURO denominated loan facilities. Big Money Bank was happy to provide such loan facilities to Fast Flights, on the basis that the existing fleet of 15 aircraft would be registered as security in favour of Big Money Bank, pursuant to the registration of aircraft security mortgage bonds.

Due to the downward valuation of the South African Rand to major foreign currencies, in conjunction with an increase in its cash outflows, pursuant to its obligations towards Big Money Bank and its newly hired employees, Fast Flights made substantial losses during the 2019 financial year.

Fast Flights has its head office in Johannesburg and runs the company through its board of directors consisting of a Chief Executive Officer (Mr B Sky), a Chief Financial Officer (Ms L Jet) and three other executive board members. Ms L Jet (an astute chartered accountant) became increasingly concerned about Fast Flights' financial condition and had doubts as to Fast Flights' ability to pay all of its debts as they became due and payable. She was further of the view that it would be reasonably likely that the company's ever-increasing liabilities would exceed its assets in the following financial year. Due to Fast Flights' increasing financial pressure in early 2020, Fast Flights procured the services of a firm of restructuring experts who, with the support of Big Money Bank, would attempt to informally restructure Fast Flights, both financially and operationally.

Under the guidance of the restructuring experts, Fast Flights proceeded to raise equity capital from its shareholders, on the speculative assumption that Fast Flights' expansion strategy would result in increased revenue from airline ticket sales, and significant dividends flowing to its shareholders once the bank loans were paid off. The equity capital raised from shareholders was only sufficient to pay arrear interest on the loans owed to Big Money Bank. Nevertheless, the intervention of the restructuring experts resulted in Fast Flights' becoming solvent and liquid (at least on its balance sheet).

On 26 March 2020, The President of South Africa announced a State of Disaster under the Disaster Management Act 57 of 2002, due to the onset of the global COVID-19 pandemic. The declaration of a National State of Disaster was accompanied by the issuing of various regulations that introduced a whole host of "lockdown" restrictions. As a result of the lockdown restrictions, Fast Flights was no longer allowed to operate domestic or international flights, and as a result, all potential revenue from flying operations came to an immediate halt.

The cessation of a large part of Fast Flights' business meant that the company experienced significant cash shortfalls. As a result, Fast Flights' board of directors came to the conclusion that it appeared reasonably unlikely that the company would be able to pay its debts (including salaries to its employees) at the end of April 2020. Fair-Labour-For-All, in conjunction with the employees of Fast Flights, saw the writing on the wall and engaged their legal advisors to assess the various options available to Fast Flights under South African law, in view of its financial difficulties. In their advice, the legal advisors, refer to business rescue proceedings as a viable option for Fast Flights, which proceedings could be commenced at the instance of Fair-Labour-For-All and the employees of Fast Flights as "affected persons" by way of a court application. Notwithstanding this advice, which set out the various requirements that needed to be satisfied in order to succeed with such an application, no further action was taken by Fair-Labour-For-All and the employees.

Although Fast Flights was no longer able to operate under the lockdown restrictions, the company was still obligated to pay for the maintenance, service, storage and insurance premiums in respect of their 23 aircraft. It was also required to service its various loan facilities with a variety of lenders, including the EURO denominated facilities made available by Big Money Bank. In addition, Fast Flights was also required to pay its employees' salaries. Finally, other critical creditors, such as the Civil Aviation Authority (CAA) and the various Airports had to be paid.

Given Fast Flights' inability to meet all of its obligations to its various creditors, certain creditors of Fast Flights decided to take further legal steps to reclaim amounts owing to them. Firstly, one of Fast Flights' trade creditors that supplied the company with aircraft lubricants and parts issued statutory letters of demand claiming payments that became due and payable by Fast Flights under the terms of the various supply agreements entered into between them.

Secondly, Fast Flights was served with a summons by the lessor of one of the aircraft hangers that was used by Fast Flights to store some of its aircraft. Thirdly, an aggressive, trade creditor that supplied on-board drinks to Fast Flight threatened to institute a liquidation application against Fast Flights. Lastly, one of the aircraft lessors threatened to cancel its lease and an instalment sale agreement with Fast Flights due to the non-payment of rentals and instalment payments that were due under the lease agreement and the instalment sale agreement, respectively.

Given the above, the board of directors of Fast Flights quickly concluded that the company could no longer continue trading in the ordinary course and that it had become financially distressed, as defined. As a result, the board of directors passed and filed a resolution with the Companies and Intellectual Property Commission (the CIPC) for the commencement of voluntary business rescue proceedings. The decision of the board of Fast Flights to commence business rescue was geared mainly at ensuring that Fast Flights benefits from the statutory moratorium on claims, but also to avoid sending out a section 129(7) notice to all of its creditors. Fast Flights was accordingly placed under business rescue proceedings on 11 May 2020 and one Mr V Bad was appointed as the business rescue practitioner of Fast Flights. A notice of his appointment was filed and published in the manner contemplated by the Companies Act 2008.

Ms L Jet was largely in favour of the commencement of the business rescue process, but was very concerned at the possibility that liquidation applications in respect of Fast Flights may have been filed with the High Court prior to the date on which the resolution commencing business rescue was passed. She however confirms that no liquidation applications were served on Fast Flights as at the date when the resolution commencing business rescue was adopted and filed with the CIPC and that Fast Flights was not aware of any such application.

It was later discovered that Mr V bad, unbeknown to the board, was found guilty in disciplinary proceedings brought against him by the professional body to which he belonged, with the result that his membership was revoked. On the basis that Mr V Bad was no longer a member in good standing of a legal, accounting or business management profession accredited by the CIPC, and as such, Mr V Bad was removed as the business rescue practitioner of Fast Flights and was replaced by Mr A Float on 15 June 2020, following certain court processes.

Immediately upon his appointment as replacement business rescue practitioner, Mr A Float scheduled a first meeting of creditors, and subsequent to that begun to investigate the affairs of Fast Flights. During the course of this investigation and following consultations with Big Money Bank, it became apparent to Mr A Float that the CEO of Fast Flights, Mr B Sky, has bound himself as surety for the debts of the company in an amount of R100 million, pursuant to a written suretyship. Mr B Sky is of the view that his obligations under the suretyship have been relinquished by virtue of the fact that Fast Flights has been placed into business rescue. It also comes to light that, that the CFO, Ms L Jet is married to the business rescue practitioner's brother. Lastly, it was discovered that Mr C Turbulence, one of Fast Flight's executive directors, has been involved in shady dealings with Royal Fuels (a jet fuel supplier) prior to the commencement of the business rescue proceedings.

It also becomes apparent during the course of this investigation that, Mr L Block, a senior director of Fast Flights, has been obstructive towards Mr A Float and has severely hampered and impeded the business rescue practitioner's execution of his statutory duties. Mr A Float engages a firm of attorneys to explore ways to have Mr L Block removed as a member of the board.

In addition to investigating the affairs of Fast Flights, immediately after his appointment Mr A Float undertook a process of examining all of Fast Flights' ongoing expenses, in an effort to reduce unnecessary overhead costs and operating expenditure, wherever possible. He quickly determined that Fast Flights' aggressive expansion in 2019, which resulted in the increase of its workforce by almost 300 employees, coupled with the mitigating socio-economic circumstances, was a primary contributing factor to their financial distress. However, due to Fast Flights' financial constraints, he was unable to offer any employees voluntary separation packages, but he was confident in his intention to include provisions regarding the reduction of the workforce in his proposed business rescue plan.

During the course of business rescue proceedings, it was also discovered that Fast Flights had entered into certain prejudicial contracts prior to the commencement of business rescue proceedings and that were hindering the effective rescue of the company. These contracts included various airline storage and baggage handling contracts. Mr A Float also identified certain expensive aircraft lease agreements that he wished to cancel, with the view of reducing the company's expenses. The payment obligations under the various contracts became due and payable during the course of the business rescue proceedings of Fast Flights. Mr A Float recalls learning that business rescue practitioners have the ability to suspend and / or cancel contracts pursuant to the provisions of the Companies Act 2008, but was not certain as to whether this was possible, as he had not done so before.

Mr A Float, in accordance with his statutory duties, consulted with the various lenders and shareholders of Fast Flights to establish whether there was a possibility of either of them providing post-commencement finance to the company. During these consultations, Big Money Bank expressed its concern about the status of the facilities made available by it prior to the commencement of business rescue proceedings, and whether such facilities would be treated differently than any new facilities provided during the business rescue proceedings. To alleviate Big Money Bank's concerns, Mr A Float requests his assistant Ms C Clerk, who has in-depth knowledge of the various provisions of the Companies Act 2008, to prepare a presentation outlining the legal position relating to post-commencement finance, for the benefit of Fast Flights' lenders and shareholders.

Mr A Float, in addition, requests Ms C Clerk to furnish him with a brief legal opinion setting out the pertinent provisions of the Companies Act 2008 relating to the remuneration of business rescue practitioners, as he wanted to know whether the amounts he had been earning to date were in accordance with the Companies Act.

At this stage, certain creditors of Fast Flights became frustrated by Fast Flights' failure to make payment of certain amounts owed to them, and subsequently elected to take legal steps to reclaim amounts owing to them. Fast Flights was, accordingly, served with two summons and a money judgment applications in the Gauteng High Court. Another creditor proceeded to issue a liquidation application against Fast Flights. All the while, certain other creditors cancelled the agreements entered into with Fast Flights, due to the non-payment of amounts due thereunder. Mr A Float and the board of directors are bewildered by the pursuant legal onslaught and are worried about how these legal proceedings will affect the business rescue proceedings of Fast Flights.

Notwithstanding the aforementioned legal challenges, Mr A Float began preparing and drafting the business rescue plan of Fast Flights for consideration by creditors at a section 151 meeting of creditors. In accordance with his determination that Fast Flights needed to drastically reduce its workforce, the business rescue plan contemplated the retrenchment of a large portion of Fast Flights' employees. The retrenchment proposal immediately resulted in tension between Fair-Labour-For-All and the business rescue practitioner. This tension was exacerbated by the fact that the employees of Fast Flights had not been paid their salaries for the duration of the business rescue process. The business rescue plan furthermore did not specify the status of the employees' unpaid salaries, which was of grave concern to them.

Included in the business rescue plan is, *inter alia*, the following information: (i) creditors include R4 billion secured creditors (lenders), R4 billion unsecured creditors and a further R2 billion inter-company claim from its catering subsidiary, which has been subordinated in favour of the secured lenders, and (ii) a footnote in the forecast notes that the business rescue practitioner is earning remuneration in excess of the tariff rates.

Nevertheless, the business rescue plan was published by Mr A Float on 1 August 2020 and was put to the vote at the meeting of creditors. The business rescue plan was approved by the requisite majority of creditors. However, Jumbo Jet Proprietary Limited, a minority creditor, voted against the plan on the basis that he genuinely believed that the plan would impose financial risks on himself as well as other creditors, and as a result was of the view that it was not bound by the terms of the approved business rescue plan at all. Subsequently, another minority creditor, Engines Proprietary Limited, made an offer to purchase the voting interests of Jumbo Jet Proprietary Limited.

Mr A Float proceeded to implement the business rescue plan. The business rescue proceedings of Fast Flights continued over a protracted period of time, but despite this, Mr A Float was of the view that it would be completely unnecessary to report on the progress of the business rescue proceedings, given that to do so would be very onerous.

After the business rescue proceedings of Fast Flights had gone on for 18 months, it became apparent that Fast Flights was un-rescuable, despite the best efforts of Mr A Float and the board of directors. Consequently, the Mr A Float begun exploring the different avenues, in terms of which the business rescue proceedings of Fast Flights could be terminated. He engages a firm of attorneys to explore ways in which to exit the business rescue process and to place Fast Flights into liquidation. The firm of attorneys furnish him with legal advice.

Some financial statements (balance sheet and income statement) for Fast Flights Airlines Ltd have been provided on the next two pages.

Balance Sheet

Statement of Financial Position as at 31 December 2019
Fast Flights Airlines Ltd

	2019 R'000s	2018 R'000s
ASSETS		
Non-current assets		
Property, plant and equipment	9,049,000	7,850,000
Intangible assets	30,000	30,000
Investment in subsidiary	100,000	180,000
	9,179,000	**8,060,000**
Current assets		
Inventories	22,000	20,500
Trade and other receivables	850,000	750,000
Cash and cash equivalents	540,000	475,000
	1,412,000	**1,245,500**
Total assets	**10,591,000**	**9,305,500**
EQUITY AND LIABILITIES		
Equity		
Share Capital	5,000	5,000
Accumulated profits	571,500	790,500
Total equity	**576,500**	**795,500**
Liabilities		
Non-current liabilities		
Interest-bearing liabilities	2,740,000	2,280,000
Inter-company loan	1,867,000	1,750,000
	4,607,000	**4,030,000**
Current liabilities		
Trade and other payables	3,782,000	3,285,000
Unutilised ticket liability	380,000	310,000
Provisions	98,000	135,000
Interest-bearing liabilities	1,147,500	750,000
	5,407,500	**4,480,000**
Total equity and liabilities	**10,591,000**	**9,305,500**

Income Statement

Statement of profit or loss for the year ended 31 December 2019
Fast Flights Airlines Ltd

	2019 R'000s	2018 R'000s
Revenue	12,125,000	10,500,000
Operating expenses	- 10,900,000	- 8,400,000
	1,225,000	**2,100,000**
Depreciation and amortisation	- 1,070,000	- 840,000
Property rental income	6,000	-
Profit / (loss) from operations	- **161,000**	**1,260,000**
Interest expense	- 380,000	- 250,000
Profit / (loss) before tax	- **219,000**	**1,010,000**
Taxation	-	- 200,000
Profit / (loss) for the year	- **219,000**	**810,000**

The self-assessment questions for Chapter 1 follow on the next page.

Self-Assessment Questions for Chapter 1

Question 1

Which of the following statements is / are **correct** in relation to business rescue proceedings in terms of the Companies Act 2008?

(a) The restructuring of companies in financial distress is on the increase globally.

(b) The worldwide trend is not to attempt to rehabilitate financially distressed companies, instead the globally accepted trend is to simply liquidate them regardless of their viability and prospects of being rescued.

(c) Business rescue encapsulates a shift from creditors' interests to a broader range of interests, that is, a shift from a creditor-focused culture of liquidation to a rescue-oriented approach where there is an emphasis on the balancing of the rights and interests of all relevant stakeholders.

(d) Both (a) and (c).

Question 2

Which of the following statements is **incorrect** in relation to business rescue proceedings in terms of the Companies Act 2008?

(a) Business rescue is virtually identical to the old judicial management procedure.

(b) Business rescue proceedings are creditor-focused and do not consider the interests of other stakeholders such as employees and trade unions.

(c) The supervision of business rescue proceedings falls within the jurisdiction of the Magistrate's Court and not the High Court.

(d) All of the above.

Question 3

Select the **correct** statement:

What are the objectives of the business rescue process as set out in Chapter 6 of the Companies Act 2008?

(a) The development and implementation of a business rescue plan to rescue the financially distressed company, which plan has the aim of allowing the company to continue in existence on a solvent basis.

(b) To provide a better return for the financially distressed company's creditors or shareholders than would result from the immediate liquidation of the company, by way of "quasi-liquidation" or "controlled wind-down".

(c) Both (a) and (b).

(d) None of the above.

Question 4

Briefly describe the two entry routes into business rescue and the requirements for each.

Question 5

Briefly discuss the moratorium as provided for under section 133 of the Companies Act 2008.

Question 6

Briefly describe post-commencement finance.

For feedback on this self-assessment exercise, see the document "Comment and Feedback on Self-Assessment Questions", which is made available to you as a separate document.

CHAPTER 2

COMMENCEMENT AND TERMINATION OF BUSINESS RESCUE

2.1 Introduction

There are two entry routes into the business rescue process. The first route is a board resolution (voluntary commencement) that must be filed with the Companies and Intellectual Property Commission (the CIPC), and the second is a formal court application by an affected person (compulsory commencement). Once business rescue proceedings have commenced, whether by a board resolution or court application, the commencement process leads to the appointment of a business rescue practitioner who must supervise the company during business rescue proceedings.[26]

The vast majority (about 91%) of business rescue proceedings are commenced by the filing of a board resolution because it is a much simpler, faster, and cheaper process.

2.2 Voluntary commencement of business rescue by the board of directors

In terms of section 129(1) of the Companies Act 2008, a company's board of directors may pass a resolution in terms of which the company resolves to commence the business rescue process and pursuant to which a business rescue practitioner (who satisfies the requirements of the Companies Act 2008) must be appointed by the board. This resolution has no force or effect until it has been filed with the CIPC.[27]

2.2.1 Restriction on voluntary commencement

It is important to note that a resolution to commence business rescue cannot be adopted if liquidation proceedings have already been "initiated by or against the company".[28] The purpose behind this restriction is to prevent boards of companies from thwarting *bona fide* liquidation applications by adopting resolutions to commence business rescue in bad faith. Note that although in terms of section 129(2)(b) a resolution to commence business rescue is of no force and effect until it has been filed with the CIPC, it is the mere adoption of a business rescue resolution that is prohibited, and not the filing. Could this perhaps mean that a resolution that was adopted before liquidation proceedings were initiated can be validly filed?

There is no definition or other indication in the Companies Act 2008 of what the word "initiated" means. As a result, the courts have expressed conflicting opinions on its interpretation. In *FirstRand Bank Ltd v Imperial Crown Trading 143 (Pty) Ltd*[29] the court held that it must be

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[26] Companies Act 2008, s 128(1)*(d)*.
[27] *Idem*, s 129(2)*(b)*.
[28] *Idem*, s 129(2)(a). An application to court by an interested person in terms of s 131 is then the only option still available.
[29] 2012 (4) SA 266 (KZD).

assumed to mean the same as "commence" because any other meaning would cause unnecessary uncertainty.[30]

A few years later, in *Tjeka Training Matters (Pty) Ltd v KPPM Construction (Pty) Ltd and Others*,[31] the court considered this question in circumstances where a resolution to commence business rescue was adopted by a company whilst a liquidation application had already been issued and filed in court by the company's creditor, but which had not yet been served on the company. The court analysed the wording used in the Companies Act 2008 and was of the view that "initiated" must be understood to be "by or against the company". Accordingly, liquidation proceedings that are initiated must be cognisable by reference to its "effect" upon the company. Therefore, the issuing of an application, without the company being aware of its existence (that is, without service of the application) cannot be said to be proceedings "initiated" against the company. Accordingly, the court held that the liquidation application must be served on the company, and not merely issued and filed at court to be regarded as having been initiated.

The court in *Mouton v Park 2000 Development 11 (Pty) Ltd and Others*[32] disagreed and held that the ordinary, grammatical meaning of the verb to "initiate" is to cause a process or action to begin and refers to a preceding act or conduct which sets a process in motion. Accordingly, the court held that the word "initiated" in section 129(2)(a) is intended to refer to a preceding act or conduct by which liquidation proceedings are set in motion and what that act or conduct may be will depend on the facts of each matter. The court held that in most instances, it will be the adoption of the necessary resolution by the creditor to launch such liquidation proceedings.

In *Pan African Shopfitters (Pty) Limited v Edcon Limited and Others*,[33] the meaning of the word "initiated" was again considered by the court. The court had regard to both the *Tjeka Training Matters* and *Mouton* decisions and found that the conclusion in the *Tjeka Training Matters* was correct, that is, that liquidation proceedings contemplated in section 129(2)(c) of the Companies Act 2008 are initiated once a liquidation application is issued and served on the company. The court held that this conclusion is in line with the inherent policy choice that a litigant remains unaffected in law until made formally aware of the steps being taken against such litigant. Although there has not as yet been a judgment by the Supreme Court of Appeal on the correct meaning of "initiated" in this context, it seems quite likely that when the question comes before the Supreme Court of Appeal, the court will agree with this interpretation based on the view it adopted in the judgment of *Lutchman NO v African Global Holdings (Pty) Ltd*[34] albeit in a different context and dealing with a different section.

2.2.2 Requirements for voluntary commencement

In order for a company to commence business rescue proceedings on a voluntary basis, the board must have reasonable grounds to believe that the company is financially distressed and

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[30] The time of commencement of an insolvent liquidation is clearly defined in the Companies Act 1973.
[31] 2019 (6) SA 185 (GJ). See also Levenstein 8-8 – 8-9; and Henochsberg 466, 468(2)-(3).
[32] 2019 (6) SA 105 (WCC). See also Levenstein 8-9 – 8-13; and Henochsberg 468(3).
[33] (10652/2020) [2020] ZAGPJHC 158 (10 July 2020). See also Levenstein 8-13; and Henochsberg 468(3).
[34] 2022 (4) SA 529 (SCA). This case is discussed in part 2.3.1 below dealing with s 131(6).

that there appears to be a reasonable prospect of rescuing the company. Chapter 6 does not provide any definitive guidance on what is meant by "a reasonable prospect of rescuing the company". It is submitted that the directors of the company will have to consider the company's specific circumstances at the time of their deliberation. There is accordingly a subjective element (relating to the personal view of the directors) and an objective element (relating to the view of the reasonable director) as to whether a company's board has reasonable grounds to believe that the company is financially distressed and that there appears to be a reasonable prospect of rescuing the company.[35]

2.2.3 Obligation to commence

In terms of section 129(7), if the board decides not to adopt a resolution commencing business rescue, despite having reasonable grounds to believe that the company is financially distressed (that is, impending commercial or balance sheet insolvency), the board must deliver a written notice to each affected person setting out the type of financial distress that the company is in, and providing reasons why the board decided not to adopt a business rescue resolution. This is clearly an attempt to put pressure on company boards to enter into business rescue as soon as they become aware of the company's financial problems.

However, when this notice is sent out, the company will be informing all its creditors that it is financially distressed, with the effect that creditors who continue to deal with it do so at their own risk. Potentially, a creditor receiving such a notice may apply to court for an urgent winding-up order in terms of the provisions of section 345(1)(c) of the Companies Act 1973.[36] Sending out such a notice could have other serious consequences if it comes to the attention of the CIPC. In terms of section 22(2), the CIPC may issue a notice to a company which it has reasonable grounds to believe is unable to pay its debts as they become due and payable in the normal course of business, demanding that the company must show cause why it should be permitted to continue trading. If the company fails to satisfy the CIPC within 20 business days after the notice was issued that it is able to pay its debts as they become due and payable, the CIPC may issue a compliance notice requiring the company to cease trading or carrying on its business.

Not surprisingly, very few companies deliver such a notice and, since there is no direct sanction in section 129(7) itself against companies who fail to do so, most companies choose to ignore this provision due to the damage it will cause to the reputation and creditworthiness of the company and its ability to keep trading.

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35 See Levenstein 8-3; and Henochsberg 467.

36 See Levenstein 8-17 – 8-20; and Henochsberg 468(9)-(10).

2.2.4 Procedure

2.2.4.1 Resolution by board of directors

In terms of regulation 123(1) of the Companies Regulations 2011, a Notice of Commencement of Business Rescue Proceedings (Form CoR 123.1) must be filed together with a copy of the board resolution to commence business rescue.[37]

It is important to note that the resolution for the commencement of business rescue must be a valid resolution that complies with all the requirements set by section 73 of the Companies Act 2008 for a board resolution. Among other things, it must be passed with the support of a majority of the directors (simple majority), subject to any higher percentage requirement imposed on the board for the passing of such a resolution, which may be imposed by a company's memorandum of incorporation.[38]

In *DH Brothers Industries (Pty) Ltd v Gribnitz NO and Others,*[39] the court held that where only one of the two directors passed the resolution (whereas the Companies Act 2008 requires a majority of directors to have done so) this brought the matter within the ambit of a failure to satisfy the procedural requirements of section 129 of the Companies Act 2008 and therefore the resolution to commence business rescue lapsed and became a nullity.

However, the Supreme Court of Appeal in *Panamo Properties (Pty) Ltd v Nel and Another NNO*[40] held that this decision was incorrect. The consequence of the board not having been properly constituted would be that the resolution was not a resolution of the board of directors. As such it was a nullity and ineffective for the purpose of commencing business rescue proceedings. Equally, in the absence of such a resolution, there was nothing to set aside in terms of section 130(1)(a)(iii) of the Companies Act 2008 (discussed further below).

2.2.4.2 Appointment of business rescue practitioner

In terms of section 129(3), within five business days after a company has adopted and filed a resolution to commence business rescue proceedings, or such longer time as the CIPC, on application by the company, may allow, the company must appoint a business rescue practitioner who satisfies the requirements of section 138 and who has consented in writing to accept the appointment.[41] Within two business days after the appointment of the business

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[37] Practice Note 3 of 2021 issued by the CIPC on 28 July 2021 requires that all business rescue filings, including the Notice of Commencement, must be submitted electronically on www.cipc.co.za/on-line transacting/new e-services. This Practice Note also contains a list of documents that must accompany the Form CoR 123.1.

[38] See Levenstein 8-1 – 8-2; and Henochsberg 463.

[39] 2014 (1) SA 103 (KZP), at para 16.

[40] 2015 (5) SA 63 (SCA). See also Levenstein 8-27 – 8-28; and Henochsberg 463.

[41] The requirements for appointment as a business rescue practitioner are discussed in Ch 8.

rescue practitioner, the company must file a notice of the appointment with the CIPC on Form CoR 123.2.[42]

2.2.4.3 Notification of affected persons

Within five business days after filing a board resolution to commence business rescue (or such longer time as CIPC on application by the company may allow), the company must publish a notice of the resolution and its effective date in the prescribed manner to every affected person, including with the notice a sworn statement of the facts relevant to the grounds on which the board resolution was founded.[43]

In *Ex parte Van den Steen NO (Credit Suisse Group AG Intervening)*[44] it was held that substantial compliance with notification requirements is allowed in terms of section 6(9) of the Companies Act 2008. Although a small group of creditors had mistakenly not been notified, the court issued a declaratory order that the company had substantially complied with the notification requirements. In *Griessel and Another v Lizemore and Others*,[45] the applicants produced proof that they had given notice of the application to all affected persons including the union and shareholders, save that in the case of creditors, the applicants could only give notice to those whose names they were able to procure. Notice was given to a substantial number, including the main creditors. The court was satisfied that there had been compliance with the requirements of notice to the unions, employees, and shareholders and that there had been substantial compliance, in all the circumstances, with notice to creditors by number and certainly by value and importance.[46]

Within five business days after filing the notice of appointment of a business rescue practitioner, the company must publish a copy of the notice of appointment to each affected person.[47]

The purpose of section 129(3) and (4) is to protect the rights of affected persons by ensuring that they are informed of the business rescue resolution and thereby enabling them to exercise their rights, including the right to have the business rescue resolution or the appointment of the business rescue practitioner set aside. It must be noted that the CIPC can extend the period within which the company must appoint a business rescue practitioner and publish a notice of the resolution to commence business rescue proceedings in terms of section 129(3), but not in

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[42] Practice Note 22 of 2022 issued by the CIPC on 31 August 2022, requires electronic filing of this notice and also lists the documents that must accompany the Form, including a Letter of Good Standing from the practitioner's accredited professional body.

[43] Companies Act 2008, s 129(3)(a). Regulation 123(2) prescribes the manner in which this Notice must be published, *inter alia* by conspicuously displaying it at the registered office of the company and any workplace where employees of the company are employed, as well as on any website maintained by the company.

[44] 2014 (6) SA 29 (GJ).

[45] 2016 (6) SA 236 (GJ).

[46] *Ibid*, paras 96 and 98. See also Henochsberg 474.

[47] Companies Act 2008, s 129(4)(b). In terms of reg 123(4), the company must either deliver a notice in Form CoR 123.3 to each affected person as prescribed by reg 7, or inform each affected person of the availability of a copy of the Form in accordance with s 6(11)(b)(ii) and reg 6.

relation to either the filing of a notice of the practitioner's appointment in terms of section 129(4) or publishing a copy of the notice of appointment of the practitioner to each affected person.[48]

2.2.4.4 Failure to comply with procedural requirements

Section 129(5) provides that if a company fails to comply with any provision of section 129(3) or (4) -

(a) its resolution to begin business rescue proceedings and place the company under supervision lapses and is a nullity; and

(b) the company may not file a further resolution (to commence business rescue) for a period of three months after the date on which the lapsed resolution was adopted, unless a court, on good cause shown on an *ex parte* application, approves the company filing a further resolution.

A number of decisions of the various divisions of the High Court held that the effect of non-compliance with the provisions of subsections (3) and (4) of section 129 was that the resolution commencing business rescue lapsed and became a nullity, thereby bringing the business rescue proceedings to an end.

In *Panamo Properties (Pty) Ltd v Nel and Others NNO*[49] the Supreme Court of Appeal disagreed and held that when a court grants an order in terms of section 130(5)(a), the effect of that order is not merely to set the resolution to commence business rescue aside, but to terminate the business rescue proceedings. It follows that until that has occurred, even if the business rescue resolution has lapsed and become a nullity in terms of section 129(5)(a), the business rescue proceedings that commenced pursuant to such resolution have not terminated. Business rescue will only be terminated when the court sets the resolution aside.[50] This will only be done if the court considers it just and equitable to do so.[51] As long as the resolution to commence business rescue has not been set aside, the standing of the business rescue practitioner appointed on the strength of that resolution cannot be challenged on the ground of non-compliance with the procedural requirements set out in section 129. This applies also where the person who challenges the standing of the business rescue practitioner is an "innocent party" and not an "affected person" as defined in section 128.[52] Therefore, in summary, any party seeking an order setting aside the resolution that commenced business rescue proceedings must bring an

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48 *Griessel and Another v Lizemore and Others* 2016 (6) SA 236 (GJ), at paras 106 - 109.

49 2015 (5) SA 63 (SCA), at para 28. In *Swanepoel and Another v Master Trucking (Pty) Ltd (In Provisional Liquidation)* (M196/2016) [2016] NWM (12 May 2016) the court, without reference to the *Panamo* or other decisions, declined to grant a declaratory order that a resolution to commence business rescue proceedings was a nullity due to non-compliance with s 129(3) and (4), amongst other reasons because the provisions "are clearly defined". See also *Levenstein* 8-27; and *Henochsberg* 468(9), 473 – 474.

50 Applied in *Alderbaran (Pty) Ltd and Another v Bouwer and Others* [2018] JOL 39938 (WCC); [2018] 3 All SA 71 (WCC), at paras 29 and 34.

51 See the discussion of this judgment in para 2.2.5.1 below.

52 *Newton Global Trading (Pty) Limited (Under Business Rescue) v Da Corte* [2015] JOL 34899 (SCA) (20785/2014) [2016], at para 9.

application to court in terms of section 130 (discussed further below). Non-compliance with section 129(3) and (4) will not result in the termination of business rescue proceedings: the court will in its discretion determine whether business rescue proceedings must be terminated.[53]

As in the case of section 344(h) of the Companies Act 1973, the conclusion that termination of the business rescue would be just and equitable in terms of section 130(5)(a)(ii) of the Companies Act 2008 involves the exercise, not of a discretion, but of a judgment on the relevant facts. Once that conclusion has been reached, the making of an order to set aside the resolution and terminate the business rescue does involve the exercise of a discretion.[54] Because business rescue (once validly initiated) remains operative until set aside by a court – even if the requirements of section 129(3) and (4) have not been complied with – there should not be a blanket rule that the setting aside of a section 129 resolution and termination of business rescue operates retrospectively with effect from the date of the section 129 resolution.[55] The rationale for the wide discretion conferred on the court in section 130(5)(c) to grant "any further necessary and appropriate order" is to equip the court to deal equitably with the various circumstances that may arise and require regulation following the setting aside of a section 129 resolution and the termination of business rescue. The discretion must be exercised judicially and the only limit on the further order that may be made is that it must be both necessary and appropriate.[56]

In *The Commissioner for the South African Revenue Service v The Business Zone 983 CC*,[57] where an entity failed to display a copy of the notices contemplated in section 129(3)(a) at the principal places where the entity conducted its businesses, it was held that the resolution to commence business rescue was a nullity in terms of the provisions of section 129(5)(a) and it was just and equitable to set aside the business rescue resolution because it was clearly an abuse of the business rescue process and did not entail a genuine attempt to achieve the efficient rescue and recovery of a financially distressed company in a manner that balanced the rights and interests of all relevant stakeholders.

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[53] The court did not consider the clear distinction made in s 129(6) between a resolution that has lapsed in terms of subs (5) and business rescue proceedings that have terminated in accordance with s 132(2), including as a result of the business rescue resolution being set aside.

[54] *Alderbaran (Pty) Ltd and Another v Bouwer and Others* [2018] JOL 39938 (WCC); [2018] 3 All SA 71 (WCC), at para 47, with reference to *Henochsberg*, commentary on s 344(h) of the Companies Act 1973.

[55] *Alderbaran (Pty) Ltd and Another v Bouwer and Others* [2018] JOL 39938 (WCC**)**; [2018] 3 All SA 71 (WCC), at paras 51 and 52.

[56] At para 54. The court did not accept the submission that the sale in execution was a nullity that had to be set aside. It was both necessary and appropriate, in all the circumstances of the case, to make an order confirming the validity of the sale in execution of the property and to authorise the finalisation of transfer of the property in terms thereof (paras 56 and 57).

[57] (9673/2015) [2015] WCC (7 September 2015); [2017] JOL 37888 (WCC), at para 32. See also Levenstein 8-30(1); and Henochsberg 474.

2.2.5 Remedies available to affected persons

2.2.5.1 Setting aside the business rescue resolution

The commencement of business rescue proceedings must not be an abuse of process and should be brought in good faith and for a proper purpose, that is, for the "rescue" of the company and not for an ulterior motive.[58]

However, in view of the fact that the initiation of voluntary business rescue proceedings is open to potential abuse, affected persons[59] are afforded protection in appropriate circumstances. In terms of section 130(1)(a), at any time after the adoption of a resolution commencing business rescue and until the adoption of a business rescue plan, an affected person may (after notice to other affected persons) apply to court for an order setting aside the resolution, on the grounds that –

(i) there is no reasonable basis for believing that the company is financially distressed;

(ii) there is no reasonable prospect for rescuing the company;[60] or

(iii) the company has failed to satisfy the procedural requirements set out in section 129;

In terms of section 130(4), affected persons have an automatic right to participate in the section 130 proceedings without the need for an order authorising them to do so. It is noteworthy that section 130(1)(a) only provides an affected person (seeking to approach a court to set aside a resolution) three grounds, or causes of action, on which to base the application. In contrast to this, section 130(5)(a)(ii) empowers a court hearing an application brought under section 130(1)(a) to set aside a resolution on those three grounds but also, in addition, to do so "if having regard to all of the evidence, the court considers that it is otherwise just and equitable to do so".

In *DH Brothers Industries (Pty) Ltd v Gribnitz NO*[61] the court suggested that the effect of the inclusion of subparagraph (ii) in section 130(5)(a) is to introduce a fourth ground for setting aside a resolution to commence business rescue in addition to the three set out in section 130(1)(a). However, the Supreme Court of Appeal held in *Panamo Properties (Pty) Ltd v Nel and Another NNO*[62] that this is incorrect. The wording of section 130(5)(a)(i) appears to be yet another case in a long line in which the legislation uses the disjunctive word "or", where the provisions are to be read conjunctively and the word "and" would have been more appropriate. Where to give

[58] *Griessel and Another v Lizemore and Others* 2016 (6) SA 236 (GJ), at para 82; and *Loots v Nongoma Medical Centre CC and Another* (5639/2016) [2016] ZAWCHC 76 (24 June 2016), at para 28.

[59] As defined in the Companies Act 2008, s 128(1)(a).

[60] The meaning of "reasonable prospect" is similar to the meaning in s 131 – *The Commissioner for the South African Revenue Service v The Business Zone 983 CC* (9673/2015) [2015] WCC (7 September 2015) [2017] JOL 37888 (WCC), at para 36. *Cf Absa Bank Ltd v Golden Dividend 339 (Pty) Ltd and Others* 2015 (5) SA 272 (GP), at paras 58 to 64.

[61] 2014 (1) SA 103 (KZP), at paras 17 and 18. See also Levenstein 8-27; and Henochsberg 478.

[62] 2015 (5) SA 63 (SCA), at para 31. See also Levenstein 8-27 – 8-28; and Henochsberg 479.

the word "or" a disjunctive meaning would lead to inconsistency between the two subsections, it is appropriate to read it conjunctively as if it were "and". This has the effect of reconciling section 130(1)(a) and section 130(5)(a) and limiting the grounds upon which an application to set aside a resolution can be brought, whilst conferring on the court in all instances a discretion, to be exercised on the grounds of justice and equity in the light of all the evidence, as to whether the resolution should be set aside.

The discretion under section 130(5)*(a)*(ii) is a so-called "discretion in the loose sense", thus a value judgment and appealable without any misdirection first required, as is the case with a "discretion in the strict sense".[63] An application in terms of section 130 is made to court and the applicant must not only establish the statutory grounds, but also satisfy the court that it is just and equitable that the resolution be set aside. If the court grants such an order, that brings the business rescue to an end. A further point in favour of this approach is that it largely precludes litigants, whether shareholders and directors of the company or creditors, from exploiting technical issues in order to subvert the business rescue process or turn it to their own advantage. Once it is recognised that the resolution may be set aside and the business rescue terminated if that is just and equitable,[64] the scope for raising technical grounds to avoid business rescue will be markedly restricted, even if it does not vanish altogether.[65]

In terms of section 130(5), the court may, when considering an application to set aside the resolution commencing business rescue, either:

(i) set aside the resolution on any of the grounds set out in section 130(1) if the court considers that it is otherwise just and equitable to do so; or

(ii) afford the practitioner sufficient time to form an opinion whether or not the company appears to be financially distressed, or whether or not there is a reasonable prospect of rescuing the company.

The court, when making an order setting aside the resolution, may also make any further necessary and appropriate order, including an order placing the company in liquidation.

Section 130(5)(c)(ii) further provides that when the court considers the setting aside of the resolution to commence business rescue, and if the court has found that there are no reasonable grounds for believing that the company would be unlikely to pay all of its debts as they became due and payable, the court may order costs against a director unless satisfied that the director acted in good faith and on the basis of information he was entitled to rely upon in terms of section 76(4) and (5).[66] Accordingly, directors need to be aware that the legislature goes so far

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[63] *BP Southern Africa (Pty) Ltd v Intertrans Oil SA (Pty) Ltd and Others* 2017 (4) SA 592 (GJ), at para 71, applied the decision by Brand JA in *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* 2013 (4) SA 539 (SCA), at para 29ff, regarding the discretion under s 134(4) to the powers under s 130(5)*(a)*(ii).

[64] See *Griessel and Another v Lizemore and Others* 2016 (6) SA 236 (GJ), at paras 122, 123 and 130, where the resolution was set aside on the ground that it was just and equitable to do so.

[65] *Idem*, at paras 33 and 34.

[66] *Cf Griessel and Another v Lizemore and Others* 2016 (6) SA 236 (GJ), at paras 138 and 139.

as to punish directors who supported a business rescue resolution when there was clearly no merit in doing so.

In terms of section 130(2) an affected person who, as a director of a company, voted in favour of a resolution contemplated in section 129, may not apply to a court in terms of section 130(1)(a) to set aside that resolution unless such person satisfies the court that the person, in supporting the resolution, acted in good faith on the basis of information that has subsequently been found to be false or misleading.[67]

After the adoption of the business rescue plan, an affected person is not entitled to apply to court for an order setting aside the board resolution commencing business rescue proceedings or an order setting aside the appointment of the practitioner. Whatever flaws may have been present before that time become of purely historical importance thereafter.[68]

It is a heavy burden for a creditor to apply to court with notice to all the affected persons. It may also be very difficult for creditors to show that the company is not financially distressed without access to the financial statements of the company. However, creditors will most likely be able to attack the board resolution if it appears that there is no reasonable prospect of rescuing the company.

When a court makes an order setting aside a resolution in terms of section 129(1) (commencing a business rescue procedure) and places the company under liquidation and that order is under appeal, the business rescue process ends immediately upon the issue of the order and not only when the appeal process is finally exhausted and the appeal or appeals adjudicated.[69]

2.2.5.2 *Setting aside the appointment of the business rescue practitioner*

In terms of section 130(1)(b) of the Companies Act 2008, an affected person may apply to court for the setting aside of the appointment of the practitioner[70] on one of the following grounds:

(i) The practitioner does not satisfy the requirements of section 138.[71]

(ii) The practitioner is not independent of the company or its management. This appears to partly be a duplication of the first ground because independence from the company is already stipulated as a requirement in section 138. However, section 138 does not require independence from management. Regrettably, it also does not require independence from

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[67] It is an open question as to whether s 130(2) permits directors to do so by making a trust the applicant rather than themselves – *Panamo Properties (Pty) Ltd v Nel and Another NNO* 2015 (5) SA 63 (SCA), at para 15.

[68] *African Banking Corporation of Botswana Ltd v Kariba Furniture Manufacturers (Pty) Ltd and Others* 2013 (6) SA 471 (GNP), at para 62; and *Panamo Properties (Pty) Ltd v Nel and Another NNO* 2015 (5) SA 63 (SCA), at para 13.

[69] *Ex parte Nell and Others NNO* 2014 (6) SA 545 (GP), at para 56.

[70] *Van Niekerk v Seriso 321 CC* (Case Number: 2011135199, High Court Johannesburg, 20 March 2012 at 35) noted that a creditor would be entitled to raise any concerns regarding the interim practitioner at the first meeting, there being nothing to suggest that the practitioner nominated did not meet the requirements of s 138.

[71] Discussed in Ch 8 below.

creditors, nor is it included as one of the grounds for removal. In *Caratco (Pty) Ltd v Independent Advisory (Pty) Ltd*[72] the court thus found there was nothing preventing a creditor of the company that was in business rescue from entering into an agreement with the business rescue practitioners to pay them a contingency fee for implementing a business rescue plan.

(iii) The practitioner lacks the necessary skills, having regard to the company's circumstances. Although this is not listed as a requirement for appointment in section 138, it constitutes grounds for removal from office of a practitioner.

In terms of section 130(6), if the court makes an order setting aside the appointment of a practitioner, the court must appoint another practitioner who meets the requirements of section 138 and who is recommended by, or acceptable to, the holders of a majority of the independent creditors' voting interests who were represented in the hearing before the court. The court may also, if deemed necessary, require a report from the newly-appointed practitioner indicating whether the company appears to be financially distressed or whether there is a reasonable prospect of rescuing the company. Depending on the contents of this report, the court may subsequently set aside the resolution to commence business rescue because it has concluded that the company is not financially distressed or there is no reasonable prospect of a rescue. An application to remove a practitioner may thus also result in termination of the business rescue procedure by the setting aside of the resolution.

2.2.5.3 Demanding security from business rescue practitioner

An affected person may also apply to court for an order compelling the practitioner to provide security in an amount and on terms and conditions that the court considers necessary to secure the interests of the company and any affected persons.[73] Unfortunately, the Companies Act 2008 does not require that a business rescue practitioner must provide security for the proper performance of his duties before being appointed, although a company and the affected persons could suffer extensive damages as a result of the actions of a dishonest, negligent or incompetent practitioner. In contrast, liquidators, trustees of insolvent estates and executors of deceased estates must all provide security before being appointed.

2.3 Commencement by application to court (compulsory commencement)

Section 131 provides that unless a company has adopted a resolution to begin business rescue proceedings, an affected person may apply to a court at any time for an order placing a company under supervision and commencing business rescue proceedings. It is important to note that a company and its directors (in their capacities as such) are not authorised to apply for a business rescue order under section 131.

[72] 2020 (5) SA 35 (SCA).
[73] Companies Act 2008, s 130(1)(c).

Section 131(2) states that the applicant must serve a copy of the application on the company and the CIPC and notify each affected person in the prescribed manner.[74] In terms of section 131(3), each affected person has the right to participate in the hearing of this application.

Unfortunately, the legislature has deemed it fit to prescribe motion proceedings in matters where an order is sought for the commencement of business rescue proceedings. Despite that being the case, litigants and their legal representatives must count the costs of bringing matters to court on motion where disputes are to be expected. The motion proceedings required for an application for business rescue are not geared toward the decision of factual disputes. The matter can only be decided on the respondent's version of the disputed facts. It must be noted that business rescue proceedings for more than one company cannot be sought in a single application unless there is a complete identity of interests.

2.3.1 *Effect of a business rescue application on liquidation proceedings*

Section 131(6) provides that if liquidation proceedings have already been commenced by or against the company at the time an application is made to begin business rescue proceedings in terms of section 131(1), the application will suspend those liquidation proceedings until the court has adjudicated upon the application,[75] or the business rescue proceedings end, if the court makes the order applied for.[76]

Since the Companies Act 2008 does not make it clear whether the words "liquidation proceedings" refer only to the court proceedings until a final liquidation order has been issued, or to the actual process of winding-up a company overseen by the liquidators and the Master after a winding-up order had been issued, or whether they cover the entire process until the liquidation has been completed, there were several conflicting judgments about this issue.[77] Eventually it was held by the Supreme Court of Appeal in *Richter v Absa Bank Limited*[78] that an application in terms of section 131 of the Companies Act 2008 to place a company under business rescue can be made "at any time", even after the final liquidation order has been issued. The court went on to say that the correct position is that upon the final order of liquidation being granted, the company continues to exist but control of its affairs is transferred from the directors to the liquidator, who exercises his authority on behalf of the company.[79] In terms of section 136(4) of the Companies Act 2008, if liquidation proceedings have been converted into business rescue proceedings the liquidator is regarded as a creditor of the

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[74] In terms of the Companies Regulations 2011, reg 124, notification of affected persons must be done by delivering a copy of the court application in accordance with reg 7 to each affected person known to the applicant.

[75] It is submitted that this adjudication refers to a decision on the application for business rescue, in particular the refusal of the application (granting of the application is dealt with in the following paragraph of the section). *Cf Firstrand Bank Ltd v Imperial Crown Trading 143 (Pty) Ltd* 2012 (4) SA 266 (KZD).

[76] Companies Act 2008, s 131(6).

[77] See, for example, *Van Staden v Angel Ozone Products CC (in liquidation)* 2013 (4) SA 630 (GNP); *ABSA Bank Ltd v Summer Lodge (Pty) Ltd* 2013 (5) SA 444 (GNP); and *Richter v Bloempro CC* 2014 (6) SA 38 (GP).

[78] 2015 (5) SA 57 (SCA). In *Van der Merwe v Zonnekus Mansion (Pty) Ltd (in liquidation)* (4653/2015) [2015] WCC (10 June 2015); [2015] JOL 33379 (WCC) the judge disagreed with the decision by the Supreme Court of Appeal, but was bound by it. See also Levenstein 8-47.

[79] *Richter v Absa Bank Limited* 2015 (5) SA 57 (SCA), at para 10.

company to the extent of any outstanding amounts owing to him for any remuneration due for work performed, or compensation for expenses incurred, before the commencement of business rescue proceedings. Consequently, the conversion of liquidation to business rescue, even after a final liquidation order has been granted, was clearly envisaged by section 136(4).[80]

Counsel for respondents averred that the court's interpretation would in future lead to an abuse of proceedings in as much as interested parties dissatisfied with the liquidation order would connive to launch business rescue proceedings with the aim of avoiding the consequences of liquidation proceedings. The court noted that, unfortunately, there was an opportunity for deceit and dishonesty wherever one looked but was convinced that the courts would be alert to such an approach and would carefully examine all the relevant facts and circumstances. A purposeful interpretation of a statute should not be defeated by the possibility of possible deceitful conduct in the future.[81]

The court conceded that a liberal interpretation of section 131(6) may have negative results for the liquidation process. These would include repetitive disruptions and uncertainty that may result from various affected parties making applications for business rescue at different times during the winding-up process. The implementation of the Companies Act 2008 may produce some seemingly awkward results in the initial stages;[82] however, that does not justify an unduly restrictive approach in the interpretation of the provisions of the Companies Act 2008. The fact of the matter is that a court can dismiss any application for business rescue that is not genuine and *bona fide* or that does not establish that the benefits of a successful business rescue will be achieved.[83]

In *Van der Merwe and Others v Zonnekus Mansion (Pty) Limited (in liquidation) and Another (Commissioner for the South African Revenue Service and Another as Intervening Parties)*[84] the court pointed out that the decision in *Richter* is consonant with the position contemplated by the legislature in section 132(1)(c), namely that if a company is already in liquidation, business rescue only commences when a court places the company under the supervision of the business rescue practitioner. However, in terms of section 131(6), the mere launching of the application for business rescue has the effect of suspending the liquidation proceedings. This does not mean that the liquidators are deprived of their statutory powers, just that they are precluded

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[80] *Idem*, at para 12. Section 131(7) read with s 135(4) contemplates the conversion of a liquidation into rescue proceedings, no matter how far the liquidation and winding-up proceedings might have progressed – the liquidation proceedings are only concluded when the final account is confirmed by the Master – *Van Staden v Angel Ozone Products CC (in liquidation) and Others* 2013 (4) SA 630 (GNP), at paras 26 and 30.

[81] *Richter v Absa Bank Limited* 2015 (5) SA 57 (SCA), at para 16. It is not clear if the court would be able to avoid an abuse of proceedings in the time between the filing of the application and the hearing of the application by the court.

[82] The practice of applying for business rescue in the face of an existing liquidation process or proceedings may be susceptible to abuse – *Jansen van Rensburg NO and Another v Cardio-Fitness Properties (Pty) Limited and Others* [2014] JOL 31979 (GSJ), at para 34.

[83] *Idem*, at para 16. See also *Newcity Group (Pty) Ltd v Pellow NO and Others, China Construction Bank Corporation and Others (Newcity Group (Pty) Ltd v Pellow NO and Others; China Construction Bank Corporation Johannesburg Branch v Crystal Lagoon Investments 53 (Pty) Ltd and Others* (12/45437,16566/12) [2013J ZAGPJHC 54 (28 March 2013)), at para 25.

[84] [2017] JOL 39477 (WCC), at para 112. See also Levenstein 8-74; and Henochsberg 448(1), 449.

from exercising them. As the facts of this case demonstrated, this can result in an undesirable state of affairs should an unscrupulous individual seek to exploit the legal *lacuna* which the Companies Act 2008 occasions in relation to day-to-day control of the liquidated company. In view of the abuse of process in this case,[85] the court issued an order that pending the finalisation of any application for leave to appeal or subsequent appeals against the dismissal of the application, the:

(a) liquidation proceedings were not suspended; and

(b) liquidators were directed to take control of the company assets in accordance with the provisions of the Companies Act 1973, read with the provisions of the Insolvency Act; and

(c) applicant, in his personal capacity and representative capacity as a trustee and other parties were interdicted from launching further applications to place the company under supervision and business rescue proceedings to commence, as envisaged in section 131 of the Companies Act 2008, without the prior written authorisation of the Senior Duty Judge of the Division.

The fact that a considerable period of time has elapsed since the company was placed in liquidation means that far-reaching steps that may have been taken by the liquidator in the winding-up process, cannot be undone without undesirable consequences.[86] A factor that is relevant in deciding whether there is a reasonable prospect for rescue is if the company has been in liquidation for a considerable period of time. In a case where an application was launched four months after the final liquidation order was made – and came to be heard almost two years after liquidation proceedings commenced, the passage of so much time, during which the company had been financially paralysed and lacking in management and leadership, did not enhance the prospects of there being a successful business rescue.[87]

In *Jansen van Rensburg NO and Another v Cardio-Fitness Properties (Pty) Limited and Others*,[88] the court decided that despite an application for business rescue in terms of section 131 of the Companies Act 2008, assets of a company in liquidation remain in the custody and under the control of a provisional liquidator until a business rescue practitioner or a final liquidator has been appointed.

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[85] *Van der Merwe and Others v Zonnekus Mansion (Pty) Limited (in liquidation) and Another (Commissioner for the South African Revenue Service and Another as Intervening Parties)* [2017] JOL 39477 (WCC), at para 104.

[86] *Burmeister v Spitskop Village Properties Limited* (76408/2013) [2015] GP (16 September 2015), at para 44; and *Newcity Group (Pty) Ltd v Pellow NO and Others, China Construction Bank Corporation and Others (Newcity Group (Pty) Ltd v Pellow NO and Others; China Construction Bank Corporation Johannesburg Branch v Crystal Lagoon Investments 53 (Pty) Ltd and Others* (12/45437,16566/12) [2013J ZAGPJHC 54 (28 March 2013), at para 25.

[87] *Van der Merwe and Others v Zonnekus Mansion (Pty) Ltd and Others* (4653/2015B) [2016] ZAWCHC 11 (18 February 2016), at para 44.

[88] [2014] JOL 31979 (GSJ) 58. Also see *Knipe and Another v Noordman NO and Others* 2015 (4) SA 338 (NCK), at para 23. *Cf ABSA Bank Ltd v Summer Lodge (Pty) Ltd* 2014 (3) SA 90 (GP), at para 22.

A completely different view was taken by the court in *Maroos v GCC Engineering (Pty) Ltd*[89] where it was held that the application for business rescue suspended the powers of the provisional liquidators and thus re-vested the property of the company in the director of the company. However, and without any provision in the Companies Act 2008 supporting this decision, the court appointed a so-called "manager" (being the intended business rescue practitioner if the application succeeded) to manage the company until the application for commencement of business rescue was finalised.

Fortunately, the Supreme Court of Appeal overturned this decision in *GCC Engineering (Pty) Ltd and Others v Maroos and Others*[90] and stated that section 131(6) of the Companies Act 2008 does not change the status of the company in liquidation, nor does it suspend the court order that placed the company under liquidation. The appointed provisional joint liquidators had to proceed with their duties and functions to protect the assets of the company for the benefit of all the creditors of the company.[91] The court found that the appointment, office, and powers of the provisional liquidators were not suspended. In section 131(6) the legislature used the word "suspend", which does not mean termination of the office of liquidator. The term "liquidation proceedings" refers only to those actions performed by a liquidator in dealing with the affairs of a company in liquidation in order to bring about its dissolution. What is suspended is the process of winding-up and not the legal consequences of a winding-up order.[92] On the granting of the winding-up order, the directors of the company cease to function as directors and the property of the company falls under the control of the Master or the appointed liquidators. The directors of the company in liquidation are stripped of their control and management of the company placed in winding-up by the court. There is no legal provision, either statutory or at common law, that sanctions the re-vesting of control and management of the company in liquidation to the directors of the company.[93]

In *The Standard Bank of South Africa Limited v Gas2Liquids (Pty) Limited*[94] Satchwell J dismissed the contention that applications for liquidation could not proceed as they were suspended in terms of section 131(6) of the Companies Act 2008 where the requirement in respect of service by the Sheriff on the respondent, or the CIPC, or notice to all affected persons, in particular the shareholder, as is provided for in section 131, was not complied with. *Standard Bank of South Africa Limited v Midnight Feast Properties 4 (Pty) Limited*[95] agreed with this decision. *Engen Petroleum Limited v Multi Waste (Pty) Limited and Others*[96] held that an applicant must satisfy the court that all reasonable steps have been taken to notify all affected persons known to the applicant by delivering a copy of the court application to them in accordance with regulation 7. In this case the requirements of section 131 had not been complied with. However, the route of business rescue remains possible despite a final winding-up order having been granted.[97]

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[89] Case no 36777/2017 of 15 June 2017 (GP).
[90] 2019 (2) SA 379 (SCA). See also Levenstein 8-56; and Henochsberg 526 36.
[91] *GCC Engineering (Pty) Ltd and Others v Maroos and Others* 2019 (2) SA 379 (SCA), at para 15.
[92] *Idem*, at para 19.
[93] *Idem*, at para 21.
[94] Case No 45543 / 2012, unreported. See also Levenstein 8-53.
[95] [2017] JOL 39365 (GJ), at para 9.
[96] 2012 (5) SA 596 (GSJ), at paras 15 – 24.
[97] *Idem*, at para 11 with reference to *Richter v Absa Bank Limited* 2015 (5) SA 57 (SCA), at para 15.

The effect of a business rescue application on a pending application for liquidation has still not been settled. In *ABSA Bank Limited v Summer Lodge*[98] it was held that the application for liquidation was not suspended but in *Standard Bank of South Africa v A-Team Trading CC*[99] the court held the opposite because in its view the liquidation application also constituted liquidation proceedings.

The Supreme Court of Appeal has now also made it clear in *Lutchman NO v African Global Holdings (Pty) Ltd*[100] that the service and notification requirements prescribed in section 131(2) are not merely procedural steps but are substantive requirements that form an integral part of making an application for a business rescue order. As a result, a business rescue application will not have been made for purposes of section 131(6) and the suspension of liquidation proceedings will not be triggered until the application has been issued and served on the company (represented by the liquidators) and the CIPC, and each affected person has been notified in the prescribed manner.

Liquidators are entitled to oppose an application for business rescue and a punitive cost order was granted where an application for business rescue was an abuse of the process of the court.[101] Although the liquidators do not fall within any of the categories of affected persons as defined in the Companies Act 2008, if they are cited as parties they are entitled to participate in the proceedings as respondents and have the right to oppose the application if they so choose.[102]

2.3.2 *Requirements for compulsory commencement*

In terms of section 131(4), a court may make an order placing a company under supervision and commencing business rescue proceedings on application by an affected person if the court is satisfied that the requirements set out in this section have been met.

In terms of section 131(7) of the Companies Act 2008, a court may place a company into business rescue at any time during the course of any liquidation proceedings or proceedings to enforce any security against the company without any application for such an order having been made.[103]

2.3.2.1 *Financial distress*

The first requirement for a business rescue order deals with the financial situation of the company. As is the case with a voluntary commencement of business rescue, financial distress (as defined) is required. However, subsection (4) contains two alternatives to proving financial

[98] 2013 (5) SA 444 (GNP), at para 11.
[99] 2016 (1) SA 503 (KZP).
[100] 2022 (4) SA 529 (SCA).
[101] *Van Staden NO And Others v Pro-Wiz Group (Pty) Ltd* 2019 (4) SA 532 (SCA).
[102] *C Rock (Pty) v H C Van Wyk Diamonds Ltd and Others* (2355/2018Â) [2018] ZANCHC 91 (7 December 2018), at para 28.
[103] *Koen and Another v Wedgewood Village Golf & Country Estate (Pty) Ltd* (24850/11) [2011] ZAWCHC 464 (9 December 2011); [2012] JOL 29024 (WCC); 2012 (2) SA 378 (WCC), at para 8.

distress. These are, firstly, if the company has failed to pay over any employment-related amount that it was obliged to do in terms of a public regulation or a contract. This would include a failure to pay employees their salaries and other benefits, but also the failure to pay over medical aid contributions, pension fund contributions, income tax payments etcetera. The second alternative is if the court is satisfied that it is otherwise just and equitable for financial reasons.

Initially, it was held in a few cases that since the definition of financial distress refers to the future insolvency of a company within the next six months, a company that was already insolvent did not meet this requirement and could not be placed in business rescue, and that in such a case liquidation was more appropriate.[104] However, in *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd*[105] the Supreme Court of Appeal explained that a commercially insolvent company still met the requirement of financial distress and could thus be placed in business rescue, but also met the requirement for an insolvent winding-up because it was unable to pay its debts. Depending on the circumstances, there will be cases where liquidation may have advantages above business rescue.[106]

The Companies Act 2008 does not contain any explanation of what is meant by "otherwise just and equitable", but in *Tyre Corporation Cape Town (Pty) Ltd v GT Logistics (Pty) Ltd (Esterhuizen Intervening)*[107] the court held that should it be wrong in its view that an already insolvent company can still be regarded as being financially distressed, this alternative could be relied on instead of financial distress.

2.3.2.2 Prospect of rescue

The second, and most important requirement for a business rescue order contained in section 130(4), is that there must be a reasonable prospect of rescuing the company. Rescuing the company is defined in section 128(1)(h) to mean achieving the goals set out in the definition of business rescue, namely, to maximise the likelihood of the company continuing in existence on a solvent basis or if that is not possible, to result in a better return for creditors or shareholders than would result from the immediate liquidation of the company. In *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd*[108] the Supreme Court of Appeal explained that

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[104] (Case No 19075/11) [2012] ZAWCHC 33 (18 April 2012); and *FirstRand Bank Ltd v Lodhi 5 Properties Investment CC* (38326/2011) [2013] ZAGPPHC 515 (9 December 2013).

[105] 2013 (4) SA 539 (SCA).

[106] See the list set out in *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* 2012 (3) SA 273 (GSJ) 49. For example, a litany of court cases that a liquidator is better placed to deal with; business rescue may entail several court applications to obtain extensions; liquidation would be more appropriate in the case of a deadlock; there is no provision for the taxation of the fees of a business rescue practitioner; ss 26-31 of the Insolvency Act are available to a liquidator but not to a business rescue practitioner. In *Nedbank Ltd v Bestvest 153 (Pty) Ltd; Essa and Another v Bestvest 153 (Pty) Ltd and Others* 2012 (5) SA 497 (WCC) 58 the court referred to generalised claims and allegations not substantiated in any way at all but apparently based upon "well known" perceptions of winding-up procedures in general. The court decided that the applicants failed to demonstrate why business rescue is the preferred option over liquidation. The court added (at para 62) that disputed claims would remain unresolved under business rescue and in such circumstances winding-up would undoubtedly be the preferred option.

[107] 2017 (3) SA 74 (WCC).

[108] 2013 (4) SA 539 (SCA).

any of the two goals would constitute valid grounds for the commencement of business rescue and that they ranked equally.

As to whether there is such a reasonable prospect, it can hardly be said that it involves a range of choices that the court can legitimately make and of which none can be described as wrong. On the contrary the answer to the question whether there is such a reasonable prospect can only be "yes" or "no". If a court of higher instance should disagree with the conclusion of a court of a lower instance, the higher court is bound to interfere.[109] The phrase "reasonable prospect'" indicates that "something less is required than that the recovery should be a reasonable probability", as was required under judicial management.[110] Rather, there must be a "reasonable possibility".[111] The concept of a "prospect" is not something that is certain. By its very nature a prospect is future-looking and dependent upon a number of variables and includes a level of risk to the extent that the future is hardly capable of accurate prediction. What is required is not certainty but a determination on the facts and on the evidence presented that the future prospects of rescuing the business appear to be reasonable.[112]

Most companies with debt issues will consider business rescue for the benefit of the moratorium on claims. However, companies without a realistic hope of survival will inevitably end up in liquidation. There is therefore no merit in placing such companies into business rescue. A

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[109] *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* 2013 (4) SA 539 (SCA), at para 21, quoted with approval in *Newcity Group v Allan David Pellow NO* (577/2013) [2014] ZASCA 162 (1 October 2014), at para 15.

[110] *MFV "Polaris": Southern African Shipyards (Pty) Ltd v MFV "Polaris" and Others* [2018] 3 All SA 2019 (WCC), at para 60: the application fell substantially short of the prescribed mark. There was no basis upon which the court could exercise its discretion in putting the company into business rescue. There was an element of disingenuity and vexatiousness in the manner in which the application had been launched. Accordingly, it was correct that costs be awarded on a punitive scale (para 16). Since the legislature did not intend to repeat the mistakes of the past with judicial management, the pertinent question was whether the appellants had established a reasonable prospect of achieving any one of the two goals of business rescue – *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* 2013 (4) SA 539 (SCA), at para 28.

[111] *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* 2012 (3) SA 273 (GSJ) at 18; *Eveleigh v Dowmont Snacks (Pty) Ltd and Others* [2014] JOL 31954 (KZP), at para 24; *Welman v Marcelle Props 193 CC (Investec Bank Limited Intervening)* [2013] JOL 30620 (GSJ) at 15; *Zoneska Investments v Midnight Storm Investments 386 Ltd* (High Court Cape Town, Case No 9831/2011 28 August 2012 at 40); *Cardinet (Proprietary) Limited v Wedgewood Golf and Country Estate (Pty) Limited (in liquidation)* (Case No 19599/2012) WCHCC (30 January 2013), at para 43; *Propspec Investments (Pty) Ltd v Pacific Coast Investments 97 Ltd and Another* 2013 (1) SA 542 (FB), at para 8; *Mtolo and Others Guilder Investments 10 (Pty) Ltd and Others* (8706/2016) [2017] ZAKZDHC 6 (2 March 2017), at paras 21, 24 and 27; and *Siyahlanza Engineering CC v Hornet Properties Pty Ltd (in liquidation) and Another* [2018] JOL 40055 (GJ), at para 10.

[112] *The Employees of Solar Spectrum Trading 83 (Pty) Limited v Afgri Operations Limited* (Case No 6418/2011 High Court Pretoria 8 May 2012 at 34). A prospect here means an expectation, which in turn signifies a possibility. A possibility is reasonable if it rests on a ground that is objectively reasonable (per Van der Merwe J in *Propspec Investments (Pty) Ltd v Pacific Coast Investments 97 Ltd and Another* 2013 (1) SA 542 (FB), at para 12 as quoted with approval in *Lidino Trading 580 CC v Cross Point Trading (Pty) Limited In Re: Mabe v Cross Point Trading 215 (Pty) Limited* [2012] JOL 29305 (FB) at 18.

reasoned and factual basis for the belief that a company can be rescued is required – vague and speculative averments are not sufficient.[113]

Something more than a *prima facie* case or arguable possibility is needed. Naturally projections involve an element of speculation but they should not be so divorced from a factual foundation that they do not provide a basis on which the court can assess the company's return to solvency.[114] A court should not set the bar at such a height that the applicant for business rescue has little chance of clearing it and persuading the court to exercise its discretion to grant supervision.[115] One can envisage that in some instances the amount of evidence required will be less than in others, such as where the application is brought by somebody without in-depth knowledge of the affairs of the company. The test should therefore be flexible and the circumstances of each case will determine whether the available facts give rise to a reasonable prospect or not. It will be neither practical nor prudent to be prescriptive about the way in which the appellant must show a reasonable prospect in every case.[116]

Accordingly, there cannot be a checklist approach to business rescue applications – the relevant considerations in deciding whether a particular proposal meets the test may differ from case to case. Whilst every case must be considered on its own merits,[117] it has been stated that it is difficult to conceive of a rescue plan in a given case that will have a reasonable prospect of success of the company concerned continuing on a solvent basis unless it addresses the cause of the demise or failure of the company's business and offers a remedy that has a reasonable prospect of being sustainable. It is axiomatic that business rescue proceedings, by their very nature, must be conducted with the maximum possible expedition.[118] Where the applicant failed

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[113] *Kovacs Investments 571 (Pty) Ltd v Investec Bank Ltd and Another; Investec Bank Ltd v Aslo Holdings (Pty) Ltd* (25051/11, 18112/2011) [2012] ZAWCHC 110 (22 February 2012).

[114] *Tyre Corporation Cape Town (Pty) Ltd and Others v GT Logistics (Pty) Ltd (Esterhuizen and Another Intervening)* 2017 (3) SA 74 (WCC), at para 70. See also *BP Southern Africa (Pty) Ltd v Intertrans Oil SA (Pty) Ltd and Others* 2017 (4) SA 592 (GJ), at para 71.

[115] *Nedbank Ltd v Bestvest 153 (Pty) Ltd; Essa and Another v Bestvest 153 (Pty) Ltd and Others* 2012 (5) SA 497 (WCC) 38; *Cardinet (Proprietary) Limited v Wedgewood Golf and Country Estate (Pty) Limited (in liquidation)* (Case No 19599/2012) WCHCC (30 January 2013), at para 42; *Newcity Group (Pty) Ltd v Pellow NO and Others, China Construction Bank Corporation Johannesburg Branch v Crystal Lagoon Investments 53 (Pty) Ltd and Others* (12/45437, 16566/12) [2013] ZAGPJHC 54 (28 March 2013), at para 14; *Propspec Investments (Pty) Ltd v Pacific Coast Investments 97 Ltd and Another* 2013 (1) SA 542 (FB), at para 13; *Newcity Group (Pty) Ltd v Pellow NO and Others, China Construction Bank Corporation Johannesburg Branch v Crystal Lagoon Investments 53 (Pty) Ltd and Others* (12/45437, 16566/12) [2013] ZAGPJHC 54 (28 March 2013), at para 14; and *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* 2013 (4) SA 539 (SCA), at para 30.

[116] See Levenstein 8-43.

[117] *Zoneska Investments v Midnight Storm Investments 386 Ltd* (High Court Cape Town, Case No 9831/2011 28 August 2012 at 53).

[118] *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 (Pt) Ltd* (15155/2011 [2011] ZAWCHC 442 (25 November 2011); 2012 (2) SA 423 (WCC), at para 21; *Koen and Another v Wedgewood Village Golf & Country Estate (Pty) Ltd* (24850/11) [2011] ZAWCHC 464 (9 December 2011); [2012] JOL 29024 (WCC); 2012 (2) SA 378 (WCC), at para 10; and *AG Petzetakis International Holdings Ltd v Petzetakis Africa (Pty) Ltd and Others (Marley Pipe Systems (Pty) Ltd and Another Intervening)* 2012 (5) SA 515 (GSJ), at para 29. This does not mean that an application for business rescue is there for the asking. The rights and interests of all stakeholders must be balanced – *Welman v Marcelle Props 193 CC (Investec Bank Limited Intervening)* [2013] JOL 30620 (GSJ), at para 25; and *Cardinet (Proprietary) Limited v Wedgewood Golf and Country Estate (Pty) Limited (in liquidation)* (Case No19599/2012) WCHCC (30 January 2013), at para 44.

to deal in the founding affidavit with the circumstances leading to the downfall of the company and substantial creditors of the company indicated that they would not vote in favour of the business rescue proposal put forward by the applicant, the application for business rescue could not succeed. In such a case the application would be ill-conceived – the company would have failed to place cogent evidence before court to support the existence of a reasonable prospect of business rescue, instead having relied purely on conjecture and speculation.[119] Accordingly, business rescue is not simply there for the taking. A proper consideration of the application to commence business rescue is required.

It was stated by the Supreme Court of Appeal in *Newcity Group v Allan David Pellow NO*[120] that it is not appropriate to attempt to set out general minimum particulars of what would constitute a reasonable prospect of rescuing a company. It also seems that to require, as a minimum, concrete and objectively ascertainable details of the likely costs of rendering the company able to commence or resume its business, and the likely availability of the necessary cash resource in order to enable the company to meet its day-to-day expenditure, or concrete factual details of the source, nature and extent of the resources that are likely to be available to the company, as well as the basis and terms on which such resources will be available, is tantamount to requiring proof of a probability and unjustifiably limits the availability of business rescue proceedings.

Unlike the Companies Act 1973 where judicial management was granted instead of a liquidation order only in exceptional circumstances, the approach in the Companies Act 2008 is the opposite and business rescue is the preferred alternative to liquidation.[121] The difficulty in practice is that one is often not simply dealing with a case where the choice between the one or the other is evenly balanced. When business rescue will probably not rescue the company, it would be manifestly wrong to perpetuate the state of affairs by engaging in a prolonged business rescue.[122] In exercising its discretion, the court should give due weight to the legislative preference for rescuing ailing companies, but only if such a course is reasonably possible.[123] The applicant must place before the court[124] a cogent evidential foundation to support the

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[119] *C Rock (Pty) v HC Van Wyk Diamonds Ltd and Others* (2355/2018Â) [2018] ZANCHC 91 (7 December 2018), at paras 76, 78 and 79.

[120] (577/2013) [2014] ZASCA 162 (1 October 2014), at para 16, quoted in *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* 2013 (4) SA 539 (SCA), paras 29 to 31, with approval. See also *Al Maya International Limited (BVI) v Valley of the Kings Thaba Motswere Proprietary Limited and Others* (EL926/2016, 2226/16) [2016] ZAECELLC 5 (23 August 2016), at apara 23. See also Henochsberg 493.

[121] *Cf* the contrary approach in *Swart v Beagles Run Investments 25 (Pty) Ltd* (2011 (5) SA 422 (GNP)) [2011] ZAGPPHC 103; 26597/2011 (30 May 2011); [2012] JOL 28486 (GNP), at para 23 *et seq* where the judge expressed the view that s 427 of the Companies Act 1973 can be of assistance when interpreting the provisions for the new innovation of business rescue.

[121] Not "reasonably probable" that the company was viable and capable of ultimate solvency as was required under the judicial management provisions.

[122] *BP Southern Africa (Pty) Ltd v Intertrans Oil SA (Pty) Ltd and Others* 2017 (4) SA 592 (GJ), at para 79.

[123] *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 (Pt) Ltd* (15155/2011) [2011] ZAWCHC 442 (25 November 2011); 2012 (2) SA 423 (WCC), at paras 21-22; *Cardinet (Proprietary) Limited v Wedgewood Golf and Country Estate (Pty) Limited (in liquidation)* (Case No 19599/2012) WCHCC (30 January 2013), at para 53; and *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* 2013 (4) SA 539 (SCA), at para 33.

[124] *Newcity Group (Pty) Ltd v Pellow NO and Others, China Construction Bank Corporation Johannesburg Branch v Crystal Lagoon Investments 53 (Pty) Ltd and Others* (12/45437, 16566/12) [2013] ZAGPJHC 54 (28 March 2013),

existence of a "reasonable prospect" that the desired object of business rescue can be achieved, through either the continued existence of the company on a solvent basis or a better return than would result from the immediate liquidation of the company.[125]

It is not for the other affected persons to demonstrate that business rescue would not result in a better return for creditors and shareholders; rather it is up to the applicant for business rescue to demonstrate that business rescue would result in a better return. Section 131(4) does not afford the court a discretion in the strict sense. The court's discretion is bound up with the question whether there is a reasonable prospect for rescuing the company. If the court is not persuaded that there is a reasonable prospect of rescuing the company, it will dismiss the application and make any further order that is necessary and appropriate, including an order placing the company in liquidation.

The applicant is not required to set out a detailed plan but must establish grounds for the reasonable prospect of achieving one or two of the goals in section 128(1)(b). A business rescue plan that is unlikely to achieve anything more than to prolong the agony (that is, by substituting one debt for another without there being light at the end of a not too lengthy tunnel, is unlikely to suffice.[126] Business rescue proceedings cannot apply to companies conducting an unlawful business, for example where it was proposed that repayment of interest and investments of earlier investors would be made from later investments in a typical Ponzi scheme.[127] Business rescue proceedings are not for terminally ill companies or close corporations. Nor are they for the chronically ill.

Although affected parties are entitled to be heard in relation to a business rescue application, and although their attitude is relevant to the exercise of the court's discretion, the existence of a reasonable prospect of rescuing the company is a factual question, albeit involving a value judgment. If the court concludes that reasonable grounds for believing that the business can be rescued have not been established, the court cannot grant the application, even though many affected parties may support business rescue.[128] *ABSA Bank Limited v Newcity Group (Pty) Limited; Cohen v Newcity Group (Pty) Limited and Another*[129] cautions against the possible abuse of the business rescue procedure, for example by rendering the company temporarily immune to legal proceedings against it. In this case ulterior purpose was branded an abuse and

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at para 24. It seems unnecessary and impossible to require it in respect of (ii) – see the comments in Henochsberg in this regard. It remains to be seen how the absence of a "reasonable prospect for rescuing the company" will derail an application for business rescue based on jurisdictional requirement (ii) – *Newcity Group (Pty) Ltd v Pellow NO and Others, China Construction Bank Corporation Johannesburg Branch v Crystal Lagoon Investments 53 (Pty) Ltd and Others, supra*.

[125] *Koen and Another v Wedgewood Village Golf & Country Estate (Pty) Ltd* (24850/11) [2011] ZAWCHC 464 (9 December 2011); 2012 (2) SA 378 (WCC), at para 17; and *Slippers v Ingogo Wildlife Studio and Taxidermy CC and Another (Standard Bank of South Africa Limited Intervening) and Related Matters* [2019] JOL 44877 (GP).

[126] *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 (Pt) Ltd* (15155/2011 [2011] ZAWCHC 442 (25 November 2011); 2012 (2) SA 423 (WCC), at para 24; and *Lidino Trading 580 CC v Cross Point Trading (Pty) Limited In Re: Mabe v Cross Point Trading 215 (Pty) Limited* [2012] JOL 29305 (FB) 24.

[127] *Registrar of Banks v Dafel and Others* [2015] JOL 32711 (GP), at para 43.

[128] *Tyre Corporation Cape Town (Pty) Ltd and Others v GT Logistics (Pty) Ltd (Esterhuizen and Another Intervening)* 2017 (3) SA 74 (WCC), at para 76.

[129] [2013] JOL 30344 (GSJ), at paras 20.4 and 28. See also Levenstein 8-41; and Henochsberg 454.

the order was refused. The court stated that close scrutiny of the factual platform presented and the rationale mounted on that platform is required in order to decide if the threshold standard has been met. Such an assessment must be made on solid information presented to the court, not upon conjecture.[130]

It has now been settled by the Supreme Court of Appeal that an applicant is not required to set out a detailed plan in the business rescue application in order to satisfy the requirement that there is a reasonable prospect of rescuing the company.[131] To suggest that a rescue plan should be a prerequisite in meeting the requirements of reasonable prospects would not only be unduly onerous to an affected person who is an applicant in business rescue proceedings, but would have the effect of importing a requirement that the legislature did not envisage, regard being had to the architecture of the Companies Act 2008 as a whole.[132] It should be left to the business rescue practitioner to formulate the rescue package once he has had an opportunity to properly assess the company, its prospects going forward and, most importantly, the reasons for its commercial and financial distress.[133] The future rescue plan and its alternative objective are certainly factors that must be borne in mind when the rescue order is under consideration. For example, if an achievable draft rescue plan that has substantial support is provided at the time of the court application for the rescue order, this will improve the prospects of the application. The absence of a final plan at the court application phase will however not necessarily be fatal to the application.[134]

If a proposed plan is unfair, this would at least be relevant to the exercise of the court's discretion in deciding whether to place the company in business rescue.[135] The applicant should base the application for business rescue upon a strategy that has a reasonable prospect of achieving one of the two objectives stated in section 128(1)(b)(iii), that is, (i) it will maximise the likelihood of the company continuing in existence on a solvent basis, or, (ii) if it is not possible to continue in existence, results in a better return for the company's creditors or shareholders than would result from the immediate liquidation of the company. If such a strategy is not advanced in the application for business rescue, a court will hardly be satisfied that a reasonable prospect for rescuing the company exists.[136] The philosophy underlining the grant of a business rescue order

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130 *ABSA Bank Limited v Newcity Group (Pty) Limited; Cohen v Newcity Group (Pty) Limited and Another* [2013] JOL 30344 (GSJ), at para 20.3, quoted with approval in *Registrar of Banks v Dafel and Others* [2015] JOL 32711 (GP), at para 42.

131 *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* 2013 (4) SA 539 (SCA), at para 33.

132 *The Employees of Solar Spectrum Trading 83 (Pty) Limited v Afgri Operations Limited* (Case No 6418/2011 High Court Pretoria 8 May 2012 at 19).

133 *Nedbank Ltd v Bestvest 153 (Pty) Ltd; Essa and Another v Bestvest 153 (Pty) Ltd and Others* 2012 (5) SA 497 (WCC) at 40.

134 *AG Petzetakis International Holdings Ltd v Petzetakis Africa (Pty) Ltd and Others (Marley Pipe Systems (Pty) Ltd and Another Intervening)* 2012 (5) SA 515 (GSJ), at para 13.

135 *Tyre Corporation Cape Town (Pty) Ltd and Others v GT Logistics (Pty) Ltd (Esterhuizen and Another Intervening)* 2017 (3) SA 74 (WCC), at para 37. Similarly placed creditors could be differentially, even unfairly, treated in terms of the proposed plan.

136 *Newcity Group (Pty) Ltd v Pellow NO and Others, China Construction Bank Corporation Johannesburg Branch v Crystal Lagoon Investments 53 (Pty) Ltd and Others* (12/45437, 16566/12) [2013] ZAGPJHC 54 (28 March 2013), at para 13.

contemplates that the court cannot "second-guess" the rescue plan that will ultimately be approved by the creditors' meetings.[137]

Another issue that has arisen in respect of the requirement of a reasonable prospect of rescuing the company, is whether an indication by a major creditor who is opposing the application, that he would vote against any plan put forward by the rescue practitioner, should influence the court's decision. In the *Oakdene Square* case, the Supreme Court of Appeal stated that such intended opposition by a major creditor could not be ignored when a court had to decide whether there was a reasonable prospect of a rescue, but only if the creditor's opposition was reasonable.[138] However, in *The Employees of Solar Spectrum Trading 83 (Pty) Limited v Afgri Operations Limited*[139] the court could not imagine that it could be contended that it was a foregone conclusion that a major creditor would vote against the business plan even before one had been developed.[140] By virtue of section 132(2)(c)(i), read with section 152 of the Companies Act 2008, rejection of the proposed rescue plan by the majority of creditors will normally sound the death knell for the proceedings. It is true that such a rejection can be revisited by the court in terms of section 153, but that would take time and attract further costs. Moreover, the court is unlikely to interfere with the creditors' decision unless their attitude was unreasonable.[141] However, in the recent decision of the Supreme Court of Appeal in *Ferrostaal GmbH v Transnet SOC Ltd (t/a Transnet National Ports Authority)*[142] it was confirmed that the test whether a creditor was reasonable in voting against a plan was an objective one taking the interests of all the affected persons into consideration and not merely the subjective interests of the particular creditor.

If the aim is to continue trading on a solvent basis, one would expect to be given some concrete and objectively ascertainable details going beyond mere speculation in the case of a trading or prospective trading company, of the –

- likely costs of rendering the company able to commence with its intended business, or to resume the conduct of its core business;

[137] *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* 2012 (3) SA 273 (GSJ).

[138] This was also the view of the courts in *Shoprite Checkers (Pty) Ltd v Berryplum Retailers CC* (47327/2014) [2015] ZAGPPHC 255 (11 March 2015) and *FirstRand Bank Limited v Normandie Restaurants Investments* [2016] ZASCA 178 (25 November 2016).

[139] Case No 6418/2011, High Court Pretoria, 8 May 2012 at 37. See also Levenstein 8-38; and Henochsberg 503.

[140] In *Zoneska Investments v Midnight Storm Investments 386 Ltd* (High Court Cape Town, Case No 9831/2011 28 August 2012 at 67) the court stated that the fact that the major creditors had indicated that they would not approve any sale of the property on the proposed conditions would not always be a weighty consideration. Although s 152(2)(a) requires the support of 75% of the creditors' voting interests for a business rescue plan, s 153 provides for certain further steps that can be taken in the event of such support not being forthcoming. This would, however, require a further application to court should the business practitioner wish to proceed and bring about further delays and costs, which is ultimately not in the creditors' best interests.

[141] *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* 2013 (4) SA 539 (SCA), at para 38.

[142] 2021 (5) SA 493 (SCA).

- likely availability of the necessary cash resource in order to enable the ailing company to meet its day-to-day expenditure once its trading operations commence or are resumed. If the company will be reliant on loan capital or other facilities, one would expect to be given some concrete indication of the extent thereof and the basis or terms upon which it will be available;

- availability of any other necessary resource, such as raw materials and human capital; and

- reasons why it is suggested that the proposed business plan will have a reasonable prospect of success.[143]

In relation to the alternative aim[144] of business rescue referred to in section 128(b)(iii) of the Companies Act 2008, being to procure a better return for the company's creditors and shareholders than would result from the immediate liquidation of the company, one would expect an applicant for business rescue to provide concrete factual details of the source, nature and extent of the resources that are likely to be available to the company, as well as the basis and terms on which such resources will be available. In *The Commissioner, South African Revenue Service v Beginsel NO and Others*[145] "better return" was held to mean more money distributed overall to creditors than in liquidation.[146] It is difficult to see how, without such details, a court will be able to compare the scenario sketched in an application with that which would obtain in an immediate liquidation of the company. Mere speculative suggestions are unlikely to suffice.[147]

In *Gormley v West City Precinct Properties (Pty) Ltd* [148] the application was refused as there was no plan put forward at all. When the papers were analysed, it became apparent that the application boiled down to nothing more than the winding-down of the company in a manner

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[143] *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 (Pt) Ltd* (15155/2011 [2011] ZAWCHC 442 (25 November 2011); 2012 (2) SA 423 (WCC), at para 24, quoted with approval in *Koen and Another v Wedgewood Village Golf & Country Estate (Pty) Ltd* (24850/11) [2011] ZAWCHC 464 (9 December 2011); [2012] JOL 29024 (WCC); 2012 (2) SA 378 (WCC), at para 16.

[144] *AG Petzetakis International Holdings Ltd v Petzetakis Africa (Pty) Ltd and Others (Marley Pipe Systems (Pty) Ltd and Another Intervening)* 2012 (5) SA 515 (GSJ), at para 12, remarked as follows: "The creation of the alternative object will probably give rise to more litigation. It is, for example, strange to create an object for a new remedy in a definition section".

[145] 2013 (1) SA 307 (WCC) at 58.

[146] See also Henochsberg 498.

[147] *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* 2013 (4) SA 539 (SCA), at para 34; *Eveleigh v Dowmont Snacks (Pty) Ltd and Others* [2014] JOL 31954 (KZP), para 24; *Propspec Investments (Pty) Ltd v Pacific Coast Investments 97 Ltd and Another* 2013 (1) SA 542 (FB), at para 26; and *Al Maya International Limited (BVI) v Valley of the Kings Thaba Motswere Proprietary Limited and Others* (EL926/2016, 2226/16) [2016] ZAECELLC 5 (23 August 2016), at para 23. In *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 (Pt) Ltd* (15155/2011 [2011] ZAWCHC 442 (25 November 2011); 2012 (2) SA 423 (WCC), at para 25 the following was pointed out: not a single fact was placed before the court as to why creditors could expect a larger dividend at the end of the moratorium; only generalisations were put forward. See also *The Commissioner for the South African Revenue Service v The Business Zone 983 CC* (9673/2015) [2015] WCC (7 September 2015); [2017] JOL 37888 (WCC), at para 79.

[148] (Case No 19075/11 High Court Cape Town 18 April 2012, at para 12). See also Levenstein 7-10; and Henochsberg 494.

that disregarded the rights of creditors. The court in *African Banking Corporation of Botswana Ltd v Kariba Furniture Manufacturers (Pty) Ltd and Others*[149] noted that there is no reasonable prospect of rescuing a company where it is clearly hopelessly insolvent and effectively dormant in that it had not traded for years and had no business contracts in place.

The applicant, as the master of the suit (*dominus litis*), must satisfy the court that there are reasonable prospects of achieving a better return for creditors than would result from immediate liquidation.[150] In *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others*,[151] on the respondents' version, the company had been stripped of all its income and virtually all its assets while under the management of the company. The court stated that these are the very circumstances at which the investigative powers of the liquidator – under sections 417 and 418 of the Companies Act 1973[152] and the machinery for the setting aside of improper dispositions of the company's assets provided for in the Insolvency Act – are aimed.[153] In light of this there was a very real possibility that liquidation would in fact be more advantageous to creditors and shareholders than the proposed informal winding-up of the company through business rescue proceedings.[154]

According to *Griessel and Another v Lizemore and Others*,[155] a person who wishes to place a company under business rescue on the alternative ground that it would result in a better return for the company's creditors or shareholders than would result from the immediate liquidation of the company, must satisfy three criteria:

(a) that the company is financially distressed as required under section 129(1)(a) of the Companies Act 2008;

(b) that it is not reasonably likely (or perhaps possible) for the company to be rehabilitated and continue in existence on a solvent basis as contemplated in section 128(1)(b)(iii); and

[149] 2015 (5) SA 192 (SCA), at paras 28 and 55. See also Henochsberg 494.

[150] *Ex parte Target Shelf 284 CC (in business rescue); Commissioner, South African Revenue Service and Another v Cawood NO and Others* [2017] JOL 37690 (GP), at para 51.

[151] 2013 (4) SA 539 (SCA), at para 35. See also Levenstein 7-13.

[152] In terms of s 424 of the Companies Act 1973 any creditor of the company can bring proceedings under that section and at any time, whether the company is under winding-up or not – also in the event of business rescue. See *Collard v Jatara Connect (Pty) Ltd* 2018 (5) SA 238(WCC), at para 25.

[153] See also *The Commissioner for the South African Revenue Service v The Business Zone 983 CC* (9673/2015) [2015] WCC (7 September 2015), at para 96; *Burmeister v Spitskop Village Properties Limited* (76408/2013) [2015] GP (16 September 2015), at para 41; and *Van der Merwe and Others v Zonnekus Mansion (Pty) Limited (in liquidation) and Another (Commissioner for the South African Revenue Service and Another as Intervening Parties)* [2017] JOL 39477 (WCC), at para 79.

[154] *Newcity Group v Allan David Pellow NO* (577/2013) [2014] ZASCA 162 (1 October 2014), at para 21 stated the following: "But, as was pointed out in *Oakdene Square Properties*, [*Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* 2013 (4) SA 539 (SCA), at para 33] the mere savings on the costs of the winding-up process in accordance with the existing liquidation provisions [can] hardly justify the separate institution of business rescue". See also *Pouroullis v Market Pro Investments 106 (Pty) Ltd (South African Bank of Athens Ltd and Absa Bank Ltd* (20370/2015) [2016] ZAGPJHC 12 (12 February 2016), at para 24.

[155] 2016 (6) SA 236 (GJ), at para 79. See also Levenstein 7-14(2); and Henochsberg 495.

(c) that the development and implementation of a plan to rescue the company would result in a better return for creditors or shareholders than would occur from its immediate liquidation.

2.3.3 Business rescue order by court

An applicant seeking an order commencing business rescue must nominate a business rescue practitioner for appointment in the application. If the court subsequently makes an order placing the company into business rescue, the court must make a further order appointing as interim practitioner the person so nominated. It must be noted, however, that this appointment is subject to ratification by a majority of the independent creditors at the first meeting of creditors, as contemplated in section 147 of the Companies Act 2008.

If the company is placed in business rescue by the court, the company must notify each affected person of the order within five business days after the date of the order.[156] The company may also not adopt a resolution placing itself in liquidation until the business rescue proceedings have ended.[157]

The court's inherent jurisdiction in regard to costs applies to proceedings under section 131 and the court may order that the applicant's costs, taxed on the scale between attorney and client, must be paid by the company.[158]

If the court dismisses the application, it may make any further necessary and appropriate order, including an order placing the company in liquidation.[159]

2.4 Duration and termination of business rescue proceedings

2.4.1 Report on progress of business rescue proceedings

If a company's business rescue proceedings have not ended within three months after the start of those proceedings, or such longer time as the court, on application by the practitioner, may allow, the practitioner must –

(a) prepare a report on the progress of the business rescue proceedings and update it at the end of each subsequent month until the end of those proceedings; and

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[156] Companies Act 2008, s 131(8)(a). The company must also inform the CIPC by uploading the prescribed information and court order on the CIPC New E-Services (Practice Note 3 of 2021). There is no prescribed form for these notifications but the process is prescribed by reg 123(6) of the Companies Regulations 2011.

[157] Companies Act 2008, s 131(8)(b).

[158] *Cape Point Vineyards (Pty) Ltd v Pinnacle Point Group Ltd (Advantage Projects Managers (Pty) Ltd Intervening)* 2011 (5) SA 600 (WCC), at paras 2 and 3.

[159] Companies Act 2008, s 131(4)(b).

(b) deliver the report and each update in the prescribed manner to each affected person and to the court, if the proceedings have been the subject of a court order, or the Commission in any other case.

The report must be filed together with a duly completed Form CoR 125.1.[160]

It is submitted that this three-month period is relatively short when one considers the nature and exigencies of corporate rescue. It is very unlikely that a successful business rescue will be completed within three months. Accordingly, there can obviously not be an inflexible rule as to how long it should be before a rescue can be said to have been successful.[161] However, it is clear that the legislature intended by its use of the word "temporary" that any rescue plan should not be of indeterminable duration. The fact that section 132(3) of the Companies Act 2008 requires reports on progress to be filed if the rescue proceedings are not completed within a period of three months, is a strong indication of the legislature's intention that the implementation of a plan should be of short duration.[162] Creditors cannot be left in a state of flux for an indefinite period.[163] A situation where an extraordinary amount of time is taken to achieve business rescue would be at the expense of the rights of creditors. The balancing of these rights should always be paramount in the ambit of fairness.[164] Business rescue proceedings cannot go on indefinitely. It was not the intention of the legislature that creditors be held to ransom and prevented from exercising their normal contractual rights for an extraordinarily long period of time.

2.4.2 Termination of business rescue proceedings

In terms of section 132(2) of the Companies Act 2008, business rescue proceedings end in one of the following ways:

(a) The court sets aside the resolution or the order that commenced these proceedings.

(b) The court has converted the proceedings to liquidation proceedings. In the recent judgment of *Commissioner for the South African Revenue Services v Louis Pasteur Investments (Pty) Ltd*[165] it was held that this subsection confirms the inherent right of the court to hear a liquidation application even after a rescue plan (which was referred to as a "sham" by the court) has been approved.

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[160] See Practice Note 3 of 2021 issued by the CIPC on 28 July 2021.

[161] See Levenstein 8-73.

[162] *Van der Merwe and Others v Zonnekus Mansion (Pty) Ltd and Others* (4653/2015B) [2016] ZAWCHC 11 (18 February 2016), at para 39.

[163] *Gormley v West City Precinct Properties (Pty) Ltd* (Case No 19075/11 High Court Cape Town 18 April 2012 at 11); *Ex parte Target Shelf 284 CC (in business rescue); Commissioner, South African Revenue Service and Another v Cawood NO and Others* [2017] JOL 37690 (GP), at para 23; and *Van der Merwe and Others v Zonnekus Mansion (Pty) Limited (in liquidation) and Another (Commissioner for the South African Revenue Service and Another as Intervening Parties)* [2017] JOL 39477 (WCC), at para 41.

[164] *South African Bank of Athens Limited and Another v Zennies Fresh Fruit CC* 2018 (3) SA 278 (WCC), at para 38. In this matter the court held at para 43 that the delay in the finalisation of the business rescue proceedings was unreasonable in the circumstances and an order was justified terminating the proceedings.

[165] Case No 12194/2017 (11 April 2022) Pretoria High Court.

(c) The practitioner has filed a notice of termination of the business rescue proceedings with the CIPC. Practice Note 3 of 2021[166] stipulates that Form C0R 125.2 must be used for this notice and must be accompanied by a statement on a letterhead setting out the grounds for termination if these grounds are not stated on the Form. In addition, there must be a confirmation of the specific grounds containing the detailed information as required in the Practice Note depending on the grounds indicated.

(d) A business rescue plan has been proposed and rejected and no affected person has acted to extend the proceedings as contemplated in section 153.[167] Section 153(5) requires that the practitioner must promptly file a notice of the termination of the business rescue proceedings. The question was whether the proceedings end automatically as soon as the plan is rejected and no further action is taken which is what section 132(2)(c)(ii) appears to provide, or whether a notice of termination is required to terminate the proceedings. In *The Land and Agricultural Development Bank of South Africa v Agri Oil Mills (Pty) Ltd*[168] it was held that the filing of the notice was an administrative requirement to inform the CIPC that the proceedings have ended, and the mere rejection of the plan without any further action being taken by affected persons was sufficient to terminate the proceedings. This was also the view of the court in *Rogal Holdings (Pty) Ltd and Another v Victor Turnkey Projects (Pty) Ltd and Others.*[169]

(e) A business rescue plan has been adopted and the practitioner has subsequently filed a notice of substantial implementation of the plan on Form CoR 125.3.[170]

In terms of section 141(2)(a) of the Companies Act 2008, if at any time during business rescue proceedings the business rescue practitioner concludes that there is no reasonable prospect for the company to be rescued, the practitioner must so inform the court, the company and all affected persons, in the prescribed manner, and apply to court for an order discontinuing the business rescue proceedings and placing the company into liquidation.

In *The Commissioner of South African Revenue Service v Primrose Gold Mines (Pty) Ltd and 2 Others*[171] the judge took a view that the business rescue practitioner was the person suited to apply to court for the discontinuance of the business rescue proceedings. However, in *Ex parte Target Shelf 284 CC (in business rescue); Commissioner, South African Revenue Service and Another v Cawood NO and Others*[172] the judge concluded that on a proper reading of section 132(2)*(a)* it was not specifically stated who should apply to have the business rescue proceedings set aside or converted to liquidation proceedings. In the circumstances of the matter, the creditors were entitled to apply for conversion of the business rescue proceedings.

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166 Issued by the CIPC on 28 July 2021.

167 The remedies available to affected persons in terms of s 153 if the business rescue plan is rejected, are discussed in Ch 10.

168 2021 JDR 1238 (KZP).

169 2022 JDR 1031 (GP).

170 A Notice of Substantial Implementation is also regulated by Practice Note 3 of 2021 and must be accompanied by a calculation of the company's PI Score at the end of implementation of the plan.

171 (56581/2014) [2014] 26 ZAGPPHC (12 September 2014). See also Levenstein 9-144.

172 [2017] JOL 37690 (GP) at 74.

Section 141(2)(b) deals with the situation where, during the business rescue proceedings, the practitioner comes to the conclusion that there no longer are reasonable grounds to believe that the company is financially distressed. In such a case, the practitioner must so inform the court, the company, and all affected persons. If the business rescue was confirmed by a court order in terms of section 130 or initiated by an application to court in terms of section 131, the practitioner must apply to court for an order terminating the business rescue proceedings. In other cases, the practitioner must file a notice of termination of the business rescue proceedings.

Self-Assessment Questions for Chapter 2

Where necessary, refer to the Case Study in Chapter 1 of these notes when answering the questions below.

Question 1

Shortly after his appointment as the business rescue practitioner, Mr A Float discovered that Fast Flights had only notified Fair-Labour-For-All of the filing of the business rescue resolution. No attempt had been made to notify the remaining 9% of employees who were either members of an unregistered trade union or not members of any trade union.

Mr Float is worried about the effect or potential effect this omission could have on the validity of the business rescue proceedings. Explain the legal position to him with reference to the Companies Act 2008, the Company Regulations 2011 and case law.

Question 2

At the first meeting of creditors, the three creditors who took, or threatened to take steps to enforce their claims before the board resolution was filed, inform Mr Float that in their view the resolution and thus the business rescue was void because the resolution was adopted after they had taken the first steps to have the company liquidated. Advise Mr Float whether there is any merit in their argument.

Question 3

Section 129(3)*(a)* requires that the notice of filing of a business rescue resolution must be accompanied by an affidavit setting out the facts regarding the grounds on which the board resolution was taken. Practice Note 3 of 2021 contains more detailed instructions on how this should be done. Draft the relevant part of the affidavit in which these reasons and grounds are explained as they existed at the time of taking the resolution.

Question 4

Advise Mr Float on the correct and appropriate way to terminate the business rescue proceedings in the circumstances set out in the final paragraph of the Case Study.

For feedback on this self-assessment exercise, see the document "Comment and Feedback on Self-Assessment Questions", which is made available to you as a separate document.

CHAPTER 3

THE GENERAL MORATORIUM

3.1 Introduction

The general moratorium is arguably one of the most important features of business rescue. In line with allowing a company in financial distress sufficient breathing space to restructure its affairs, the general moratorium aids in achieving this purpose by placing a stay or prohibition on all legal proceedings against the company while the company is in business rescue.

This is provided for in section 133(1) of the Companies Act 2008, which states that no legal proceedings, including enforcement action, may be commenced or proceeded with against the company or in relation to any property belonging to the company, or lawfully in its possession, unless the written consent of the business rescue practitioner has been obtained or with the leave of the court. The moratorium therefore provides a period of respite for a company to restructure its affairs in such a way which would allow it to resume operations.

The importance of the general moratorium has been judicially recognised by a number of cases since the introduction of Chapter 6 of the Companies Act 2008. In the case of *Murray NO and Another v FirstRand Bank Ltd*[173] the SCA stated that:

> "It is generally accepted that a moratorium on legal proceedings against a company under business rescue, is of cardinal importance since it provides the crucial breathing space or a period of respite to enable the company to restructure its affairs. This allows the practitioner, in conjunction with the creditors and other affected parties, to formulate a business rescue plan designed to achieve the purpose of the process."

Another important feature of the general moratorium, taking into consideration the rights of creditors, is that if the enforcement of any claim against the company is subject to time limit, according to section 133(3) of the Companies Act such time limit prescribed for the enforcement of such claim will be suspended for the duration of the business rescue proceedings. The moratorium therefore achieves a complex balance of the interests of the company under business rescue and the legal rights of affected persons / creditors. On the one hand it balances the need to prevent an influx of litigation against the company while it restructures its affairs and on the other hand it considers the impact of such moratorium on the rights of creditors and therefore allows the time limit within which an affected person is to enforce its claim, to be suspended. This balancing exercise is consistent with the purpose of the Companies Act (specifically business rescue) set out in section 7(k), as follows – "to provide for the efficient rescue and recovery of financially distressed companies in a manner that balances the rights and interests of all the relevant stakeholders".

[173] 2015 (3) SA 438 (SCA).

3.2 Application

As mentioned, the general moratorium is a crucial element of business rescue proceedings, as it allows the company sufficient breathing space to be able to find a solution to the financial problems it is experiencing at that time.[174] It is a personal but temporary benefit that it is only available to the company in business rescue and its business rescue practitioner. In the case of *Timasani (Pty) Ltd (in business rescue) and Another v Afrimat Iron Ore (Pty) Ltd*[175] the SCA stated that:

> "The general moratorium in s 133(1) is a defence *in personam*: it is a personal, temporary benefit in favour of a company undergoing business rescue that cannot be utilised indefinitely to delay the claims of creditors or result in the extinction of their claims. Indeed, and as stated, legal proceedings in relation to those claims may be initiated or continued with the consent of the BRP or leave of the court."

As the moratorium is a defence *in personam*, a creditor has no *locus standi* to rely on non-compliance with the section. Only the business rescue practitioner may seek its protection and only the business rescue practitioner may waive or consent to dispense with compliance therewith.[176]

The moratorium applies only for the duration of the company's business rescue proceedings. However, section 150(2)(b)(i) provides that a business rescue plan may make provision for the moratorium to extend beyond the duration of the business rescue proceedings. Henochsberg[177] however submits that such a moratorium will not be a wide one such as the one envisaged in section 133. It must be specific, applying to a particular creditor or creditors, or to particular circumstances that warrant the extension of a moratorium beyond the duration of the business rescue proceedings.

In considering the phrase "no legal proceedings, including enforcement action against the company", the following is important to bear in mind –

- Chapter 6 does not define "legal proceedings" or "enforcement action", but according to the case of *Blue Star Holdings (Pty) Ltd v West Coast Oyster Growers CC*[178] the intention of section 133 is clear – it is to cast the net as wide as possible in order to include any conceivable type of action against the company such as liquidation proceedings.

- In the case of *Merchant West Working Capital Solutions (Pty) Ltd v Advanced Technologies and Engineering Company Ltd*[179] the court held that the term "legal proceedings" in the

[174] Henochsberg 523.
[175] [2021] 3 All SA 843 (SCA).
[176] *Chetty t/a Nationwide Electrical v Hart NO and Another* [2015] 4 All SA 401 (SCA).
[177] Henochsberg 523.
[178] 2013 (6) SA 540 (WCC).
[179] 13/12406, 10 May 2013 (GSJ).

context of section 133 could only attract its ordinary meaning. Legal proceedings would therefore include any matter to be referred to court, tribunal or any other formal proceedings which are intended to adjudicate a matter, specifically including that of proceedings instituted to perfect security.

- The SCA considered the meaning of "enforcement action" in the case of *Cloete Murray and Another NNO v FirstRand Bank Ltd t/a Wesbank*[180] and held that the cancellation of a master instalment agreement during business rescue proceedings was not a "legal proceeding, including enforcement action", requiring the written consent of the business rescue practitioner or leave of the court. "Enforce" and "enforcement" usually refer to the enforcement of obligations. The SCA was of the view that "enforcement action" was therefore a species of legal proceeding. This conclusion was strengthened by the fact that section 133(1) provides that "no legal proceeding, including enforcement action, . . . may be commenced or proceeded with in any forum". In addition, the court held that the terms "enforcement" and "cancellation" are mutually exclusive. The term "cancellation" refers to the termination of obligations between parties to an agreement.

In relation to the phrase "or in relation to any property belonging to the company, or lawfully in its possession", the following must be considered –

- The moratorium only extends its protection to anyone attempting to lay claim to the company's own property, or lawfully in its possession.[181] The moratorium is not applicable to legal proceedings involving property belonging to another company or property unlawfully possessed by the company in business rescue.

- If the company is not lawfully in possession of the property, that is, because those rights are based on a contract that was validly cancelled, section 133 does not apply. In the case of *Madodza (Pty) Limited v Absa Bank Limited and Others*[182] the court found that certain vehicles that were the subject of finance agreements which had been cancelled were not lawfully in the possession of the company in business rescue and that as a result section 133(1) was not an obstruction to the recovery of the vehicles. The court found that whenever a company lacks the *jus possidendi* to possess an asset it is not in lawful possession of it and cannot be protected by section 133(1).

- In the case of *Kythera Court v Le RendezVous Café CC and Another*[183] an applicant brought an application to evict a company in business rescue from its premises. Prior to the commencement of the business rescue, the company had fallen into arrears of its rental obligations. The landlord therefore cancelled its lease on 7 March 2016 (after the date of the commencement of business rescue). The company refused to vacate the premises on the basis of section 133 and argued that the landlord was precluded from cancelling the lease and launching the eviction application. The court held that the juristic act of cancelling

[180] 2015 (3) SA 438 (SCA).
[181] *Timasani (Pty) Ltd (in business rescue) and Another v Afrimat Iron Ore (Pty) Ltd* [2021] 3 All SA 843 (SCA).
[182] 38906/2012, 15 August 2012 (GNP), at para 12.
[183] 2016 (6) SA 63 (GJ) (22 June 2016).

the lease agreement does not constitute an enforcement action in terms of section 133(1) and it was therefore permissible for an agreement to be cancelled during business rescue proceedings. The court confirmed that the moratorium does not apply when the property in question does not belong to the company in business rescue or is not lawfully in its possession. Thus, eviction proceedings in relation to property not in the unlawful possession of a company in business rescue, are permissible. This judgment provides certainty for landlords as it has been determined that section 133(1) does not encompass legal proceedings for ejectment when a lease has been validly cancelled and the company in business rescue is an unlawful possessor of the property.

The words "in any forum", extends to legal proceedings/actions brought by way of arbitration proceedings. The SCA in *Chetty t/a Nationwide Electrical v Hart NO and Another*[184] held that arbitration proceedings were indeed legal proceedings for the purposes of section 133(1) and that the purpose of section 133(1), requires the term "legal proceedings" to be construed widely.

The moratorium does not extend to juristic acts such as the cancellation of an agreement / contract, or the dispatch of a letter of demand.

The High Court has exclusive jurisdiction over business rescue matters as business rescue proceedings affect the rights of a number of parties beyond the employment relationship and, in particular, shareholders and other creditors. The High Court is therefore best placed to balance the rights and interests of all relevant parties. The Labour Court in the case of *National Union of Metalworkers of South Africa (NUMSA) obo Members and Others v South African Airways and Others*[185] confirmed that the High Court has exclusive jurisdiction over business rescue matters and, as such, a party seeking to initiate proceedings, including those that concern an employment-related claim, against a company in business rescue, must secure the written consent of the business rescue practitioner or obtain the leave of the High Court to institute those proceedings.

3.3 Instances in which the moratorium may be lifted

The moratorium is not an absolute bar to legal proceedings. It merely serves as a procedural limitation on a party's rights of action and section 133 sets out a number of exceptions in which legal proceedings, including enforcement action, may be commenced or proceeded with.

These exceptions include –

- Section 133(1)(a) – with the written consent of the business rescue practitioner.

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[184] [2015] 4 All SA 401 (SCA).
[185] (2021) 42 ILJ 1256 (LC).

Henochsberg states that:

> "The consent required in terms of subs (1) is not a jurisdictional fact, i.e. a condition precedent for the proceedings (including arbitration) to commence or proceed, the absence of which carries with it the implication that a Court or tribunal has no power or competence to determine an issue between the parties and if it, nevertheless, proceeds to determine the matter notwithstanding, the absence of jurisdiction will have the consequence that the proceedings are void. Section 133 (1) is merely a procedural limitation and not an absolute bar against institution of proceedings, as a creditor can still initiate proceedings, inter alia, subject to the written consent of the business rescue practitioner (subs (1) (a)) or leave of the Court (subs (1) (b)). This is a strong indication that noncompliance will not result that the proceedings will be a nullity…"

In most cases, the business rescue practitioner will not consent to the legal proceedings to be commenced or proceeded with unless it benefits the company in business rescue.

- Section 133(1)(b) – with the leave of the court.

  In the case of *Merchant West Working Capital Solutions (Pty) Ltd v Advanced Technologies and Engineering Company (Pty) Ltd and Another*[186] the court held that:

  > "'Leave of the court' as laid down in section 133(1)(b) cannot be a simple one that can be advanced from the bar. Such leave in my view and finding must be motivated in the same way, just like, for instance, as criteria for departure from the Rules of Court to justify a prayer for urgency. A court being asked for leave to proceed against a company under business rescue, thus during a moratorium, must receive a well-motivated application for that so that it could apply its mind to the facts and the law if necessary and then be in a position to make a ruling in accordance with any terms it may consider suitable in the peculiar circumstances."

  In *Arendse and Others v Van der Merwe and Another NNO*[187] the court held that an applicant seeking to obtain leave under the section must as a minimum requirement establish a *prima facie* case against the company in business rescue and the court will consider the following factors –

  - the effect that the grant or refusal of leave would have on the applicants' rights as opposed to other affected persons and relevant stakeholders;
  - the impact that the proposed legal proceedings would have on the wellbeing of the company and its ability to regain its financial health; and

[186] 13/12406, 10 May 2013 (GSJ).

[187] [2016] 4 All SA 48 (GJ), 2016 (6) SA 490 (GJ). See also *Mabote and Others v Van der Merwe NO and Another* (2015/40324) [2016] ZAGPJHC 185 (8 July 2016).

- whether the grant of leave would be inimical to the object and purpose of business rescue proceedings as set out in sections 7 (k) and 128 (b) of the Act.

There are, however, instances where neither the consent of the business rescue practitioner nor the leave of the court is required –

- where an affected person exercises the right in terms of section 130(1) to set aside the voluntary business rescue process initiated in terms of section 129. The court in *LA Sport 4X4 Outdoor CC and Another v Broadsword Trading 20 (Pty) Limited and Others*[188] held that there is also no indication that the right in section 130(1) is subject to section 133(1). This was confirmed in the case of *Resource Washing (Pty) Ltd v Zululand Coal Reclaimers Proprietary Limited and Others*[189] where the applicant sought an order granting leave in terms of section 133(1)(b) to launch proceedings to set aside the resolution in terms of section 130(1)(a) and 130(5)(a). The court herein held that there was no need to apply in terms of section 133(1)(b) for leave to institute proceedings to set aside the resolution, as sections 130(5) and 132(2)(a)(i) "permit applications to court to set aside a company's resolution to begin business rescue proceedings without rendering these sections subject to the leave of the court being granted in terms of s 133";[190]

- an application to remove a business rescue practitioner in terms of section 139; and

- any proceedings relating to the business rescue plan proposed by the business rescue practitioner. In the case of *Moodley v On Digital Media (Pty) Ltd and Others*[191] an application was brought to set aside the adopted business rescue plan. The question before the court was whether the moratorium in section 133 applied to proceedings relating to the development, adoption or implementation of a business rescue plan. The court held that the purpose of section 133(1) is to prohibit the commencement or continuation of any legal proceedings against a company in business rescue. Section 133(1) is not concerned with the development, adoption and implementation of the business rescue plan but rather with the temporary "freezing or stay" of legal proceedings against a company in business rescue.

- Section 133(1)(c) – set-off against any claim made by the company in any legal proceedings.

  In terms of section 133(1)(c), legal proceeding against the company may be proceeded with if it amounts to a set-off against any claim made by the company in any legal proceedings, irrespective of whether the proceedings commenced before or after the commencement of the business rescue proceedings.

- Section 133(1)(d) – criminal proceedings against the company or any of its directors or officers.

[188] (A513/2013) [2015] ZAGPPHC 78 (26 February 2015).
[189] (10862/14) [2015] ZAKZPHC 21 (20 March 2015).
[190] *Idem*, at para 13.
[191] 2014 (6) SA 279 (GJ) (11 July 2014).

- Section 133(1)(e) – proceedings concerning any property or right over which the company exercises the powers of a trustee.

  In *Afrimat Iron Ore Proprietary Limited v Timasani Proprietary Limited (in business rescue) and Another*[192] the court found that the deposit held by the agent of the company in business rescue in respect of a sale, was also held as "trustee" (as interpreted by the court in para 19) and therefore falls within the exception in this subsection. In the case of *Timasani (Pty) Ltd (in business rescue) and Another v Afrimat Iron Ore (Pty) Ltd*[193] the SCA held that the deposit held by an agent of a company in business rescue in respect of a sale was not paid as property in trust, and that the agent was not given any powers of administration typically exercised by a trustee. The powers envisaged by a trustee include taking investment decisions regarding trust assets, advancing trust capital or distributing trust assets to beneficiaries. This section is therefore aimed at companies that hold funds in trust, such as incorporated firms of attorneys, estate agents, professional trustees and financial institutions owing fiduciary duties in terms of the Financial Institutions (Protection of Funds) Act 2001.

- Section 133(1)(f) - proceedings by a regulatory authority in the execution of its duties after written notification to the business rescue practitioner.

  "Regulatory authority" is defined in section 1 of the Companies Act as "an entity established in terms of national or provincial legislation responsible for regulating an industry or sector of an industry".

3.4 An applicant seeking leave under section 133(1)(b)

Should the business rescue practitioner refuse consent in terms of section 133(1)(a), and should none of the other exceptions in terms of section 133(1)(c) to (f) be applicable, then an applicant is obliged to bring an application in terms of section 133(1)(b), seeking the leave of the court to institute proceedings against the company in business rescue.

There are a number of factors that need to be taken into account by an applicant when seeking the leave of the court –

- As set out in *Merchant West Working Capital Solutions (Pty) Ltd v Advanced Technologies and Engineering Company (Pty) Ltd and Another*[194] the court must be presented with a properly motivated application which sets out sufficient detail supporting the need for interference in the business rescue process.

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192 [2019] JOL 41473 (GP), at para 19.
193 [2021] 3 All SA 843 (SCA).
194 13/12406, 10 May 2013 (GSJ).

- The court in the case of *Mabote and Others v Van der Merwe NO and Another*[195] held that an applicant seeking leave under section 133 must establish a *prima facie* case against the company in business rescue.

- In respect of whether leave must be obtained first before the main application is launched, the court in *Booysen v Jonkheer Boerewynmakery (Pty) Ltd (in business rescue) and Another*[196] held that there is no reason why leave to commence or continue with legal proceedings against a company under business rescue must in every case be obtained before the institution of proceedings. In contrast to this view, the court in *Lockstock Investments (Pty) Ltd and Others v Peter van den Steen NO and Others*[197] held that the applicant in such circumstances (where a business rescue plan had been published and substantial progress had been made to implement such plan), must first seek leave from the High Court to commence legal proceedings before the main application can proceed and before the appointed business rescue practitioners will be required to deliver answering affidavits on behalf of the company. The business rescue practitioners would be immensely prejudiced if they were to be expected to file answering affidavits, and incur costs and expenses in the process, in circumstances where the applicants might not even be granted leave by the court to proceed with the main application.

3.5 The effect of the moratorium on sureties and guarantors

Section 133(2) states that a guarantee or surety by a company under business rescue in favour of any other person may not be enforced by any person against the company except with leave of the court and in accordance with any terms the court considers just and equitable in the circumstances. The accessory nature of a suretyship means that a suretyship is dependent on the existence of a valid underlying obligation. The obligation would be "stayed" on the commencement of business rescue proceedings and could not be enforced in terms of section 133(1). Section 133(2) specifically refers to suretyships undertaken by the company in business rescue and not to a suretyship undertaken by a third party in favour of the company in business rescue.

In the case of *Investec v Bruyns*[198] the defendant was sued as surety for the debts of two companies and raised a defence that the statutory moratorium in terms of section 133(1) in favour of the principal debtors (the two companies in business rescue) would preclude the plaintiff from enforcing its claim. The court therefore considered section 133(1) and section 133(2) and held that:

> "Section 133 (1) is a general provision and affords the company protection against legal action on claims in general except, inter alia, with the written consent of the business rescue practitioner or (presumably failing such consent) with the leave of the Court. Section 133 (2) is a special provision dealing

[195] (2015/40324) [2016] ZAGPJHC 185 (8 July 2016).
[196] [2017] 1 All SA 862 (WCC).
[197] Gauteng Local Division, Johannesburg (Case no 2020/12079) Ali AJ (10 August 2021).
[198] 2012 (5) SA 430 (WCC), at para 16.

> specifically with the enforcement of claims against the company based on guarantees and suretyships [by the company], and stipulates that in such cases the claims against the company may be enforced only with the leave of the Court. The business rescue practitioner is not empowered to consent to the enforcement against the company of claims based on guarantees and suretyships. Section 133 (2), as the special provision, would apply to the exclusion of s 133 (1) insofar as claims based on guarantees and suretyships are concerned."

The court found that the statutory moratorium created by section 133(1) is a defence *in personam* (that is, it is available to the principal debtor and not the surety) and would not have the effect of extinguishing or discharging the obligations of the principal debtor. The court stated that, "if the lawmaker intended to prohibit creditors from enforcing their claims against sureties of companies undergoing business rescue proceedings, it would have done so."[199]

This was confirmed in the case of *New Port Finance Company (Pty) Ltd and Another v Nedbank Limited; Mostert and Another v Nedbank Limited*[200] where the court held that the statutory moratorium in favour of the company undergoing business rescue proceedings was a defence *in personam* and therefore that the statutory moratorium in favour of the company did not avail the surety.

Self-Assessment Questions for Chapter 3

Question 1

With reference to the Case Study appearing in the latter part of Chapter 1, answer questions 1.1 to 1.10 by indicating whether the relevant statement is **TRUE** or **FALSE**.

Question 1.1

Fast Flights does not enjoy any protection against legal proceedings being instituted against it despite being in business rescue, with the result that the creditors who have served it with summons and money judgment applications in the Gauteng High Court are entitled to institute and continue with those legal proceedings as if Fast Flights was not in business rescue.

Question 1.2

To enable it to restructure its affairs, Fast Flights does not need any moratorium on the summons and money judgment applications served on it after business rescue.

[199] *Ibid*.
[200] [2015] 2 All SA 1 (SCA).

Question 1.3

As the creditors who served summons and money judgment applications on Fast Flights had not been paid, they were entitled to institute legal proceedings against Fast Flights post-business rescue without obtaining consent from the business rescue practitioner, Mr A Float.

Question 1.4

Because the summons which was served by the lessor of one of the aircraft's hangars was served before Fast Flights was placed in business rescue, that summons is not affected by the moratorium that came into effect when Fast Flights was subsequently placed in business rescue, with the result that the lessor in question is entitled to proceed with that summons until the legal action is finalised, as if Fast Flights was not subsequently placed in business rescue.

Question 1.5

Should the lessor of one of the aircraft's hangars who issued summons before Fast Flights was placed in business rescue wish to continue and proceed with the summons after Fast Flights was placed in business rescue, and should Mr A Float refuse to consent to the continuation of that legal action, then there is nothing that the lessor can do in order to continue or proceed with that legal action.

Question 1.6

Should the lessor of one of the aircraft's hangars who issued summons before Fast Flights was placed in business rescue wish to continue with that summons post-business rescue, it would be legally permissible for the lessor to proceed with that legal action if Mr A Float gives verbal consent to that effect.

Question 1.7

One of Fast Flights' trade creditors that issued statutory letters of demand for payment that was due and payable in respect of aircraft lubricants and parts should urgently issue summons against Fast Flights despite the fact that Fast Flights was subsequently placed in business rescue, because the time limit for the enforcement of such a claim will not be suspended under business rescue even if the enforcement of such a claim was subject to a time limit.

Question 1.8

The lessor who threatened to cancel its lease and instalment sale agreement due to non-payment by Fast Flights would be precluded from cancelling those agreements post-business rescue as a result of the moratorium which is created by Fast Flights' business rescue.

Question 1.9

Had Fast Flights already been in business rescue at the time the letters of demand were issued for payment of the monies which were due and payable for the aircraft lubricants and parts which were supplied in terms of the supply agreements, those letters of demand would have been affected by the moratorium, with the result that the creditor concerned would have been required to first obtain the business rescue practitioner's consent or leave of the court before issuing those letters.

Question 1.10

When Fast Flights was placed in voluntary business rescue on 10 April 2020 by way of a board resolution which was filed with the CIPC, all and any legal proceedings that were instituted before Fast Flights was placed in business rescue were not automatically stayed because the CIPC did not issue a statutory notice confirming that all legal proceedings against Fast Flights have been stayed or prohibited.

Question 2

What is the duration of the moratorium that applies when a company is placed in business rescue?

Question 3

What is the meaning of "legal proceedings" and "enforcement action" envisaged in section 133 of the Companies Act 2008? You answer should address what the Companies Act 2008 and the relevant case law say regarding the meaning of these terms.

Question 4

If the aircraft lessor who threatened to cancel its lease and instalment sale agreement with Fast Flights due to non-payment of rentals and instalment payments respectively, had validly cancelled those agreements before business rescue and instituted legal proceedings after Fast Flights was placed in business rescue for the return of the aircrafts which had been given to Fast Flights pursuant to those agreements, would the moratorium extend to those proceedings and, if so or if not, explain why. Your answer should refer to the relevant and applicable provision(s) of the Companies Act 2008 and case law.

Question 5

Does the Labour Court have jurisdiction over business rescue matters, including employment-related claims which a party may wish to pursue by instituting legal proceedings against a company in business rescue? Substantiate your answer with reference to the relevant case law.

Question 6

The general rule is that the moratorium created by section 133 of the Companies Act 2008 stays or suspends the institution or continuation of legal proceedings. List the exceptions to this general rule where legal proceedings may be instituted or proceeded with despite the company being in business rescue.

Question 7

List the instances where neither the consent of the business rescue practitioner nor the leave of the court is required for purposes of instituting legal proceedings against the company in business rescue.

Question 8

In relation to the summons that was served on Fast Flights before it was placed in business rescue by the lessor of one of the aircraft hangars for payment of the rental owing to the lessor–

Question 8.1

What is the minimum requirement or threshold that the lessor would have to establish in the court application should they seek leave to continue with that summons against Fast Flights after 10 April 2020 (that is, the date on which Fast Flights was placed in business rescue)?

Question 8.2

What factors will the court consider when determining whether or not to grant the leave sought by the lessor?

Question 8.3

Based on the facts of the Case Study, advise whether the lessor is likely to discharge the minimum threshold / requirement referred to in question 8.1 above, and why.

Question 8.4

With reference to the relevant facts of the Case Study and factors to be considered by the court, advise whether you are of the opinion that the court is likely to grant the leave sought by the lessor, and why.

Question 9

With reference to the relevant and applicable provisions of the Companies Act 2008 and relevant case law, advise the CEO of Fast Flights, Mr B Sky, whether he is correct in contending that his obligations under the suretyship he signed for the debts of Fast Flights in the amount of R100 million (in favour of Big Money Bank) are relinquished by virtue of Fast Flights having been placed in business rescue.

For feedback on this self-assessment exercise, see the document "Comment and Feedback on Self-Assessment Questions", which is made available to you as a separate document.

CHAPTER 4

THE STATUS OF PROPERTY INTERESTS IN THE BUSINESS RESCUE PROCESS

4.1 Disposals of property by the business rescue practitioner

One of the fundamental tasks, upon his appointment as the business rescue practitioner of a distressed business, is for the practitioner to identify the assets of the company, the state and value of those assets, the importance of the assets for the ongoing operations of the company and, most importantly, whether or not such assets are subject to the security of any particular creditor of the company.

The importance of this process cannot be understated, as it will fundamentally determine the ultimate success of the business rescue process and whether or not the practitioner is able to present a business rescue plan that is not only effective in terms of securing the successful restructuring of the affairs of the distressed business, but is acceptable to the required majority of the creditors of the company.

The Companies Act 2008 highlights the importance of balancing the rights and interests of all stakeholders affected by the business rescue process.[201] Section 134 is a further example of the need to balance the interests of the company versus the rights of creditors and in particular secured creditors who hold particular assets of the distressed company as security for the indebtedness of the company.

The section is aimed at protecting both the interests of the company and third parties during business rescue. It not only ensures a company's ability to continue to trade whilst it's affairs are being restructured, but also provides the ability for a company to dispose of its property, under particular circumstances, whilst also protecting the rights of creditors who may either own or hold these assets as security.

Section 134 reads as follows:

> "**134. Protection of property interest-** (1) Subject to subsections (2) and (3), during a company's business rescue proceedings-
>
> *(a)* the company made dispose or agreed to dispose of property only-
>
> (i) in the ordinary course of its business;
>
> (ii) in a *bona fide* transaction at arm's length for fair value approved in advance and in writing by the practitioner; or
>
> (iii) in a transaction contemplated within, and undertaken as part of the implementation of a business rescue plan that has been approved in terms of section 152;

[201] Companies Act 2008, s 7(K).

(b) any person who as a result of an agreement made in the ordinary course of the company's business before the business rescue proceedings began, is in lawful position of any property owned by the company may continue to exercise any right in respect of that property as contemplated in that agreement, subject to section 136; and

(c) Despite any provision of an agreement to the contrary, no person may exercise any right in respect of any property in the lawful position of the company, irrespective of whether the property is owned by the company, except to the extent that the practitioner consents in writing.

(2) The practitioner may not unreasonably withhold consent in terms of subsection (1)(c), having regard to –

(i) the purpose of this Chapter;

(ii) the circumstances of the company; and

(iii) the nature of the property, and the rights claimed in respect of it.

(3) If, during a company's business rescue proceedings, the company wishes to dispose of any property over which another person has any security or title interest, that company must-

(a) obtain the prior consent of that other person, unless the proceeds of the disposal would be sufficient to fully discharge the indebtedness protected by that person's security or title interest; and

(b) promptly-

(i) pay to that other person the sale proceeds attributable to that property up to the amount of the company's indebtedness to that person; and

(ii) provide security for the amount of those proceeds the reasonable satisfaction of that other person."

"Property" is not defined in the Companies Act 2008 and must under the circumstances bear its ordinary meaning at common law, representing the sum of all patrimonial rights, for example real rights, personal rights and immaterial property rights.[202] In simple terms, property can best be described as all of the assets, whether movable, immovable or immaterial property of a company.

"Disposal" or "to agree to dispose" is likewise not defined in the Companies Act 2008 and should therefore also bear its ordinary dictionary meaning of selling or agreeing to sell something. When property is disposed of during business rescue, whether the disposal is verbal or in writing, such disposal must meet the clear requirements as set out in section 134.

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[202] Henochsberg 526 (14B).

Section 134 effectively regulates the circumstances under which a practitioner may or may not dispose of any of the assets of a company in business rescue. It provides for three alternative requirements for the disposal of any property of the company, namely-

(1) either in the ordinary course of its business; or

(2) in a *bona fide* transaction at arm's length, for fair value, approved in advance and in writing by the practitioner; or

(3) in a transaction contemplated within, and undertaken as part of the implementation of, a business rescue plan that has been approved in terms of section 152.

The first and the most obvious requirement is that the disposal of the property of the company must be in the ordinary course of the company's business. There is no definition of ordinary course of business in the Companies Act 2008 and it has been suggested[203] that one should seek reference in the definition of ordinary course as found in the Insolvency Act.[204] There is not a finite set of circumstances to consider in assessing whether or not a transaction is in the ordinary course of business.

Applying, as suggested, the general principles as set out in the Insolvency Act and the considerable case law[205] on the subject, the determination of whether a disposal of property, or an agreement for the disposal of such property, is made in the ordinary course of its business should entail a consideration of all the circumstances under which it was made. Such relevant circumstances would depend on the facts of each and every particular case, where the company operates and in particular the kind of business, the customs and practices particular to that type of business, coupled with a decision as to whether the particular disposal, given such circumstances, would have occurred between solvent businessmen and in the context of business rescue, in circumstances where neither of the parties is financially distressed.[206] An example would be where a retail business continues to sell the stock on its shelves to customers.

The second requirement, where a disposal is perhaps not in the ordinary course of business, is that such a disposable must be of a *bona fide* transaction, at arm's length and for fair value. It is submitted that examples of such circumstances would be where so-called non-core assets are identified by the business rescue practitioner for disposal in order to either reduce ongoing operational expenses, or in order to fund the ongoing operations of the business during business rescue or perhaps even fund a proposed compromise with creditors.

Levenstein[207] suggests that the transaction must not be a simulated one and that there should not be a questionable relationship between the company and the other party to the transaction. The purchase price should reflect the fair market value of the property being disposed of as

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[203] Henochsberg 526 (16).
[204] In particular, s 29 of the Insolvency Act when dealing with voidable preferences in insolvent circumstances.
[205] See, eg, *Hendriks NO v Swanepoel* 1962 (4) SA338 (A).
[206] Henochsberg 526 (16).
[207] Levenstein 9-52(2).

between a willing buyer and a willing seller in the relevant circumstances. The only additional requirement under these circumstances is that such disposal has to be approved by the practitioner in writing prior to the disposal. An obvious example would be where a retail business had at some point in time acquired an aircraft. The aircraft is not required for the ongoing operations of the business and may be defined as a non-core asset. Under such circumstances and in terms of these provisions a practitioner will be able to dispose of such an aircraft as long as the disposal meets the requirement of a *bona fide* transaction as defined in the Companies Act 2008. The only additional requirement is that the transaction must have been approved in writing by the practitioner prior to the disposal.

Levenstein further highlights[208] the need for a practitioner to continuously assess whether or not there is a reasonable prospect of the company being rescued.[209] Levenstein submits that in circumstances where no such reasonable prospect exists, it would be improper for the company's practitioner to agree to the disposal of company property to a third party, even if the transaction is at fair value, in the sense that if a winding-up is inevitable, the disposal of assets in these circumstances will result in creditors receiving less of a dividend than they would receive under normal circumstances in the winding-up. In such circumstances, Levenstein submits, it would be difficult to justify any transaction as being *bona fide*.

The final alternative for a practitioner is to dispose of property of the company pursuant to an adopted business rescue plan. An example of the applicability of this alternative would be where a proposed business rescue plan provides for either the orderly disposal of particular assets or business units. Such proposals are often aimed at the alternative definition of a successful business rescue being the delivery of a better alternative to creditors than would otherwise be the result of the immediate liquidation of the company[210]. Such a disposal of defined assets can only be achieved in terms of an adopted business rescue plan.

Of particular importance is that section 134 regulates the specific circumstances where "the company" may dispose of its property. It is submitted that in this context the company is still represented by its duly appointed board of directors, even though the board may under such circumstances be subject to the managerial control of the practitioner,[211] the directors remain responsible[212] for the conclusion of the transactions as contemplated in this section.[213] Although there is no authority on the subject, it is submitted that a transaction concluded by a practitioner, and not by the board of directors, may be subject to scrutiny as the section specifically empowers the company and not the practitioner to dispose of its property.

If the company is in liquidation and there is a subsequent application for business rescue, certain aspects of the liquidation proceedings are suspended. It is submitted that under those circumstances the directors of the company have been divested of their office and employment

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208 *Idem*, at 9-52 (1).
209 As defined in the Companies Act 2008, s 141(2)(a).
210 *Idem*, s 128(1)(b)(iii).
211 *Idem*, s 140(1)(a).
212 *Idem*, s 137.
213 Henochsberg 526(15).

and that the property of the company remains under the custody and control of the provisional or final liquidator, as the case may be, and that under such circumstances the company must be represented by the liquidator when disposing of its assets in terms of section 134.[214]

4.2 The status and protection of security interests and property interests that exist prior to business rescue

Neither the concept of "security interest" nor " property interest" is defined in the Companies Act 2008 and are unfamiliar terms in the South African context. The meaning attributed to these terms in other jurisdictions seems to indicate a close relationship between the terms, but differentiating between them specifically based on whether or not the company in question owns the particular property.[215]

An example of a security interest would be where movable property of a company is either held by way of a lien or a registered (special) notarial bond in favour of a third-party creditor. That third-party creditor would therefore have a security interest in the underlying assets. An example of a title interest would be the interest of a seller of property on credit where ownership has been reserved by that creditor in order to protect itself against losses in the event of default by the purchaser. In such a case the seller's interest in the property is its title, hence the reference to title interest.

Another practical example of a title interest would be where a motor vehicle was financed by a financial institution as an instalment sale agreement in terms of the National Credit Act 2005. In terms of the basic definition of an instalment sale agreement, the ownership of the vehicle would remain with the financial institution, whilst the company has the contractual right to the use and possession of the vehicle during the course of the agreement. Under such circumstances, the financial institution would have a "title interest" in the asset in question whilst in the possession of the company in business rescue.

In the matter of *Energy Drive Systems (Pty) Ltd vs Tin Can Man (Pty) Ltd and Others*[216] the creditor had leased goods to a company, with a clear contractual reservation of ownership. The company subsequently filed for business rescue and an adopted business rescue plan provided for the disposal of all of the business of the company, including the leased property subject to the creditors clear reservation of ownership. In ordering the return of the property, the court found that the creditor had a clear title interest as provided for in section 134, and that the practitioner could not dispose of the property without the consent of a party holding such title interest.

Section 134(1)(b) confirms the right of any person who is in lawful possession of any property of a company in business rescue, pursuant to an agreement made in the ordinary course of the company's business prior to the commencement of business rescue proceedings, may continue to exercise such rights in respect of that property as contemplated in the agreement. The section

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[214] *Ibid*.
[215] *Idem*, 526(19).
[216] 2017 (3) SA 539 GJ.

is specifically made subject to the provisions of section 136, which seems to indicate that the business rescue practitioner remains able to either partially or entirely suspend obligations relating to the particular agreement. It is submitted that although the practitioner will be able to suspend obligations of the company, they will not be in a position to insist on the return of the particular assets, which may remain in the lawful possession of the other party for the duration of business rescue proceedings.

Section 134(1)(c) prohibits the exercise of any right by a person in respect of property in the lawful possession of the company, except to the extent that the business rescue practitioner consents in writing. However, if the company is not in lawful possession of the property, for example because those rights were based on a contract that has validly been cancelled, this section does not apply.[217] A prime example that business rescue practitioners in practice are often confronted with, is where creditors supply product on credit subject to a reservation of ownership. Often upon the commencement of business rescue proceedings, creditors would insist on the return of the assets in question based on the contractual reservation of ownership. In such circumstances the practitioner is not obliged to immediately return the unpaid assets subject to the particular creditors "title interest ", but rather to reasonably assess whether or not the retention of these items would be beneficial to the overall restructuring of the company whilst also taking into consideration the value of the assets in question and how any disposal of such assets would affect the "title interest " of the owner of those goods.

It is commonplace for parties to include provisions in their agreements that seek to elevate the right of either of the contracting parties in the event of one or either of them filing for business rescue, liquidation or even just committing an act of insolvency . One such standard clause is where the mere filing for rescue requires the company, without having breached or defaulted on the agreement, to return property to its owner. Despite such provisions in any agreement, no person may exercise any right in respect of any property in the lawful possession of the company, irrespective of whether the property is owned by the company, except to the extent that the business rescue practitioner consents in writing, rendering such standard clauses in agreements *pro non scripto*.

In *Cloete Murray and Another NNO vs FirstRand Bank t/a Wesbank*[218] the liquidators sought to set aside the earlier actions of the practitioner who had returned, and seemingly consented to, the disposal by the secured of property of the company when it was still subject to business rescue proceedings. Although many aspects were traversed in the judgement, it ultimately came down to an assessment of the requirement for such consent to be in writing and the effect on such consent of it was not in writing. The court accepted that the consent of the practitioner was not in writing, but regarded such requirement as peremptory rather than directory and such consent should be regarded as a nullity, simply because it was not in writing.

In balancing the rights of all affected parties, the practitioner may not unreasonably withhold such consent having regard to the overall purpose of Chapter 6, the circumstances of the

[217] Henochsberg 526(17) and *Cloete Murray and Another NNO vs FirstRand Bank t/a Wesbank* 2015 (3) SA 438 at para 24.

[218] 2015 (3) SA 438, at para 24.

company, the nature of the property and the rights claimed in respect of it.[219] Again, the practitioner is required to balance the rights of the company on the one hand and its ability to continue to conduct its business, weighed against the contractual rights of a third party.

Unlike initially suggested, the purpose of section 134(3) is not aimed at the destruction or dilution of the rights of secured creditors. The protected and privileged status of the secured creditor remains consistent with the common law as it existed before the introduction of business rescue, and has not interfered with the common law principle as it relates to secured rights. It simply ensures that the business rescue process does not dilute or diminish it.[220]

Ultimately, subsection 3 of section 134 protects the holder of either a security or title interest, as it requires the practitioner to obtain its express consent before disposing of the property subject to either its "security" or "title interest". The section not only seeks to regulate the requirements for consent, but also to protect such a secured creditor from any potential prejudice that may flow from the actions taken by the company or the business rescue practitioner during the course of business rescue proceedings.[221]

The requirement for consent is not absolute in the event that the proceeds of the disposal would be sufficient to fully discharge the indebtedness of the secured creditor. In such circumstances the business rescue practitioner would be able to dispose of the property, but is required to promptly pay to the secured creditor the sale proceeds attributable to that property up to the amount of the company's indebtedness to that creditor, or provide security for the amount of such proceeds to the reasonable satisfaction of the creditor in question.[222] There must be prompt payment of the proceeds of the disposition and the payment must fully discharge the indebtedness of the company. In the matter of *Louis Pasteur Holding (Pty) Ltd and Others v Absa Bank Ltd and Others*[223] the SCA held that periodic payments that may eventually discharge the indebtedness do not comply with this requirement. This matter related to the contentious business rescue of MECI, the owner of a well-known landmark building in the centre of Johannesburg. It was common cause that the only source of income for MECI was its rental income, which had been ceded to ABSA Bank as security for MECI's indebtedness. Louis Pasteur, as an affected party, was seeking an order preventing the liquidation of MECI based on the proposition that MECI be allowed to utilise its rental income to fund its ongoing operations and only pay to ABSA the excess income. ABSA did not consent to such utilisation and the question the court was left with was whether a business rescue practitioner would be entitled to utilise the rental income if such income was sufficient to fully discharge the indebtedness of MECI to ABSA over time, and found that the periodic payments as proposed simply did not satisfy the requirement of prompt payment of the proceeds of the disposition to the secured creditor.[224]

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[219] Companies Act 2008, s 134(2).
[220] Henochsberg 526 (18).
[221] *Idem*, 526 (20).
[222] Companies Act 2008, s 134(a) and (b).
[223] 2019 (3) SA 97 (SCA).
[224] *Idem*, at para 11.

It is submitted that a general notarial bond confers neither a title interest nor a security interest to its beneficiary. In order for the rights of a holder of a general notarial bond to be elevated to that of a secured creditor, the creditor must have taken possession of the assets subject to the general notarial bond either voluntarily with the consent of the company, or by obtaining an order from a competent court in order to take possession of the assets in question, prior to the commencement of business rescue.[225] The holder of a general notarial bond would be prohibited from seeking the perfection of the general notarial bond post the adoption of a business resolution without the express consent of the practitioner, as such an application is considered to be an "enforcement action" as defined in the Companies Act 2008.[226]

One of the questions that has often been considered, is whether section 134(3) prohibits the practitioner from utilising the debtors (book debts) of the company as working capital during the business rescue proceedings without the consent of the holder of the session of such debtors. Our courts have held[227] that where the rental stream of a company had been ceded to the bank, out-and-out, the practitioner could not utilise the proceeds of such collection as the revenue simply did not belong to the company, the ownership thereof having passed to the bank in question upon the cession thereof. In such circumstances, the collection of the rental would not be considered an "enforcement action"[228] as the particular rental stream belonged to the bank.

However, where the debtors (book debts) of a company have been ceded to a bank as security *in securitatem debiti*, the debtors in question remain the property of the company. Whether the utilisation of the debtors book as working capital for the company would constitute "disposal" of the company's property has also been called into question. The definition of "disposal" in our law is "to transfer", "to part with" or alienate in some manner or form.[229] Whether the use by the company of the proceeds of the debtors book would constitute an effective "disposal", which would require the bank's consent as required in terms of section 134(3) was, according to Levenstein, initially debatable.[230]

The debate has now clearly been settled by our courts,[231] having found that when a creditor holds security over a debtor's property, in most instances the company's debtors (book debts), the business rescue practitioner cannot dispose of or use such encumbered property without the secured creditor's consent, unless he of course first discharges the company's entire secured debt in favour of the creditor as envisaged in terms of section 134(3).

The earliest authority on this particular subject is *Kritzinger and Another v Standard Bank of South Africa Ltd*.[232] In this matter the practitioner wilfully refused to remit to Standard Bank, the secured creditor by way of a cession of debtors, the proceeds of payments received form the debtors of

[225] A so-called "perfection application".
[226] Companies Act 2008, s 133(1).
[227] *Gromley v West City Precinct Properties (Pty) Ltd* 2013 JDR 1895 (WCC).
[228] As contemplated in the Companies Act 2008, s 133.
[229] Levenstein 9-56.
[230] *Ibid*.
[231] *Kritzinger and Another v Standard Bank of South Africa Ltd* (3034/2013) [2013] ZAFSHC 215.
[232] *Ibid*.

the company in business rescue, but rather transferred such proceeds to another bank account where the funds were utilised to fund the ongoing operations of the company. The Bank contended that they held a security interest in respect of the property and that the business rescue practitioner could not dispose of the proceeds without their consent. The business rescue practitioner on the other hand contended, *inter alia*, that the bank could not "call on its security" under circumstances where the company was not in default of its underlying agreement with the bank. The court found that the book debts of the company could not be treated as the exclusive property of the company any longer and, since the company had ceded its debtors book to the respondent, such book debts now constituted the bank's outright collateral[233] and that the commencement of business rescue proceedings did not and could not demote the bank of its rightful position as a secured creditor.[234]

A full bench of the South Gauteng High Court, in the matter of *Van den Heever NO and Others v Van Tonder*[235] confirmed that for purposes of section 134, a cession of book debts ceded as security, constitutes "property" that may not be disposed of without the cessionary's consent. In this matter the joint liquidators sought compensation form the erstwhile business rescue practitioner following his utilisation of the proceeds of ceded book debts to fund the ongoing operations of the company in disregard of the secured creditors express demand that the proceeds of all debtors be paid to them. The practitioner submitted that section 134 had no application as a cession of book debts neither constituted "property" as contemplated in the section, nor did the collection and application of the book debt by the company constitute a disposal. The full bench in its judgement laid to rest the contention in finding that book debts constitute "property" for purposes of section 134 and that "disposal" in the context of section 134 purposefully also means "to deal with or settle", "to give", "sell" or transfer to another".[236]

Our courts have further held that security attached to an asset prior to business rescue proceedings is not affected by the post-commencement finance provisions as set out in section 135,[237] as section 135 can only apply to security given to a creditor whose debt arose after the commencement of business rescue proceedings. In *National Union of Metalworkers of SA v VR Laser Services (Pty) Ltd*[238] the court went on to state that business rescue practitioners do not have the authority to elevate post-commencement finance claims above those of secured creditors without an express waiver of the security by the particular creditor, and in doing so the court upheld, in no uncertain terms, that a creditor's security, obtained prior to the commencement of business rescue proceedings, is not to be diluted or diminished post-business rescue without the secured creditor's express consent or without the secured debt being liquidated.

[233] *Idem*, at para 49.
[234] *Idem*, at para 54.
[235] *Van den Heever NO and Others v Van Tonder* 2021 ZAGPJHC 486.
[236] *Idem*, at para 44.
[237] [2020] 2 All SA 536 (GJ).
[238] *Ibid*.

In *Redpath Mining South Africa (Pty) Ltd v Marsden NO and Others*[239] an adopted business rescue plan sought to reduce the benefit Redpath, as a secured creditor, would receive from the proceeds of the sale of the assets subject to its (albeit disputed) security, in favour of other creditors. Redpath, aggrieved by this, approached the court seeking the setting aside of the adopted business rescue plan. Ultimately, other aspects of the application led to the court refusing the relief sought, but in doing so the court seemingly left the door open for a situation where the need to implement an adopted business rescue plan, adopted by the majority of creditors, outweighs the rights of a minority, albeit a secured creditor. It is submitted that this aspect of the *Redpath* judgement is incorrect when considered against the application of the principles of the impenetrable rights of secured creditors as now firmly confirmed by our courts.

Considering the clear provisions of section 134 and the now considerable case law on the various aspects of this particular section, it is clear that if a company wishes to dispose of any property during its business rescue proceedings, which is subject to either the security or title interest of another person, the company must first obtain the prior consent of the holder of the security interest, unless the proceeds of the disposal is sufficient to fully discharge the indebtedness protected by that person's security or title interest, and promptly pay to such holder of the security or title interest the proceeds of the sale of that property, up to the amount of the company's indebtedness to that person, or alternatively provide security for the amount of those proceeds to the reasonable satisfaction of the security or title interest holder.

Self-Assessment Questions for Chapter 4

Where necessary, refer to the Case Study contained in Chapter 1 of these notes in order to answer the questions below.

Question 1

Indicate whether the following statements are **TRUE** or **FALSE**. Provide reasons for your answer.

Question 1.1

"Disposal" as defined in section 134 of the Companies Act 2008 simply means to sell any assets of the company in business rescue.

Question 1.2

Considering the general moratorium on enforcement actions, a business rescue practitioner is not obliged to give reasons for refusing to give permission for an affected party to take possession of their own assets.

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[239] 2013 ZAGPJHC 148.

Question 1.3

If a business rescue practitioner *bona fide* consents to the disposal of an asset of the company for value in an arm's length transaction, but does not do so in writing, such agreement is considered void.

Question 1.4

Section 134 of the Companies Act 2008 has not changed the common law rights of secured creditors.

Question 2

In addition to the registration of an aircraft security mortgage bond, Big Money Bank insisted on a cession, *in securitatem debiti*, of the shares and the loan account of Fast Flights in its newly acquired catering company. The business rescue practitioner has identified the potential sale of this catering company as a source of emergency funding in order to finance the ongoing operational expenses of Fast Flights during business rescue proceedings. Briefly describe the options available to the business rescue practitioner and what would be the requirements for the practitioner to enter into such a disposal.

Question 3

Pickled Plum, one of Fast Flights' jet fuel suppliers, had four months prior to the commencement of business rescue proceedings insisted on additional security for an extended line of credit. Fast Flights agreed and a general notarial bond was registered over all the movable assets of Fast Flights.

Briefly discuss:

(a) the security interest, if any, of Pickled Plum; and

(b) the requirements, if any, if the practitioner wishes to continue to utilise these assets or any proceeds derived from these assets during business rescue proceedings.

Question 4

Easy Seats had supplied Fast Flights with specially branded seats to be used on their five newly acquired aircraft. Fast Flights could not afford the initial additional capital required for these custom-made seats and it was agreed with Easy Seats that the purchase price would be paid over a period of 36 months in equal instalments, and that the ownership of these easily identifiable seats would remain with Easy Seats until such time as the purchase price had been settled in full.

At the commencement of business rescue, Fast Flights were not in arrears with the payment of these agreed monthly instalments, but Easy Seats is not convinced that Fast Flights will be able to continue to honour their contractual commitments in this regard. Briefly discuss and describe Easy Seats' interest in the business rescue and whether or not they would be entitled to insist on the immediate return of the property.

For feedback on this self-assessment exercise, see the document "Comment and Feedback on Self-Assessment Questions", which is made available to you as a separate document.

CHAPTER 5

POST-COMMENCEMENT FINANCE (PCF)

5.1 Introduction

Post commencement finance may be obtained by a company in order to assist its business rescue practitioners in managing the company in business rescue out of its financial distress.[240] In other words, post commencement finance is needed more often than not to keep the wheels turning and is critical to achieving either one of the two objectives of business rescue proceedings: (1) to return a financially distressed company to solvency on a going concern basis, or (2) to achieve a better return for creditors than they would have received in the company's immediate liquidation.

Section 135 of the Companies Act 2008 attempts to set out the order in which the claims of creditors (particularly creditors with post commencement finance claims) rank during business rescue. In terms of this section, post commencement financiers are preferred in the order of preference created by the Companies Act 2008. It states:

> "(1) To the extent that any remuneration, reimbursement for expenses or other amount of money relating to employment becomes due and payable by a company to an employee during the company's business rescue proceedings, but is not paid to the employee-
>
> (a) the money is regarded to be post commencement financing; and
>
> (b) will be paid in the order of preference set out in subsection (3)(a).
>
> (2) During its business rescue proceedings, the company may obtain financing other than as contemplated is subsection (1), and any such financing-
>
> (a) may be secured to the lender by utilising any asset of the company to the extent that it is not otherwise encumbered; and
>
> (b) will be paid in the order of preference set out in subsection (3)(b).
>
> (3) After payment of the practitioner's remuneration and expenses referred to in section 143, and other claims arising out of the costs of the business rescue proceedings, all claims contemplated -
>
> (a) in subsection (1) will be treated equally, but will have preference over-
>
> (i) all claims contemplated in subsection (2), irrespective of whether or not they are secured; and
>
> (ii) all unsecured claims against the company; or
>
> (b) in subsection (2) will have preference in the order in which they were incurred over all unsecured claims against the company.
>
> (4) If business rescue proceedings are superseded by a liquidation order, the preference conferred in terms of this section will remain in force, except to the extent of any claims arising out of the costs of liquidation."

[240] *The South African Property Owners Association v Minister of Trade and Industry and Others* 2018 (2) SA 523 (GP) (29 November 2016).

There are anomalies that may arise on interpreting this section in practical situations. As such, there has been much legal debate around the ranking of creditors' claims or the so-called "payment waterfall" in business rescue proceedings as envisaged in section 135.

How to identify whether or not a creditor is a post commencement financier, how that creditor ranks both in business rescue proceedings in any subsequent liquidation proceedings are clarified below with reference, where applicable, to case law.

5.2 The who, what, when and how of post-commencement claims

5.2.1 Trade creditors

For creditors who provide goods or services post the commencement of business rescue proceedings under an agreement that was concluded prior to the commencement of these proceedings, the judgment by the High Court of the Gauteng Division, Pretoria in the case of *The South African Property Owners Association v Minister of Trade and Industry and Others*[241] (the *SAPOA* judgment) is instructive as it has settled the ranking of those creditors.

During November 2016, Van der Westhuizen AJ of the High Court, Gauteng Division, Pretoria handed down the *SAPOA* judgment, wherein the applicant, the South African Property Owners Association, sought a declaratory order that the rights of a landlord in respect of rental and other services (such as electricity, water, sanitation and sewerage charges and payments to other service providers disbursed by the landlord) in respect of a property leased by a company in business rescue, fell within the ambit of either post commencement financing in terms of section 135(2) of the Companies Act 2008 or as costs arising out of the business rescue proceedings in terms of section 135(3) of the Companies Act 2008.

It is important to note that section 135(2) of the Companies Act 2008 provides that during a company's business rescue proceedings "the company may **obtain financing** other than as contemplated is subsection (1), and any such financing – …(b) will be paid **in the order** of preference set out in subsection (3)(b)…".

Van der Westhuizen AJ essentially held that:

> "In my opinion, and applying the principles of interpretation, the financing intended in subsection (2) of section 135 of the Act relates to **the obtaining of financing in order to assist in managing the company out of its financial distress**, hence the provision that any asset of the company may be utilised to secure that financing to the extent that the asset is not otherwise encumbered. **It does not lean to an interpretation that encompasses existing obligations, other than to company employees, of the company that are utilised to assist in managing the company during the business rescue proceedings**. Further in this

[241] 2018 (2) SA 523 (GP) (29 November 2016).

> regard, sections 133 and 136(2) of the Act mitigate against such interpretation." (emphasis added)

Van der Westhuizen AJ further held that the costs relating to the lease agreement are a direct result of the terms of the lease agreement and that those costs cannot constitute post commencement financing or costs classified as costs occasioned by the business rescue proceedings. If that were the case, a lessor would enjoy a preference over other creditors which would defeat the purpose or aim of the business rescue proceedings.

Accordingly, any costs or liability that arise out of an agreement that was concluded prior to business rescue proceedings, and which were incurred during business rescue proceedings, will not constitute "post commencement financing" or "costs arising out of the costs of business rescue proceedings".

Such costs and / or liabilities, unless already secured, will merely form the subject of an unsecured (concurrent) claim against the company in business rescue and will not enjoy any preference above other creditors. Business rescue practitioners who intend returning the company in business rescue to solvency through implementation of the business rescue plan should, however, have regard to section 154 of the Companies Act.

5.2.2 Post-commencement funders

A company in business rescue may obtain financing in order to assist in managing the company out of its financial distress (having regard to the *SAPOA* judgment), and any such financing will be paid in the order of preference set out in subsection (3)(b). Such financing may include trade creditors who have concluded agreements after the commencement of business rescue for the provision of goods and services on credit to the company in business rescue.

Such post commencement finance may be secured to the financier by utilising any asset of the company to the extent that it is not otherwise encumbered.

5.2.3 Employees

Section 144(2) provides that to the extent that any unpaid remuneration, reimbursement for expenses of other amount of money relating to employment that became due prior to the commencement of business rescue, the employee is a preferred unsecured creditor of the company.

However, to the extent that any remuneration, reimbursement for expenses or other amount of money relating to employment becomes due and payable by a company to an employee during the company's business rescue proceedings, but is not paid to the employee, it is clear from section 135(1) that the employee in question will be a post commencement financier.

5.2.4 Business rescue practitioner's remuneration and expenses

The practitioner's remuneration and expenses referred to in section 143 of the Companies Act 2008 will be paid, in a business rescue, before the post commencement finance claims contemplated in section 134(1) and 135(2) are paid.

5.2.5 Secured creditors

Section 134(3) of the Companies Act 2008 provides:

> "(3) If, during a company's business rescue proceedings, the company wishes to dispose of any property over which another person has any security or title interest, the company must-
>
> (a) obtain the prior consent of that other person, unless the proceeds of the disposal would be sufficient to fully discharge the indebtedness protected by that person's security or title interest; and
>
> (b) promptly-
>
> (i) pay to that other person the sale proceeds attributable to that property up to the amount of the company's indebtedness to that other person; or
>
> (ii) provide security for the amount of those proceeds, to the reasonable satisfaction of that other person."

In the circumstances, a secured creditor, whether as a pre-commencement of post commencement financier, will enjoy the protection afforded by this section.

However, it should be noted that where a pre-commencement creditor holds security and that creditor's claim is either compromised in terms of section 154(1) or becomes unenforceable under section 154(2),[242] the security, unless disposed of in the business rescue proceedings under section 134(3), may have to be released unless the business rescue plan provides otherwise.

A post commencement financier that holds security over the assets of a company in business rescue will retain that security even after an approved business rescue plan has been implemented.

5.3 Ranking of section 135 claims in a liquidation

In addition to the *SAPOA* judgement, the Supreme Court of Appeal, in *Diener NO v Minister of Justice and Others*,[243] and the Constitutional Court thereafter in the case of *Diener NO v Minister*

[242] *Van Zyl v Auto Commodities (Pty) Ltd* (279/2020) [2021] ZASCA 67; [2021] 3 All SA 395 (SCA); 2021 (5) SA 171 (SCA) (3 June 2021).

[243] 2018 (2) SA 399 (SCA).

of Justice and Correctional Services and Others[244] (the *Diener* judgments), had regard to the ranking of business rescue practitioners' fees in an instance where business rescue proceedings had been converted into liquidation proceedings. By extrapolation, this judgment is equally important on the ranking of creditors' claims in instances where business rescue proceedings fail and where the liquidators may be faced with a significant bill from the business rescue practitioner(s) for their fees.

In this case, shortly after the applicant, one Diener, was appointed as the business rescue practitioner of JD Bester Labour Brokers CC, Diener instructed certain attorneys to institute an application in terms of section 141(2)(a) of the Companies Act 2008 to convert the business rescue proceedings into liquidation proceedings on the basis that Diener was of the view that the company could not be rescued.

An order for liquidation of the company was granted. Diener sought a preference for payment of his fees and submitted a claim to the joint liquidators of the company. Diener argued that the claim for remuneration by a practitioner was not a concurrent claim, but a special class of claim created by section 135 of the Companies Act 2008, and that it enjoyed "a special and novel preference" and granted the practitioner "security over all assets, even above securities existing when the practitioner takes office".

It is important to remember that section 135(4) of the Companies Act 2008 provides that "[i]f business rescue proceedings are superseded by a liquidation order, the preference conferred in terms of this section will remain in force, **except to the extent of any claims arising out of the costs of liquidation**" (own emphasis).

The Supreme Court of Appeal held:

> "[45] This leads me to the place of the preference created by s135(4) **in the broader scheme of the Insolvency Act**. Section 135(4) contains a strong indication when it provides that the claims that it deals with rank after the costs of sequestration.
> [46] **Section 96 of the Insolvency Act** provides that the first call on the free residue of an insolvent estate – that 'portion of the estate which is not subject to any right of preference by reason of any special mortgage, legal hypothec, pledge or right of retention' – is in respect of funeral expenses and death bed expenses of the insolvent and his or her family. **This is followed, in s97, by the costs of sequestration**.
> …
> [49] For these reasons, I conclude that s135(4) and s143(5), whether taken individually or in tandem, do not create the 'super-preference' contended for on behalf of Diener. **Section 135(4) provides to the BRP, after the conversion of business rescue proceedings into liquidation proceedings, no more than a preference in respect of his or her remuneration to claim against the free**

[244] 2019 (2) BCLR 214 (CC).

> **residue after the costs of liquidation but before claims of employees for post commencement wages**, of those who have provided other post commencement finance, whether those claims were secured or not, and of *any other* unsecured creditors" (own emphasis).

The Constitutional Court concluded at paragraph 71 that there is no "…basis on which to interfere with the order of the Supreme Court of Appeal".

By extrapolation, in a liquidation, the following ranking should be applied:

(1) Proceeds from the sale of the **encumbered assets** –

- Section 89 of the Insolvency Act – Payment of the cost of maintaining, conserving, and realising any property. In this regard, the realisation costs include, in terms of this section, "[t]he trustee's remuneration in respect of any such property and a proportionate share of the costs incurred by the trustee in giving security for his proper administration of the estate, calculated on the proceeds of the sale of the property, a proportionate share of the Master's fees, and if the property is immovable, any [property] tax [and penalties thereon]"; and

- Section 95(1) of the Insolvency Act – Payment of secured creditors.

(2) Proceeds from the sale of the **unencumbered assets** –

- Section 97 of the Insolvency Act, read with s135(4) of Companies Act 2008 – Payment of the costs of liquidation;

- Section 135(3) and (4) of the Companies Act 2008, read with the *Diener* judgments:

    - Payment of the business rescue practitioner's remuneration and expenses, and other claims arising out of the costs of the business rescue;

    - Payment of any remuneration, reimbursement for expenses or other amount of money relating to employment that becomes due and payable by a company to an employee during the company's business rescue proceedings (in terms of section 135(1)); and

    - Payment of unsecured post commencement financiers (in terms of section 135(2));

(3) Section 98 of the Insolvency Act – Payment of the costs of execution;

(4) Section 98A of the Insolvency Act – Payment of salaries or wages of former employees of the company, subject to the limits described in this section. It is worth pointing out that this section would only become applicable if salaries and wages became payable prior to the

commencement of business rescue proceedings, failing which it will fall under section 135(3) of the Companies Act 2008, as described aforesaid;

(5) Section 99 of the Insolvency Act – Payment of statutory obligations (for example Workmen's Compensation, taxes, Unemployment Insurance Fund, etcetera);

(6) Section 101 of the Insolvency Act – Payment of taxes on persons or the incomes or profits of persons per any Act of Parliament;

(7) Section 102 of the Insolvency Act – Payment of unperfected general notarial bonds; and

(8) Section 103 of the Insolvency Act, read with the *SAPOA* judgment – Payment of concurrent creditors, including those concurrent creditors who provide services and supply goods after the commencement of business rescue proceedings under an agreement that was concluded prior to the commencement of business rescue proceedings and from whom the company did not "obtain financing" in terms of section 135(2) of the Companies Act 2008.

5.4 Conclusion

The *SAPOA* and *Diener* judgments clarify the following:

(1) Any costs and / or liability incurred by a creditor during business rescue pursuant to an agreement concluded prior to business rescue will simply be a concurrent claim during business rescue. Such a creditor will not enjoy any preference as set out in section 135 of the Companies Act 2008 unless the creditor concludes a new agreement or an addendum to its current agreement which provides that any services provided during business rescue will enjoy a preference during business rescue. Business rescue practitioners should only enter into such arrangements if they are of the view that the contract and the service provided by the creditor is essential to the successful rescue of the company; and

(2) Claims under section 135 of the Companies Act 2008 will have to be proved like any other claim in terms of section 44 of the Insolvency Act, and will not enjoy any preference over secured claims in liquidation. However, such claims will rank after the costs of liquidation but before other preferent creditors and concurrent creditors.

Self-Assessment Questions for Chapter 5

Where necessary, refer to the Case Study in Chapter 1 of these notes when answering the questions below.

Question 1

Fast Flights has a large staff complement, which includes pilots, cabin crew, engineers, maintenance and service support personnel, as well as financial and general support staff. A vast majority of Fast Flights' employees are represented by Fair-Labour-For-All, a South African registered trade union that seeks to advance the interests of employees engaged in the aviation industry.

How will the claims of the Fast Flights staff, both pre-business rescue and during the business rescue process be treated in the business rescue plan and a liquidation, respectively?

Question 2

In terms of section 13 of the Labour Relations Act 1995, certain of Fast Flight's employees of Fair-Labour-For-All, a representative trade union, have authorised Fast Flights in writing to deduct subscriptions and levies payable to that trade union from their wages. However, before Fast Flights entered business rescue it withheld not only payments of PAYE to SARS, but also the subscriptions and levies to Fair-Labour-For-All.

How will the claims of SARS and Fair-Labour-For-All be treated in the business rescue plan and a liquidation, respectively?

Question 3

When Fast Flights expanded its operations in 2019 by acquiring an airline catering company and five aircraft, substantial financing was required. These and other assets were secured in favour of Fast Flights' financiers. However, these financiers are not willing to provide post-commencement financing in the course of Fast Flights' business rescue proceedings.

The business rescue practitioner intends to sell these assets. How will the claims of these financiers be treated in the business rescue plan?

Question 4

When Fast Flights entered business rescue, the aircraft lessors claimed that the continued possession and use of the aircraft during the business rescue proceedings constitutes post-commencement finance.

While the business rescue practitioners suspended the rental payments that would become due during business rescue proceedings for some of the aircraft, and negotiated reduced rentals with certain of the aircraft lessors for the continued use of some of the aircraft, the business rescue practitioners were unwilling to take a firm position in respect of the others even though the aircraft were being flown.

How would the various categories of aircraft lessors' claims be treated in the business rescue plan?

For feedback on this self-assessment exercise, see the document "Comment and Feedback on Self-Assessment Questions", which is made available to you as a separate document.

CHAPTER 6

EFFECT OF BUSINESS RESCUE ON EMPLOYEES AND CONTRACTS

6.1 Status of employees when business rescue proceedings commence

Employees are defined as "affected persons" in terms of the Companies Act 2008[245] and very importantly, the status and rights of employees, including the ranking of employee claims, are specifically provided for during business rescue proceedings.

Section 136 of the Companies Act 2008 provides for the effect that business rescue proceedings have on employees and more specifically their contracts of employment, and in doing so the legislature has codified such effects, in terms of an employee's status.

The status of employees is paramount during business rescue proceedings and by its very nature business rescue is designed and intended to prevent the loss of jobs within financially distressed companies. The mechanisms within Chapter 6 of the Companies Act 2008 are specifically designed with the intention to preserve ongoing employment and provide opportunities for further and future employment, as part and parcel of an adopted business rescue plan.

Section 7 of the Companies Act 2008 provides for the purpose of the Act and more specifically in section 7(K), it provides specifically for the efficient rescue and recovery of financially distressed companies, in a manner that balances the rights and interests of all relevant stakeholders. Employees and their representative unions or representatives are significant stakeholders in the efficient restructuring of a business' affairs, especially within the context of business rescue proceedings and accordingly the status of employees is elevated within a business rescue context.

The provisions of the Companies Act 2008 (and more specifically in section 136(1)(a) and 136(1)(b) thereof) deals specifically with the status of employees within the context of their contracts of employment. It provides that despite any provision of any agreement to the contrary, during a company's business rescue proceedings employees of a company, immediately before the beginning of those proceedings, continue to be so employed on the same terms and conditions, except to the extent that changes occur in the ordinary course of attrition; or the employees and the company, in accordance with the applicable labour laws, agreed different terms and conditions with the company; and any retrenchments of any such employees contemplated in the company's business rescue plan is subject to section 189 and 189A of the Labour Relations Act 1995,[246] and other applicable employment related legislation.

It is noteworthy that section 136 of the Companies Act 2008 deals more specifically with the effect that business rescue has on an employee's contract of employment and further deals with the regulation of the position of the company in respect of its obligations in terms of existing

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[245] Companies Act 2008, s 128 (1)(a).

[246] Hereinafter referred to as the Labour Relations Act.

contracts, rather than the employees themselves.[247] It is however clear from the provisions of the Companies Act 2008 that the status of an employee at the commencement of business rescue proceedings is not negatively affected, both from a contractual and from a statutory perspective, with the rights of employees effectively being entrenched in statue.[248]

The contractual rights of an employee that exist as at the commencement date of business rescue proceedings remains enforceable by the employee as against the company and *vice versa* for the company in relation to the employee, for the period of business rescue, subject only to the provisions of all applicable labour legislation, which may include the Labour Relations Act, Basic Conditions of Employment Act 1997[249] and all relevant regulations to such applicable legislation.

Of importance for a financially distressed company, is that employees are also required to adhere to their obligations in providing services to the company in rescue, in accordance with such employee's contractual obligations to do so. If anything, an employee's obligations to assist the company through its financial distress is significant if the restructuring of the company's affairs is to be successful. Considering that a major portion of any business's intellectual property is attributed to its employees, this aspect of any successful restructuring of a financially distressed company cannot be over emphasised and the status of employees becomes directly attributable to a successful business rescue process.

The status of employees is further codified and catered for in the Companies Act 2008 *vis-a-vis* the ranking of employees' claims within a business rescue process as well as prior to a business rescue process, and in doing so the status of employees' claims within a business rescue context is clarified.[250] Employee claims are catered for in the Companies Act 2008 from both a pre-and post-commencement of business rescue perspective, with specific provision being made for the ranking of such claims in respect of both scenarios. Employees enjoy a super preference claim in terms of section 135, and preference is given to claims of employees for pre-business rescue amounts that have not been paid to such employees, as at the commencement of business rescue proceedings.

Employees are also entitled and are encouraged to participate in the business rescue proceedings, with specific statutory engagements envisaged between the business rescue practitioner, the employees and any registered trade union or employee representative, that include rights to participate in the development of the proposed business rescue plan and ongoing engagements with the business rescue practitioner during proceedings.

Prior to the introduction of Chapter 6, the status of an employee's contract of employment was most often affected within the context of the liquidation of a company. Juxtaposed to the preferable position catered for in business rescue provisions of the Companies Act 2008, once a company has been liquidated, employees' contracts of employment are suspended and

[247] See Henochsberg 526(27).
[248] Companies Act 2008, s 144.
[249] Hereinafter referred to as the Basic Conditions of Employment Act.
[250] Companies Act 2008, ss 144 and 135.

terminate with the effluxion of time and by operation of law.[251] Employees also only enjoy a limited preference in terms of their preference claims within a liquidation scenario, with the balance of their claims ranking as concurrent claims. It is therefore clear that the business rescue provisions with regards to the status of an employee's contract of employment, ranking of claims and participation rights, are significantly preferable to the effect that a liquidation has on the status of an employee and their contract of employment.

6.2 Rights of employees during business rescue proceedings

The rights of employees are specifically catered for in Chapter 6. Section 135(1) of the Companies Act 2008 deals with remuneration, reimbursement for expenses and / or other amounts of money relating to employment that become due and payable by a company to an employee during the company's business rescue proceedings.

These amounts are regarded as post-commencement financing and are paid in the order of preference set out in subsection (3)(a). Any post-commencement claims in relation to employees are dealt with in terms of section 135(1), and such claims enjoy a preference over all other post-commencement finance claims incurred during proceedings, irrespective of whether these are secured or unsecured claims against the company. By creating a preference for employees in terms of the Companies Act 2008, the legislature has ensured that a business rescue process is far more beneficial and preferable for an employee as opposed to a liquidation process.[252] Of importance is that any preference created during business rescue proceedings in favour of employees will continue to apply if the company is liquidated post the termination of a business rescue process.[253] This is significant for employees who continue to render services during business rescue proceedings and whom may have reservations in continuing to work for a financially distressed entity.

Section 136(1)(a) and 136(1)(b) of the Companies Act 2008 (as discussed above) is significant for the rights of employees in the sense that it confers a generous position in favour of any employee rendering a service to the company and to a certain extent even imbues some form of perceived guarantee of employment, at least for the period of business rescue proceedings. In the matter of *Solidarity obo BD Fourie and Others v Vanadium Products Proprietary Ltd and Others*,[254] the court considered an interpretation of section 136 in context, as the primary objective of the section is to prevent the unilateral variation of the obligations of the company by a business rescue practitioner during those business rescue proceedings, but not to stop the business rescue practitioner to suspend performance of certain contractual obligations except those relating to employees. Of importance however is that this section is not directed at preventing the lawful termination of contracts of employment as part and parcel of a business rescue plan that observes the applicable labour laws.

[251] Companies Act 1973, s 38.
[252] See Henochsberg 526(27).
[253] Companies Act 2008, s 135(4).
[254] (J385/16 and J393/16) [2016] ZALCJHB 106.

Any retrenchments of any such employees contemplated in the company's business rescue plan is subject to sections 189 and 189A of the Labour Relations Act 1995, and other applicable employment related legislation. This provision of the Labour Relations Act was tested on appeal in the matter of *South African Airways SOC Ltd and Others v National Union of metalworkers of South Africa obo members and Others*[255] where the court found that section 136(1)(b) requires that any retrenchments contemplated during business rescue proceedings need to be dealt with in the business rescue plan, and further that there is no provision in the section or anywhere else in Chapter 6 of the Companies Act 2008 that empowers the business rescue practitioner to retrench employees in the absence of an adopted business rescue plan. The court further found that the provisions of section 136 is in accordance with the spirit, purport and objects of the Constitution of the Republic of South Africa, 1996 and especially with regard to section 32 thereof.

This appeal matter heard by the Labour Court on face value appears to be an excellent outcome for employees, but one must however consider that a section 189 or section 189A consultation process in terms of the Labour Relations Act 1995 is one that must be commenced at any time that the rights of employees may be affected, and this may not coincide with the publication of a proposed business rescue plan. The business rescue practitioner may then be forced to expedite the publication of the business rescue plan (not ripe for publication), which may be detrimental to the successful turnaround of the company and ultimately the preservation of jobs.

Section 144 of the Companies Act 2008 further provides for the rights of employees during a company's business rescue proceedings. Importantly, any employees of the company who are represented by a registered trade union may exercise any rights set out in Chapter 6 of the Act collectively through their trade union and in accordance with applicable labour law, or in the event that an employee is not represented by a registered trade union he may elect to exercise any rights set out in Chapter 6 either directly or by proxy through an employee organisation or representative. The legislature has therefore insured effective engagement between not only the employees but also the representatives of such employees with the business rescue practitioner. This accords with the provisions of the Labour Relations Act 1995, the Basic Conditions of Employment Act 1997 and the regulations thereto.

Section 144 further provides that during a company's business rescue process every registered trade union representing an employee of the company and any employee who is not so represented, is entitled to (i) notice which must be given in the prescribed manner to employees at their workplace and served at the head office of the relevant trade union, of every court proceeding, decision, meeting or other relevant event concerning the business rescue proceedings, and (iii) participate in any court proceedings arising during the business rescue proceedings. This is again a clear demonstration by the legislature of the need to observe the rights of employees within business rescue proceedings and to participate meaningfully at any given juncture during the business rescue proceedings. At certain times the weight of the workforce behind a business rescue practitioner may have a significant impact on the outcome of litigation that the business may find itself embroiled in, or may also have a negative effect on

[255] [2021] 6 BLLR 627 (LC).

the outcome of the business rescue as a whole, if in fact the employees have not been meaningfully involved in the business rescue process.

The Companies Act 2008 further provides for employees to form an employee's representative committee, and importantly such right may be exercised at the first meeting of employees in terms of section 148 or at any time during the business rescue proceedings. Ongoing and meaningful engagement with both the employees of the company and the business rescue practitioner has again been highlighted in this section of the Act.

Section 144(3)(d) to section144(3)(g) confers rights on employees with regard to all aspects relating to the business rescue plan and the meeting of creditors[256] pursuant to a publication of a proposed business rescue plan. Employees are entitled to consult with the practitioner during the development of the business rescue plan and the business rescue practitioner must afford sufficient opportunity to review any such business rescue plan. Employees are further entitled to address the meeting of affected persons to consider the business rescue plan.

Employees are also vested with the rights to vote with creditors on any motion to approve the proposed business rescue plan to the extent that the employee is also a creditor of the company, and employees are further entitled to propose the development of an alternative business rescue plan in the manner contemplated in section 153 or to present an offer to acquire the interests of one or more of the affected persons in the manner contemplated in section 153.

The rights of employees are clarified in section 144(4) of the Companies Act 2008 with regard to unpaid amounts due to a medical scheme, pension scheme or provident scheme for the benefit of the past or present employees of the company. It is clear that to the extent that the company has not paid over any deductions in relation to such schemes, the relevant scheme is an unsecured creditor of the company for purposes of Chapter 6 to the extent of any amount that was due and payable by the company to the trustees of the scheme at any time before the beginning of the company's business rescue proceedings, and that had not been paid immediately before the beginning of those proceedings. This is also the situation in the case of a defined benefit pension scheme with regard to the present value at the commencement of business rescue proceedings of any unfunded liability under that scheme.

The legislature has further provided a catchall provision in section 144(5) of the Companies Act, in that the rights set out in this section are in addition to any other rights arising or accruing in terms of any law, contract, collective agreement, shareholding, security or court order.

Section 136(2) of the Companies Act 2008 provides for a business rescue practitioner's rights to suspend entirely, partially or conditionally, for the duration of business rescue proceedings, any obligation of the company that arises under an agreement to which the company was a party at the commencement of the business rescue proceedings and would otherwise become due during those business rescue proceedings. A business rescue practitioner may even apply urgently to a court to entirely, partially, or conditionally cancel on any terms that are just and

[256] Companies Act 2008, s 151.

reasonable in the circumstances, any obligation of the company in terms of such contractual agreement.

Employees' rights are however specifically catered for in the Companies Act 2008 *vis-à-vis* their contracts of employment in that a business rescue practitioner may not suspend nor cancel an employment contract[257] and accordingly the legislature has carved out employment contracts and has elevated the rights of employees.

6.3 Employees' statutory preference in relation to pre-business rescue claims

Employees are an integral part of any restructuring process and accordingly the legislature has ensured that employees are sufficiently catered for in relation to their pre-business rescue claims by providing for a preference for such claims. By elevating the pre-business rescue claims of employees to that of a creditor it also ensures that employees will have a direct influence on the outcome of the voting with regard to a proposed business rescue plan, to the extent that employees are also then creditors of the company.

Section 144 clarifies the position of employees claims that arose prior to the commencement of business rescue and to the extent that any remuneration, reimbursement for expenses or other amount of money relating to employment became due and payable by a company to employee at any time before the beginning of the company's business rescue proceedings, and had not been paid to that employee immediately before the beginning of those proceedings, the employee is a preferred unsecured creditor of the company for purposes of Chapter 6 of the Companies Act 2008.

The term "preferred unsecured creditor" is not defined in the Companies Act 2008 and appears to derive its genesis from trite insolvency law in various jurisdictions. The effect for purposes of Chapter 6 is that employees' claims appear to be preferential unsecured claims for purposes of the business rescue proceedings and the ranking of claims in such business rescue proceedings. A prudent business rescue practitioner would then have to deal with the preferential nature of such employee claims as part and parcel of the business rescue plan of the company. The statutory preference created for employees in Chapter 6 is in stark contrast to the provisions of section 98A of the Insolvency Act, where limited preferences are afforded to an employee of a company that is in liquidation and accordingly the business rescue provisions *vis-à-vis* the ranking of the pre-commencement claims of employees is highly preferable. It is of course of importance to differentiate between the claims of employees in relation to pre-commencement claims and those that arise post the commencement of business rescue, as is dealt with in section 135 of the Companies Act 2008.

The statutory preference conferred on employees is also not capable of being compromised in a business rescue plan, as was dealt with in the matter of the *South African Pilots Association and South African Airways*.[258] It was made clear that the preferences afforded to employees

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[257] *Idem*, s 136(2A)(b).
[258] [2021] 6 BLLR 627 (LC).

under section 144(2) could not be compromised or negated in a business rescue plan, which is of significance to employees in the context of voting for a business rescue plan.

6.4 Suspension of contracts by the practitioner

A business rescue practitioner has certain powers conferred on him once appointed and in terms of section 136(2) of the Companies Act 2008 a business rescue practitioner has the ability to suspend obligations of a company in rescue *vis-à-vis* any contracts that it has entered into prior to the commencement of business rescue proceedings.

A business rescue practitioner, whilst developing a restructuring plan for the business, may identify certain contracts as being onerous or prejudicial to the ongoing operations and ultimately the solvency of the company, and accordingly the legislature has conferred powers on the business rescue practitioner to address the onerous nature of such contracts by entirely, partially or conditionally suspending, for the duration of business rescue proceedings any obligation of the company that arises under an agreement to which the company was party at the commencement of business rescue proceedings, or any obligations that would otherwise become due during those proceedings.

Of utmost importance, in section 136, is the use of the wording "entirely, partially or conditionally" with regard to the powers of the practitioner to suspend any obligations of the company. Why this is of significant importance is that the business rescue practitioner can apply his mind as to exactly how such suspension may take place in order to tailor make a position for the company that will give it the best opportunity to successfully restructure its affairs.

The business rescue practitioner may elect to entirely suspend all obligations of the company in terms of any agreement, or alternatively only suspend a portion of those obligations and even make the suspension conditional on certain fundamental aspects of the contract being fulfilled or negotiated between the contracting parties. The suspension of contractual obligations remains an underutilised tool by business rescue practitioners and one that should be carefully explored in any restructuring process within a business rescue.

The onerous nature of any contract may manifest itself in terms of oppressive obligations on the company which may include excessive rental amounts in lease agreements, loan agreements with excessive interest payments, or supply agreements with unfair pricing arrangements.

It is of utmost importance that when considering a suspension of any contractual obligation, the business rescue practitioner considers the moratorium provided for in section 135 together with the contractual position prior to the business rescue practitioner enforcing such suspension on whatever cogent terms necessary to protect the interests of the company.

Our courts have dealt with the effects of such suspension and as to when such suspensions are valid and enforceable by the business rescue practitioner.

The correct position should be that if the contract with the company is validly terminated before the commencement of business rescue proceedings, the company is not lawfully in possession of the property in question and accordingly the general moratorium in section 133 of the Companies Act 2008 cannot apply. The practitioner is then not in a position to suspend the obligations of the company in terms of such agreement, if in fact the agreement was cancelled prior to the commencement of business rescue proceedings and accordingly the contracting party would be entitled to enforce its rights either in terms of the surviving provisions of the contract or its common law rights.[259]

In the matter of *Homez Trailers and Bodies (Pty) Ltd v Standard Bank of South Africa Ltd*[260] the court considered a cancellation and / or suspension of an overdraft facility in terms of the relevant contractual provisions. In order for a business rescue practitioner to suspend an agreement, the agreement needed to be in place as at the commencement of business rescue proceedings. If the contract is in existence at the commencement of business rescue, then the business rescue practitioner can entirely, partially or conditionally suspend during the duration of business rescue proceedings any obligation of the company that arises under that agreement. However, if the contract has been validly cancelled, then there are no obligations to be suspended.

In *Cloete Murray and Another NNO v FirstRand Bank Ltd t/a Wesbank*[261] the court held that by invoking the provisions of section 136, a practitioner can prevent a creditor from instituting an action and repossessing or attaching property in the company's possession.

In *Tayob v Multi Furn Wholesalers and Retailers (Pty) Ltd*[262] the court dismissed an application in terms of section 136(2)(b), where disputes of fact could not be resolved on the papers. Generally speaking, where obligations owed by contracting parties to each other are reciprocal in nature, it is not open to the party that is unable or unwilling to perform to insist that the other party must perform. This common law principle is not overruled by section 136 of the Companies Act 2008. Accordingly, care should be taken in each case to determine on the specific facts whether the obligations in question are in fact truly reciprocal, or whether they are merely contained in the same agreement.

In the case of *BP Southern Africa (Pty) Ltd v Intertrans Oil SA (Pty) Ltd and Others*[263] the court held that it must be accepted that a creditor maintains its common law contractual remedies for the non-performance by a distressed company which is under business rescue proceedings. In other words, a creditor in respect of an agreement which a practitioner has suspended maintains its common law right to withhold continued, reciprocal, performance (the *exceptio non adimpleti contractus* remedy), or alternatively to cancel the agreement. Court held that BP Southern Africa (Pty) Ltd was entitled to withhold access to the lease premises or alternatively

[259] See Henochsberg 526(30).
[260] (35201/2013) [2013] ZAGPPHC 465 (27 September 2013).
[261] 2015 (3) SA 438 (SCA), at para 35.
[262] (32604 / 2017) [2018] ZAGPPHC 548 (6 August 2018).
[263] 2017 (4) SA 592 (GJ) (25 November 2016). See also Levenstein 9-84, 9-116; and Henochsberg 526(30).

could cancel the agreement in its entirety, notwithstanding the suspension of the company's obligations in terms of section 136(2)(a).

6.5 Cancellation of contracts by the practitioner

The legislature has further conferred powers on a business rescue practitioner to seek the cancellation of contracts that the practitioner may deem to be onerous or prejudicial to the company in business rescue. In terms of section 136(2)(b) contracts tend to be cancelled entirely, partially or conditionally if the business rescue practitioner applies to court and the Companies Act 2008 makes further mention that the practitioner may do so on an urgent basis.

A court must consider whether the cancellation sought by the business rescue practitioner will in the circumstances be just and reasonable on the basis set out in the papers before the court. The powers of the business rescue practitioner to cancel contracts cannot be over-emphasised as many financially distressed businesses are often hamstrung by a singular contract, that in the absence of the company being held to such contractual terms may see the successful restructuring of its affairs. The court is of course imbued with a discretion to determine what is just and equitable in the circumstances of each case.

Many business rescue practitioners would immediately suspend the obligations of the company in relation to the onerous contract with the view to ultimately apply to court for the cancellation of such onerous contract, and it is of importance that once the suspension provisions of the Companies Act 2008 are utilised by a practitioner in order to suspend obligations of the company for the period of business rescue, the counterparty is not in a position to cancel the agreement. If the creditor then purports to cancel the agreement after the notice of suspension has already been provided by the practitioner, such cancellation would be unlawful.

It is further trite that once an agreement is cancelled then the creditor cannot frustrate the business rescue practitioner in relation to the occupation of property or any assets in the company's possession in terms of such agreement, and the goods subject to the cancelled agreement remain in the possession of the company, after cancellation. This was dealt with in the matter of *LA Sport 4X4 Outdoor CC and Another v Broadswood Trading 20 (Pty) Ltd and Others*,[264] where the court held that because the cancellation of the contract was valid, the company under business rescue was in unlawful possession of the property. However, the court did not specifically determine whether the property had to be returned to the creditor and this decision places the business rescue process in jeopardy in that the property enabling the company to trade may ultimately be returned to the creditor disabling the business rescue process in seeking the successful restructuring of the company's affairs.

In the matter of *178 Stamfordhill CC v Velvet Star Entertainment CC*[265] the court ruled that it was competent for the landlord to cancel the lease and to seek the ejectment of the tenant when the tenant did not honour its obligations in terms of the lease incurred prior to the commencement of business rescue. The court found that the position of the business rescue practitioner is akin

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[264] (A513/2013) [2015] ZAGPPHC 78 (26 February 2015).
[265] (1506/15) [2015] ZAKZDHC 34 (1 April 2015).

to that of a liquidator or trustee in insolvency and that notwithstanding the establishment of a *concursus creditorum*, the contract with the respondent could be cancelled. The so-called suspension of the lease in section 136(2) of the Companies Act 2008 cannot amount to anything more than the practitioner's rights not to be compelled to perform in terms of the contract, and the court held that the applicant was entitled to an order for the ejectment of the respondent from the premises. This is an important decision in that, despite section 133 and the general moratorium, landlords can seek the ejectment of a tenant in business rescue who remains in occupation and who suspends the obligation to pay rent to the landlord.

The effects of a court cancelling a contract on the papers presented to it, is that the contracting counterparty or creditor would be entitled to enforce damages claims as against the company in business rescue. The calculation of such damages would be for a court to determine based on the facts, as there is no definition in the Companies Act 2008 of how such damages are to be calculated. One needs to make a distinction between both direct and consequential damages. Direct or general damages can be defined as damages suffered as a direct consequence of the wrongful act, and consequential damages can be defined as damages that do not flow directly and immediately from a wrongful act but result indirectly from such wrongful act. It is clear therefore that only a court would be able to determine the extent of either the general or consequential damages that flow from an order cancelling an onerous contract, on application.

Any such damages claims would fall to be dealt with in terms of the proposed business rescue plan with many business rescue practitioners seeking to have such claims compromised in terms of the plan.

Self-Assessment Questions for Chapter 6

Refer to the Case Study in Chapter 1 of these notes when answering the questions below.

Question 1

After investigating the affairs of Fast Flights, the business rescue practitioner ascertains that the various aircraft subject to instalment sale agreements are vital to the company's rescue process, but due to cash flow constraints cannot afford the monthly instalments. The business rescue practitioner elects to suspend Fast Flights' obligations relating to payment in terms of the instalment sale agreements for the period of the rescue. Is the business rescue practitioner entitled to do so if the instalment sale agreements were cancelled by the financial institution prior to the rescue procedure commencing? Provide reasons for your answer.

Question 2

Since Fast Flights is experiencing severe cashflow constraints, can the business rescue practitioner unilaterally reduce all staff salaries and wages to 50% of their contractual entitlement for the period of the business rescue in order to alleviate the cash flow constraints?

Question 3

The business rescue practitioner of Fast Flights wishes to publish a proposed business rescue plan that includes a proposal for the sale of the business of the company to third party purchaser, as a going concern. It is the intention of the business rescue practitioner to sell the business out of the corporate entity and for the purchaser of the business to house it in a new corporate entity. However, the business rescue plan is silent on what effect the sale of the business would have on the employees of the company.

Do the employees of the company have any legal recourse in relation to the sale of the business and their ongoing employment? Select the **correct** answer from the list below:

(a) No, the employees do not have any right of recourse and would remain employed by the company in rescue.

(b) No, the employees do not have any right of recourse and would have to approach the purchaser of the business in order to negotiate re-employment.

(c) Yes, the employees have rights in terms of section 197 of the Labour Relations Act 1995 and their contracts of employment would be transferred to the purchaser by operation of law.

(d) Yes, but the employees would be required to reach agreement with the purchaser of the business as to the terms and conditions of their employment and the transfer does not take place by operation of law.

For feedback on this self-assessment exercise, see the document "Comment and Feedback on Self-Assessment Questions", which is made available to you as a separate document.

CHAPTER 7

THE EFFECT OF BUSINESS RESCUE ON SHAREHOLDERS AND DIRECTORS

7.1 The rights of shareholders and their participation in the business rescue proceedings

A shareholder is defined as the holder of a share issued by a company, who is entered as such in the certificated or uncertificated securities register and includes a person who is entitled to exercise any voting rights in relation to a company.[266]

During business rescue proceedings, shareholders (together with employees, trade unions and creditors) are "affected persons"[267] and, as such, are afforded certain rights to be notified of,[268] participate in, and object to[269] the proceedings. Affected persons are also afforded the right to bring an application to commence business rescue proceedings.[270]

During business rescue proceedings, shareholders are also entitled to notice of and the right to participate in, court proceedings and other business rescue meetings and, if the proposed business rescue plan alters the rights of the holders of any class of the company's securities (that is, the rights attached to their shares), to vote on the approval or rejection of the proposed business rescue plan.[271]

There has been much debate as to what it means to "alter the rights of the holders of any class of the company's securities". Would a dilution in the value of shares amount to an alteration of rights, or would something more, such as an alteration in the voting rights attached to a particular class of share, be required? While a court has not yet pronounced on this, it is submitted that the latter view is likely to be correct.

During business rescue, an alteration in the classification or status of any issued securities can only be affected via either a business rescue plan[272] (which would have to be approved by a majority of the holders of the class or classes of securities at a meeting held immediately after the meeting convened in order for the creditors to vote on the business rescue plan)[273] or through a court order. Presumably the latter route would only be followed by a business rescue practitioner as a last resort, probably against the wishes of the shareholders affected by the alteration.

Shareholders are often also creditors who may be entitled to vote on a business rescue plan in both or one of those capacities. Shareholders who are also creditors may, in certain

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266 Companies Act 2008, s 1 as read with s 57(1).
267 *Idem*, s 128(1)(a).
268 *Idem,* s 129(3)(a).
269 *Idem,* s 130.
270 *Idem,* s 131(1).
271 *Idem,* s 146 as read with s 152(3)(c).
272 *Idem,* s 137(1)(a) and (b).
273 *Idem*, s 152(3) (c).

circumstances, be found to be not independent[274] or subordinated, which will impact on the voting interest[275] accorded to the creditor for voting purposes.

Moreover, the business rescue practitioner has an obligation to consult with creditors, other affected persons and the management of the company before preparing a business rescue plan for consideration and possible adoption.[276]

The court in the case of *Hlumisa Investments Holdings (RF Limited and Another) v Van der Merwe NO and Others*,[277] found that there is a clear distinction between "informing" and "consulting". With regard to "consulting", the court quoted, with approval, what Rogers J emphasised from various cases he considered in the matter of *Scalabrini Center Cape Town and Others v Minister of Home Affairs and Others*,[278] as follows:

> "…at a substantive level, consultation entails a genuine invitation to give advice and a genuine receipt of that advice;
>
> consultation is not to be treated perfunctorily or as a mere formality. This mean inter alia that engagement after the decision-maker has already reached his decision or once his mind has already become "unduly fixed", is not compatible with true consultation; and
>
> that while at a procedural level consultation may be conducted in any appropriate manner determined by the decision-maker, the procedure must be one which enables consultation in the substantive sense to occur."

Based on the above analysis, the court in *Hlumisa* found, *inter alia*, that informing creditors and shareholders of what was happening by way of Stock Exchange New Service[279] announcements and in meetings with individual shareholders and a body of preferent shareholders, did not amount to "consultation" and granted an interim interdict preventing a meeting that was convened to vote on the proposed business rescue plan from proceeding. The fact that the shareholders in question were not in fact entitled to vote on the proposed business rescue plan at the meeting that was ultimately prevented from proceeding, and that they held a combined 4.9% of the shareholding of the company in business rescue, were found to be irrelevant factors. This judgment constitutes a powerful tool which, if wielded correctly, could be used by shareholders and other affected persons (for example employees, trade unions or minority creditors) who may otherwise not be able to have their views heard.

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274 *Idem*, s 128(1)(g) read with s 2.
275 *Idem*, s 145(4)(b) read with *Commissioner of SARS v Beginsel NO and Others* (15080/12 [2012] ZAWCHC 194.
276 Companies Act 2008, s 150(1).
277 [2016] JOL 34326 (GP).
278 2013 (3) SA 531 (WCC) at 72.
279 The Johannesburg Stock Exchange offers a service that provides the user with access to company announcements such as mergers, take-overs, rights offers, capital issues, cautionaries - all of which have a direct impact on the movement in the market. This service is called Stock Exchange News Service.

If a business rescue plan has been rejected, and the business rescue practitioner does not (i) seek a vote of approval from the holders of voting interests to prepare and publish a revised plan,[280] or (ii) advise the meeting that the company will apply to a court to set aside the result of the vote by the holders of voting interests or shareholders (as the case may be), on the grounds that it was inappropriate,[281] shareholders (and other affected parties) are entitled to call for a vote of approval from the holders of voting interests requiring the business rescue practitioner to prepare and publish a revised plan[282]or apply to court to set aside the result of the vote on the basis that it was inappropriate.[283] Shareholders (and other affected persons) are also entitled to make a binding offer to purchase the voting interests of the person / persons who opposed the adoption of the business rescue plan.[284] However, it is noted that since the Supreme Court of Appeal found that a "binding offer" is binding only on the offeror until the offeree responds to it,[285] this option is, in practice, very rarely exercised.

Business rescue also limits rights that shareholders would otherwise have held. For example, a special resolution of shareholders is not required to dispose of all or a greater part of the assets of a company, if that disposal is pursuant to an adopted business rescue plan.[286]

If one compares the respective voting rights of shareholders in and out of business rescue, it becomes evident that, in certain circumstances, business rescue could be utilised as a strategic tool to conclude a transaction without shareholder support.

Boards of companies are under a duty to act in the best interests of the company. Previously this duty had been narrowly interpreted to mean to return value to shareholders. While this narrow interpretation is changing to include a broader group of stakeholders, shareholders sometimes find themselves at odds with business rescue practitioners. This is because business rescue practitioners (unlike boards of directors), have a statutory duty to develop and implement a business rescue plan that, at the very least, results in a better return for the company's creditors or shareholders than would result from the immediate liquidation of the company. The effect of this is that business rescue practitioners take into account and balance the interests of all affected parties and not just shareholders. Moreover, shareholders who may previously have been able to exercise control over the board (*inter alia* because they may have had the power to remove and replace directors), may find themselves unable to exercise the same level of control over an independent business rescue practitioner.

Tensions between business rescue practitioners and shareholders sometimes play themselves out in the realm of the remuneration of the business rescue practitioner. A business rescue practitioner is entitled to propose an agreement with the company providing for further remuneration on the basis of a contingency, in addition to that which is permitted by the

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[280] Companies Act 2008, s 153(1)(a)(i).
[281] *Idem*, s 152(1)(a)(ii).
[282] *Idem*, s 153(1)(b)(i)(aa).
[283] *Idem*, s 153(1)(b)(i)(bb).
[284] *Idem*, s 153(1)(b)(ii).
[285] *African Banking Corporation of Botswana v Kariba Furniture Manufactures (Pty) Ltd* 2013 (6) SA 471 (GNP), at para 29.
[286] Companies Act 2008, s 112 (1)(a).

government regulated tariff.[287] This agreement is final and binding on the company if it is approved by the "holders of a majority of the creditors' voting interests"[288] and the "holders of a majority of the voting rights attached to any shares of the company that entitle the shareholder to a portion of the residual value of the company on winding up".[289] Some business rescue practitioners have interpreted this (in the authors' view, incorrectly) to mean that a meeting of shareholders to vote on a remuneration agreement is only required if the shareholders would actually receive a dividend (from the residual value of the company by virtue of their shareholding) on the winding-up of the company. If this interpretation were correct, it would mean that shareholders would very rarely, if ever, have a say on remuneration agreements. The better view (and the view that is more frequently adopted in practice) is that the section in question entitles shareholders to vote if their class of share would entitle them to lodge a claim in a liquidation (in other words, regardless of whether there would be an actual dividend paid to the shareholder in a liquidation scenario).

7.2 The rights and duties of directors in the business rescue context

Ordinarily the powers of both governance and management of a company reside in the board of directors, as appears from section 66(1) of the Companies Act 2008, which reads as follows:

> "The business and affairs of a company must be managed by or under the direction of its board, which has the authority to exercise all of the powers and perform any of the functions of the company, except to the extent that this Act or a company's Memorandum of Incorporation provides otherwise."

Upon a company being placed under supervision and in business rescue, the business rescue practitioner assumes full management control of the company in substitution for its board and pre-existing management and may then delegate any power or function to a director or pre-existing management of the company.[290]

During business rescue, directors must continue to exercise their functions as directors, subject to the authority of the business rescue practitioner and they owe a duty to the company to exercise any management function in accordance with the instructions of the business rescue practitioner. Directors also remain bound by the requirements of section 75 of the Companies Act 2008, and to the extent that they act according to the instructions and subject to the authority of the business rescue practitioner, they are relieved from the duties and liabilities set out in sections 76 and 77, other than section 77(3)(a), (b) and (c) of the Companies Act 2008.[291] If one

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[287] *Idem,* s 143(2).
[288] *Idem,* s 143(3)(a).
[289] *Idem,* s 143(3)(b).
[290] *Idem*, s 140(1)(a) and (b).
[291] Companies Act 2008, s 73(a), (b) and (c) reads as follows:
"(3) A director of a company is liable for any loss, damages or costs sustained by the company as a direct or indirect consequence of the director having–
(a) acted in the name of the company, signed anything on behalf of the company, or purported to bind the company or authorise the taking of any action by or on behalf of the company, despite knowing that the director lacked the authority to do so;

or more directors or the board purports to take any action on behalf of the company that requires the approval of the practitioner, that action is void unless approved by the practitioner.[292]

Directors have mandatory statutory duties to co-operate with and assist the business rescue practitioner: directors must (i) attend to the reasonable requests of the business rescue practitioners, (ii) provide information about the company's affairs, and (iii) as soon as possible after the commencement of the business rescue proceedings, deliver to the business rescue practitioner all of the company's books and records that may be in their possession. Directors must also, within five business days of the commencement of the business rescue, provide the business rescue practitioner with a statement of affairs containing details of any material transactions involving the company or its assets occurring within the previous 12 months, any legal proceedings, assets, liabilities, income and disbursements, employees, debtors and creditors.[293] If one has regard to the fact that a business rescue practitioner is an independent professional who is parachuted into a company in distress, generally on very short notice and sometimes without much experience of the industry in question, it would be difficult to run a successful business rescue if the entire board were either to resign (and there is nothing preventing them from doing this) or be uncooperative.

In practice, a business rescue will have a better prospect of success if the directors and existing management take an active role in the matter and assist the business rescue practitioner in the continuation of the business, with a view to successfully developing and implementing a business rescue plan.

There has been much recent debate as to what, if any, authority is retained by directors to act on behalf of the company during business rescue proceedings. Must all their actions be either mandated or ratified by the business rescue practitioner? The court in *Ragavan v Optimum Coal Terminal (Pty) Ltd*[294] was tasked with this analysis and the case summary, quoted below, provides some answers:

> "The applicants in the case of Ragavan v Optimum Coal Terminal (Pty) Ltd, were the directors of Tegeta and Exploration and Resources, a creditor of the first respondent, Optimum Coal Terminal (OCT). Both companies were in business rescue. The applicants sought a declarator that they, instead of OCT's business rescue practitioners should vote on behalf of OCT at any meeting of creditors in respect of section 151(1) of the Companies Act 71 of 2008.
>
> The court held that clarity is needed in the Companies Act to resolve the tension between directors who still want to be in control and view matters subjectively

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(b) acquiesced in the carrying on of the company's business despite knowing that it was being conducted in a manner prohibited by section 22 (1);
(c) been a party to an act or omission by the company despite knowing that the act or omission was calculated to defraud a creditor, employee or shareholder of the company, or had another fraudulent purpose;".

[292] *Idem*, s 137(4).
[293] *Idem*, s 142(1), (2) and (3).
[294] 2022 3 SA 512 (GJ).

> and the business rescue practitioners who have a more holistic view of what is good for the company in business rescue and want to do things their way and are armed with statutory powers. Business rescue practitioners take over full management control of the company in business rescue in substitution for its board of directors and pre-existing management. The business rescue practitioner is tasked with developing and then implementing a business rescue plan which is in the best interest of all affected parties which includes creditors, employees, trade unions and shareholders. That occurs while the board of directors retains obligations in terms of the Companies Act.
>
> The court confirmed that the Companies Act gives business rescue practitioners full management control. While there are overlapping areas between managing the business of the company and the affairs of the company in the ordinary course, the provisions of Chapter 6 are clear and there is not much overlap, with the respective roles being clear. The question of who is entitled to vote requires a logical application of Chapter 6. An analysis of the relevant sections in chapter 6 made it clear that the powers of the Director are limited in business rescue proceedings and there is a legal transfer of power to the business rescue practitioners.
>
> On a proper construction of chapter 6, the powers of directors become substantially curtailed. Governance functions remain for the directors, but it is a neutral function far removed from full management control. Nothing of significance can be done by the directors during business rescue proceedings without the authorization by the Business Rescue practitioner."

The application was dismissed, however leave to appeal to the Supreme Court of Appeal was granted but (as at the date of this publication) not yet heard.

The court in the case of *Tayob and Another v Shiva Uranium (Pty) Limited and Others*[295] found that if a business rescue practitioner dies, resigns or is removed from office, a substitute must be appointed by the board of the company or by the affected persons who made the nomination[296] and that the absence of approval by the relevant business rescue practitioner would not render the decision made by the company void. This judgment of the Supreme Court of Appeal was upheld by the Constitutional Court.[297]

Henochsberg submits that:

> "the directors acting as an internal organ of the company will be actions by the directors merely as directors and/or exercising functions as directors, while acting to the outside, as agents etc. would be the exercise of management powers...

[295] 2020, JOL, 49109 (SCA).
[296] Companies Act 2008, s 139(3).
[297] *Shiva Uranium (Pty) Limited (in business rescue) and Another v Tayob and Others* 2022 3 SA 432 (CC).

> In respect of business rescue it will be logical to remove the (management) powers to act to the outside (and bind the company to contracts) from the directors and give it to the business rescue practitioner while the same reasoning would obviously not apply to internal acts…
>
> The position should therefore be that if an act is purely an internal act by the directors as an organ of the company, and that act is not subject to restrictions of conditions of e.g., s137, or exclusively within the powers of the business rescue practitioner in terms of e.g., s141, the directors are exercising their functions in terms of sub-s(2)(a). Actions to the outside, e.g., as agents for the company will be management of the company regulated by s140 and thus will be exercised by the business rescue practitioner unless delegated to the directors by the business rescue practitioner."[298]

While the proposed divide between "internal" and "external" acts seems logical, it is possibly an oversimplification in that "the fact that an act may have an external manifestation does not mean that it is an external act; it may be an internal act with an external aspect – For example, casting a vote as a creditor in another rescue process. The decision how to vote is probably internal although the casting of the vote is an act to the outside".[299]

An affected party may, at any time after the adoption of a resolution placing a company into business rescue but prior to the passing of a business rescue plan, apply to court for an order setting aside the resolution or the appointment of the practitioner. A director who initially voted in favour of the resolution/s in question may not apply to court for this relief unless he can show that when he initially supported the resolution, he did so in good faith and on the basis of information that has subsequently been found to be false or misleading.[300]

7.3 The removal and replacement of directors by the business rescue practitioner

The business rescue practitioner is only able to remove a director during business rescue proceedings by means of a court order, if the director has failed to comply with a requirement of Chapter 6 of the Companies Act 2008, or by act or omission has impeded or is impeding the business rescue practitioner in (i) the performance of his powers and functions, or (ii) the management of the company by the practitioner, or (iii) the development or implementation of a business rescue plan.[301]

In practice, court ordered removals during business rescue rarely happen in that the business rescue practitioner's powers in matters of importance will always trump those of directors. Furthermore, litigation of this nature is costly and time consuming and not in the best interest of

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[298] *Henochsberg* 526(38).

[299] Heads of argument filed by counsel for the appellants in the Supreme Court of Appeal in the matter of *Ragavan V Optimum Coal Terminal (Pty) Ltd* 2022 3 SA 512 (GJ).

[300] Companies Act 2008, s 130(2).

[301] *Idem*, s 137(5). This right is in addition to any right of a person to apply to court in terms of s 162 of the Companies Act 2008, to have a director declared delinquent or under probation.

the rescue process. It is far easier to remove directors by way of an ordinary resolution adopted at a shareholders' meeting.[302]

If, as is often the case, a director is also an employee of the company in business rescue, his removal as a director would not automatically terminate his contract of employment. A business rescue practitioner can only terminate a contract of employment in accordance with the Labour Relations Act.

Chapter 6 does not specifically empower the business rescue practitioner to appoint new directors. The appointment of directors is generally a matter for the shareholders of a company and it is submitted that this remains the position in business rescue.

Self-Assessment Questions for Chapter 7

Refer to the Case Study in Chapter 1 of these notes when answering the questions below.

Question 1

What rights would the shareholders have to participate in Fast Flight's business rescue process?

Question 2

Mr Float would have had an obligation to consult with creditors, other affected persons, and the management of the company before preparing a business rescue plan for consideration. What should "consultation" entail? What steps can the shareholders take if Mr Float fails to consult properly with them?

Question 3

Consider whether Fast Flight's shareholders would have any rights to vote on its business rescue plan, or on Mr Float's remuneration agreement.

Question 4

What duties would Mr L Block and his fellow directors owe to Mr A Float?

Question 5

In which circumstances could Mr A Float have Mr L Block removed as a director? Which, if any, powers and obligations would Mr Block and his fellow board members retain during the business rescue process?

[302] *Idem*, s 71(1).

Question 6

Would Mr Float be able to appoint a new director in Mr Block's place?

For feedback on this self-assessment exercise, see the document "Comment and Feedback on Self-Assessment Questions", which is made available to you as a separate document.

CHAPTER 8

THE BUSINESS RESCUE PRACTITIONER

8.1 Who is the business rescue practitioner?

The business rescue practitioner of a company is a professional person of the highest ethical standards that is appointed to manage the affairs of the company whilst investigating its affairs and preparing a business rescue plan for consideration by the company's creditors and shareholders.[303]

The business rescue practitioner not only has full management control of the company in substitution for its board and pre-existing management,[304] who consequently has the responsibilities, duties and liabilities of a director as set out in sections 75 to 77 of the Companies Act 2008, but is also an officer of the court.[305]

8.2 How to qualify as a business rescue practitioner

The minimum required qualifications of a business rescue practitioner are set out clearly in section 138 of the Companies Act 2008. This section essentially seeks to set a minimum bar or standard to be met by any business rescue practitioner and is the first indication in the Act that the legislature intended that a business rescue practitioner meets the highest ethical and professional standards.

Specifically, the practitioner must:

- be a member in good standing of a professional body that has been accredited by CIPC[306] (SARIPA is one of the accredited professional bodies);
- be licenced by CIPC as a business rescue practitioner;
- not be subject to an order of probation in terms of section 167(7) of the Companies Act 2008;
- not be disqualified from acting as a director of the company in terms of section 69(8) of the Companies Act 2008;

[303] *Idem*, s 128(1)(d).
[304] *Idem*, s 140(1)(a).
[305] *Idem*, s 140(3). However, see *Knoop and Another NNO v Gupta (No 2)* (Case No 116/2020) [2020] ZASCA 163 (9 December 2020), at paras 32, 33 and 111, where the Supreme Court of Appeal stated that describing a business rescue practitioner as an officer of the court has no application to a voluntary business rescue (para 32); the Court also stated that describing a business rescue practitioner as an officer of the court does not add anything to their duties or responsibilities (para 33). The stance of the court is to be borne in mind when describing a business rescue practitioner as an officer of the court.
[306] Companies Act 2008, s 138(1)(a).

- not have a relationship with the company that would lead a reasonable and informed third party to conclude that the integrity, impartiality or objectivity of the business rescue practitioner is compromised by that relationship; and

- is not related, as defined in the Companies Act 2008, to a person with a relationship to the company that would lead a reasonable and informed third party to conclude that the integrity, impartiality or objectivity of the person is compromised by that relationship.[307]

The CIPC, in licencing practitioners, considers the qualifications and experience of the applicant in determining whether the prospective business rescue practitioner is to be licenced as junior, intermediate or senior business rescue practitioner.

CIPC Notice 23 of 2022[308] requires that the information relating to the form CoR126.1 and legal documents in terms of section 138(1) of the Companies Act 2008, must be submitted via the electronic platform New e-Services. The documents to be submitted include:

- A comprehensive résumé (CV) containing full and detailed particulars of the applicant's history and relevant experience of active engagement in a business turnaround and / or business rescue activities.

- A schedule of experience, including the following, must be supplied:

  - Enterprise name and number for which a business turnaround or business rescue was conducted;

  - Duration (day / month / year);

  - Specific role the incumbent had, or is having in the company; and

  - The outcome.

- Supporting documentation to substantiate the information in respect of the history and relevant practical experience (provide references).

- Copy of a valid tax clearance certificate (individual).

- Letter of good standing from the accredited professional body by the Commission.

- A sworn statement in terms of Section 138 (1) stating that the applicant:

  - is not subject to an order of probation in terms of section 162 (7);

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[307] *Idem*, s 138(1)(b).

[308] https://www.cipc.co.za/?p=14123. Note that notices may be amended by the CIPC from time to time and it is your responsibility to keep abreast with any changes.

- would not be disqualified from acting as a director of the company in terms of section 69 (8); and
- is of sound financial status.

- The applicant must adhere to the concurrent application of section 5(6) of the Companies Act 2008 as amended, in case of a listed entity.

8.3 Appointment of a business rescue practitioner

Business rescue practitioners are appointed either by the company or by the court and follows from the method of commencing the business rescue proceedings. In a case where the board of a company has commenced business rescue proceedings by resolution, that same board is tasked with appointing the practitioner.[309] Similarly, where the proceedings commence by order of court the Act provides that the court may (not must) make a further order appointing an interim practitioner.

An interim business rescue practitioner appointed by the court must be confirmed as the business rescue practitioner of the company at the first meeting of creditors.[310] The ratification is carried by a simple majority of the independent creditors' voting interests voted at the meeting.[311]

The wording in the Companies Act 2008 is curios, as there does not appear to be provision for the appointment of a practitioner where the court chooses not to appoint an interim practitioner. Similarly, the sections dealing with the first meeting of creditors does not deal with the ratification of the appointed practitioner, or what happens if the interim practitioner's appointment is not ratified. However, in the case of *Shiva Uranium (Pty) Limited (in business rescue) and Another v Tayob and Others*, the Supreme Court of Appeal held, and the Constitutional Court confirmed,[312] that the substitute appointment of a business rescue practitioner will be made by the company's board of directors if business rescue proceedings commenced voluntarily by board resolution, or by the affected person who brought the business rescue application if a Court ordered that the company enter business rescue proceedings.

When appointing a practitioner, the company and the court will need to ensure that the practitioner qualifies to be its business rescue practitioner. The practitioner must be a member in good standing of an accredited professional body and have a licence from CIPC to be a business rescue practitioner, must be independent of the company,[313] not be disqualified from

[309] Companies Act 2008, s 129(3)(b).
[310] *Idem*, s 131(5).
[311] *Idem*, ss 131(5) and 147.
[312] 2022 (3) SA 432 (CC) (9 November 2021).
[313] Companies Act 2008, s 138(1)(e).

acting as a director of the company[314] and not be subject to an order of probation.[315] CIPC require that the practitioner confirms the above before it will acknowledge the appointment of the practitioner.

8.4 The removal of business rescue practitioners

A business rescue practitioner can only be removed by order of court. The application to remove a practitioner is brought by an affected person who is required to establish and set out the reasons for the removal of the practitioner, and can only be based on a limited number of grounds set out in sections 130 and 139 of the Companies Act 2008. These limited grounds are, the business rescue practitioner:

- does not meet the requirements of section 138 of the Companies Act 2008 when appointed, or at a later date;[316]
- is not independent of the company or its management;[317]
- lacks the necessary skills, having regard to the company's circumstances;[318]
- is incompetent or fails to perform the duties of a practitioner;[319]
- fails to exercise the proper degree of care in the performance of his functions;[320]
- engages in illegal acts or conduct;[321]
- has a conflict of interest;[322] or
- is incapacitated and unable to perform the functions of that office and is unlikely to regain that capacity within a reasonable time.[323]

The applicant will need to prove the grounds for removal of a business rescue practitioner and must provide evidence in support of their assertions that a practitioner falls to be removed on one or more of the above grounds. However, as was held by the Supreme Court of Appeal in *Knoop and Another NNO v Gupta (No 2)*,[324] the court has a discretion either to grant or to refuse an order for the removal of business rescue practitioner. The discretion is exercisable if one or

[314] *Idem*, ss 138(1(d) and 69(8).
[315] *Idem*, ss 138(1)(c) and 162(7).
[316] *Idem*, ss 130(1)(b)(i) and 139(2)(d).
[317] *Idem*, ss 130(1)(b)(ii) and 139(2)(e).
[318] *Idem*, s 130(1)(b)(iii).
[319] *Idem*, s 139(2)(a).
[320] *Idem*, s 139(2)(b).
[321] *Idem*, s 139(2)(c).
[322] *Idem*, s 139(2)(e).
[323] *Idem*, s 139(2)(f).
[324] Case No 116/2020) [2020] ZASCA 163 (9 December 2020).

more of the grounds for removal set out in section 139(2) has been established on a balance of probabilities. However, proof of a ground for removal alone does not dictate that an order for removal must follow. The power of removal is not combined with a duty to exercise that power. The range of actions by business rescue practitioners that might fall within these sub-sections, and the degree of seriousness and varying implications they may have for the business rescue process, must be such that proof of one or more of these grounds will necessitate removal. Whether they do is a matter for judgment on the facts of the particular case.

8.4.1 When can an application in terms of section 130 or section139 be launched?

An application to remove a business rescue practitioner can be brought in terms of section 130 of the Companies Act 2008 between the adoption of the resolution appointing a business rescue practitioner (but logically only after the practitioner has actually been appointed) and the date on which the business rescue plan is adopted.

This restriction in time does not appear to apply to an application that may be brought for the removal of a business rescue practitioner under section 139 of the Companies Act 2008. However, as mentioned above, even if the grounds for removal as set out in section 139(2) of the Companies Act 2008 are met, the degree of seriousness and varying implications they may have for the business rescue process, will be taken into account by a court when exercising its discretion under this section.

8.5 Who appoints the replacement practitioner?

The Constitutional Court[325] confirmed the Supreme Court of Appeal[326] judgment which held that, where a practitioner appointed by a company in terms of section 129(1)(b) resigns or is removed, the company itself (acting through its board) may appoint the substitute. On the other hand, where a practitioner appointed by the court in terms of section 131(5) resigns, the "affected person" who applied for the company to be placed in business rescue, and who made the nomination envisaged in section 131(5), would have the ability to appoint a substitute practitioner.

The Constitutional Court was of the view that this interpretation of section 139(3) would ensure that the appointment of substitute practitioners would be quick and uncontentious, thereby resulting in the efficient rescue and recovery of financially distressed companies.

On the issue as to whether an appointment by a court in terms of section 130(6)(a) of the Companies Act 2008 changed this position, the Constitutional Court held that there were numerous factors that militated against any such interpretation.

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325 *Shiva Uranium (Pty) Limited (in business rescue) and Another v Tayob and Others* [2021] ZACC 40 (9 November 2021).

326 *Tayob and Another v Shiva Uranium (Pty) Ltd and Others* (Case no 336/2019) [2020] ZASCA 162 (8 December 2020).

It is now clear what the law says in relation to the appointment of substitute practitioners, in the event that a practitioner dies, resigns or is removed from office. Depending on whether the business rescue is voluntary or compulsory, the substitute appointment will be made by the company or by the affected person who brought the business rescue application. It is also important to note that any function of a director that falls outside the ambit of the authority of the practitioner cannot be subject to the practitioner's approval – this would include the appointment of a substitute practitioner if the company was originally placed in business rescue voluntarily by board resolution. In addition, the Constitutional Court held that the board of directors of a company in business rescue retains all of its powers and functions, except to the extent that the Companies Act 2008 expressly or by necessary implication provides otherwise.

8.6 The remuneration of business rescue practitioners

The remuneration of a business rescue practitioner is dealt with expressly in section 143 of the Companies Act 2008, read with regulations 128, 127(2) and 26(2) of the Companies Regulations 2011.

The remuneration of the practitioner has three possible components, namely, an hourly fee or rate charged for each hour of work done, a success fee and the ability to recover costs incurred by the practitioner in performing his duties as a business rescue practitioner.

8.6.1 Hourly fees

In terms of section 143 the business rescue practitioner is entitled to charge the company for the remuneration and expenses incurred by the practitioner in accordance with the tariff prescribed by the Act.

The business rescue practitioner will charge for each hour worked in accordance with the prescribed tariff. This tariff is set in the Companies Regulations 2011 and is based on the size of the company being rescued. The tariff is set out in regulation 128 and prescribes the hourly rate and daily maximum that the practitioner will charge if the company is a small, medium or large company.

The basic remuneration of a business rescue practitioner is to be determined at the time of the appointment of the practitioner by the company, or the court, as the case may be, and may not exceed –

- R1,250 per hour (maximum of R15,625 per day) (inclusive of VAT) for a small company;
- R1,500 per hour (maximum of R18,750 per day) (inclusive of VAT) for a medium company; or
- R2,000 per hour (maximum of R25,000 per day) (inclusive of VAT) for a large company or a state-owned company.

To determine the size of the company, one needs to look at regulations 127(2) and 26(2) which provide us with the components of a company score and the score range that will determine if a company is small, medium or large. The score is calculated as follows:

- a number of points equal to the average number of employees of the company during the financial year (1 point per employee);
- 1 point for every R1 million (or portion thereof) in third party liability of the company, at the financial year end;
- 1 point for every R1 million (or portion thereof) in turnover during the financial year;
- 1 point for every individual who, at the end of the financial year, is known by the company –
  - in the case of a for-profit company, to directly or indirectly have a beneficial interest in any of the company's issued securities; or
  - in the case of a not-for-profit company, to be a member of the company, or a member of an association that is a member of the company.

If a company's score is below 100 points, it is classified as a small company; between 100 and 500 points, a medium-sized company; and a large company if its score is above 500.

8.6.2 Contingency (success) fees

A practitioner is, in addition to the hourly rates, entitled to propose or negotiate a contingency (success) fee with the company. The success fee however needs to be contingent on achieving a specific outcome, be that the adoption of a business rescue plan or achieving a particular result relating to the business rescue proceedings. An example of such a result would be the retention of a certain percentage of staff by the company, or achieving a minimum dividend distribution to creditors and / or shareholders.

This contingency agreement will only be binding if it is approved by (i) the holders of a majority of the creditors' voting interests, present and voting at a meeting called to consider the agreement; and (ii) the holders of a majority of the voting rights attached to any shares of the company that entitle the shareholder to a portion of the residual value of the company on winding-up, present and voting at a meeting called for the purpose of considering the proposed agreement.[327]

Any creditor who votes against such an agreement may make application to court, within 10 business days after the date on which a vote was taken, for an order setting aside the proposed agreement on the basis that the agreement is not just and equitable or not reasonable having regard to the financial circumstances of the company.

[327] Companies Act 2008, s 143(3).

If the company and the practitioner reach agreement on a success fee, that fee becomes binding on the company, and enforceable by the business rescue practitioner.

It is worth noting that the Supreme Court of Appeal has made it clear in the judgment in *Caratco (Pty) Ltd v Independent Advisory (Pty) Ltd*[328] that it is not illegal or in contravention of the Companies Act 2008 for a business rescue practitioner to be paid a success fee by a third party outside the confines of section 143 of the Companies Act. In this case, the business rescue practitioners agreed with a third party, related[329] to the company in business rescue, that the company of which the business rescue practitioners were directors would be paid a success fee. However, business rescue practitioners should be aware that the Supreme Court of Appeal's findings regarding whether the agreement in this case was against public policy, was case specific and every matter will be decided on its own facts.

The success fee of a practitioner is one of the possible conflicts that can arise in business rescue. The statutory fees applicable to the business rescue practitioner are relatively low when compared to the hourly rates of similarly qualified professionals. Whether by design or due to the fact that the statutory rate has not been updated since the Act was promulgated, it has become common practice for business rescue practitioners to negotiate a higher hourly fee and an additional success fee. The success fee itself is often a lump sum or a percentage of the amount realised for or paid to the employees, creditors and shareholders of the company.

This form of arrangement is perfectly acceptable, provided that a simple majority of the creditors and shareholders endorse this additional fee in terms of section 143(3) of the Companies Act 2008, or by adopting the business rescue plan which includes the success fee. The above process is ethically sound given that creditors and shareholders are afforded an opportunity to vote against the proposal.

Business rescue practitioners must however be careful to structure their success fees in such a way as to eliminate a conflict between their own personal interests and those of the affected persons (creditors, employees and shareholders). When business rescue practitioners are incentivised to benefit from higher values being achieved, or certain targets being achieved, this could take care of these potential conflicts.

An inherent personal conflict may arise in this context, however, as the business rescue practitioner's fee is often tied to the success of the rescue and he or she may be reluctant to end the rescue proceedings and place the entity into liquidation given the personal financial implications that flow form such action.

A further ethical conflict will arise when a business rescue practitioner, as part of their remuneration, would be entitled to equity in the company (that is, equity in the business they are rescuing. By way of example, a business rescue practitioner would endeavour to compromise all creditors to ensure that when the company comes out of rescue, it has no liabilities and only assets. From an ethical and conflict perspective, a mandate which entitles

[328] Case No 982/18) [2020] ZASCA 17.
[329] See the definition of "related" in the Companies Act 2008, s 1.

business rescue practitioners to earn and own equity in a company post rescue can and usually will create an ethical dilemma and conflict for a business rescue practitioner. In this scenario, it is in the business rescue practitioner's interests to compromise and eliminate liabilities and preserve value and assets. This would add value to the equity they are entitled to in direct conflict to the interests of employees and creditors. It is recommended that business rescue practitioners should avoid this type of conflict as it will, on regular occasions, test the practitioners' ethical values.

8.6.3 Disbursements and cost recovery

In addition to remuneration, a practitioner is also, in terms of section 143(1) of the Companies Act 2008, read with Regulation 138(3) of the Companies Regulations 2011, entitled to be reimbursed for the actual costs of any disbursements incurred by the business rescue practitioner, or expenses incurred by the business rescue practitioner, to the extent reasonably necessary to carry out the practitioner's functions and to facilitate the conduct of the company's business rescue proceedings.[330]

In terms of section 135(3), the business rescue practitioner's remuneration and expenses will, in a business rescue, rank ahead of employees with post-commencement claims for any remuneration, reimbursement for expenses or other amount of money relating to employment, and ahead of post-commencement financiers.

In addition, the Supreme Court of Appeal, in *Diener NO v Minister of Justice and Others*[331] and the Constitutional Court thereafter, in the case of *Diener NO v Minister of Justice and Correctional Services and Others*[332] (the *Diener* judgments), had regard to the ranking of the business rescue practitioner's fees in an instance where business rescue proceedings had been converted into liquidation proceedings.

The Supreme Court of Appeal held that section 135(4) provides the business rescue practitioner, after the conversion of business rescue proceedings into liquidation proceedings, with no more than a preference in respect of his or her remuneration (and presumably also expenses) to claim against the free residue of the insolvent estate after the costs of liquidation but before the post-commencement claims of employees and unsecured post-commencement financiers. The Constitutional Court concluded at paragraph 71 of its judgment that there is no "…basis on which to interfere with the order of the Supreme Court of Appeal".

The ranking of claims is dealt with in more detail in Chapter 5 above.

8.7 The general powers and duties of business rescue practitioners

The general powers and duties of the business rescue practitioner are not specified in any one section of the Companies Act 2008, but rather almost every section of Chapter 6 makes

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[330] *Murgatroyd v Van den Heever NO and Others* 2015 (2) SA 514 (GJ) (29 July 2014).
[331] 2018 (2) SA 399 (SCA).
[332] 2019 (2) BCLR 214 (CC).

reference to specific duties or powers. There are additional duties contained in the Companies Regulations 2011 that must not be overlooked.

An example of this is the requirement a that a business rescue practitioner notify affected persons of each court proceeding, decision, meeting or other relevant event concerning the business rescue proceedings. These obligations are set out in sections 144(3)(a), 145(1)(a) and 146(a) of the Companies Act, which must be read in conjunction with regulation 125(2) of the Companies Regulations 2011, and which stipulates how that notice is to be published.

The business rescue practitioner is responsible for developing a business rescue plan to be considered at a meeting convened in terms of section 151, and to implement any business rescue plan that has been adopted in terms of section 152.[333] In fact, our Courts have held that The formulation of a business rescue plan is the central task of the business rescue practitioner and that it must be developed with the greatest expedition.[334]

However, section 150, read with sections 144, 145 and 146, imposes an additional duty on the business rescue practitioner to consult with employees, trade unions, creditors and shareholders before doing so. This was confirmed by the courts in *Hlumisa Investment Holdings (RF) Ltd and Another v Van der Merwe NO and Others*[335] where the shareholders successfully interdicted the meeting to consider the business rescue plan on the basis that the business rescue practitioners had not consulted shareholders prior to publishing the proposed business rescue plan.

Some of the other duties are discussed in later sections, but include the duty to:

- publish monthly progress reports on the business rescue proceedings if the proceedings last for more than three months;[336]
- ensure that the company protects the interests of creditors that hold a security or title interest over any property;[337]
- notify regulatory authorities of the commencement of business rescue proceedings and that they have been appointed;[338]
- the duties and liabilities of a director as set out in sections 75 to 77 of the Act;[339]

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333 Companies Act 2008, s140(1)(d). See Ch 10 below for a full discussion of the development of a business rescue plan.
334 *South African Airways (SOC) Limited (in business rescue) and Others v National Union of Metalworkers of South Africa obo Members and Others* 2021 (2) SA 260 (LAC) (9 July 2020).
335 (77351/2015) [2015] ZAGPPHC 1055 (14 October 2015).
336 Companies Act 2008, s 132(3).
337 *Idem*, s 134(3).
338 *Idem*, s 140(1A).
339 *Idem*, s 140(3).

- investigate the affairs of the company;[340]

- notify affected persons of each court proceeding, decision, meeting or other relevant event concerning the business rescue proceedings;[341]

- determine if a creditor is independent and appoint a suitably qualified person to determine the participation rights of subordinated creditors and notify those creditors of the determinations;[342]

- convene and preside over a first meeting of creditors within 10 business days of being appointed and at the meeting to confirm that the business rescue practitioner believes that there is a reasonable prospect of rescuing the company;[343]

- give notice of the first meeting to every creditor of the company whose name and address is known or can reasonably be obtained;[344]

- convene and preside over a first meeting of employees within 10 business days of being appointed and at the meeting to confirm that the business rescue practitioner believes that there is a reasonable prospect of rescuing the company;[345]

- give notice of the first meeting to every employee and registered trade union representing employees of the company;[346]

- consult with affected persons prior to publishing a proposed business rescue plan;[347]

- ensure that the proposed business rescue plan contains the minimum prescribed information;[348]

- convene a meeting to consider the proposed business rescue plan within 10 business days of publication of that plan and publish notice of that meeting to all affected persons within five days of that meeting;[349]

- preside over the meeting to consider the business rescue plan and at that meeting to introduce the business rescue plan, inform the meeting whether the business rescue practitioner continues to believe that there is a reasonable prospect of the company being rescued, invite discussion on the proposed business rescue plan, entertain motions to

[340] *Idem*, s 141.
[341] *Idem*, ss 144(3), 145(1)(a) and 146(a).
[342] *Idem*, s 145.
[343] *Idem*, s 147(1).
[344] *Idem*, s 147(2).
[345] *Idem*, s 148(1).
[346] *Idem*, s 148(2).
[347] *Idem*, s 150, read with ss 144, 145 and 146.
[348] *Idem*, s 150(2).
[349] *Idem* s 151.

amend the proposed business rescue plan or to adjourn the meeting to further revise the plan and call for a vote for approval of the proposed business rescue plan;[350]

- direct the company to take the necessary steps to satisfy any conditions on which the business rescue plan is contingent and to implement the plan as adopted;[351]

- entertain motions requiring the practitioner to prepare and publish a revised plan where the proposed plan was rejected;[352]

- file a notice of termination of business rescue proceedings if a plan is rejected and neither the practitioner nor an affected person successfully takes any of the allowed steps to prolong the proceedings.[353]

The governing principle regarding management of the day to day affairs of the company is that the business rescue practitioner has full management control of the company[354] and the directors must assist the practitioner and act in accordance with the business rescue practitioner's instructions.[355]

Additionally, section 137(2)(b) of the Companies Act 2008 provides that during a company's business rescue proceedings, "each director of the company has a duty to the company to exercise any management function within the company in accordance with the express instructions or direction of the practitioner, to the extent that it is reasonable to do so". In fact, section 137(3) goes further and states that "[d]uring a company's business rescue proceedings, each director of the company must attend to the requests of the practitioner at all times, and provide the practitioner with any information about the company's affairs as may reasonably be required". Section 137(4), on the other hand, provides that if, during a company's business rescue proceedings, the board, or one or more directors of the company, purports to take any action on behalf of the company that requires the approval of the practitioner, that action is void unless approved by the practitioner.

If at any time during the business rescue proceedings, a director has –

- failed to comply with a requirement of Chapter 6; or

- by act or omission, has impeded, or is impeding –

    - the practitioner in the performance of the powers and functions of practitioner;

    - the management of the company by the practitioner; or

[350] *Idem*, s 152(1).
[351] *Idem*, s 152(5).
[352] *Idem*, s 153(1)(b)(i)(aa).
[353] *Idem*, s 153(5).
[354] *Idem*, s 140(1)(a).
[355] *Idem*, s 137(2), (3).

- the development or implementation of a business rescue plan in accordance with this Chapter 6 of the Act,

then the business rescue practitioner may, in terms of section 137(5) of the Companies Act 2008, apply to a court for an order removing a director from office and may apply to have a director declared delinquent in terms of section 137(6) read with section 162.

In the Supreme Court of Appeal judgment of *Tayob and Another v Shiva Uranium (Pty) Ltd and Others*,[356] confirmed by the Constitutional Court in *Shiva Uranium (Pty) Limited (in business rescue) and Another v Tayob and Others*,[357] the courts deal with the question of the role of a company's board of directors during the business rescue process. In this regard, the Supreme Court of Appeal and the Constitutional Court confirmed that there is a distinction made between "management functions" and "functions of governance", The former being within the scope of the business rescue practitioner's powers, whilst the latter remained in the domain of the company's board of directors. The courts further confirmed that any function of a director that falls outside the ambit of the authority of the practitioner, cannot be subject to the practitioner's approval.

In the judgment of *Ragavan and Others v Optimum Coal Terminal (Pty) Ltd NNO and Others*,[358] the High Court dealt with the interplay or "rules of engagement" between business rescue practitioners and the company's board. The judgment hinged on the concept of "internal vs external" functions, whereby governance functions (or functions that are internal in nature), for instance presenting annual financial statements, issuing shares, scheduling shareholders' meetings, proposing resolutions, holding board meetings and (per the Constitutional Court, appointing substitute business rescue practitioners), are retained by directors during the course of business rescue proceedings. On the other hand, external functions, which involve interactions with the outside world and that concern management powers (including voting at section 151 meetings) are conferred upon business rescue practitioners, pursuant to the provisions of Chapter 6 of the Companies Act 2008.

Therefore, whilst business rescue practitioners are responsible for all external functions of the company, which involve interactions with the outside world and those functions that concern management powers, directors still have a role to play in the business rescue context. Accordingly, an important lesson to be learnt is that directors are not completely absolved from actively fulfilling their fiduciary duties once a company is placed in business rescue, in view of the fact that their powers are not totally relinquished to business rescue practitioners during the business rescue process.

The business rescue practitioner also has the power to:

- approve the sale of property in a *bona fide* arm's length transaction;[359]

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[356] [2020] ZASCA 162 (8 December 2020).
[357] [2021] ZACC 40 (9 November 2021).
[358] [2022] ZAGPJHC 14 (18 January 2022).
[359] Companies Act 2008, s 134(1)(a)(i).

- entirely, partially or conditionally suspend, for the duration of the business rescue proceedings, any obligation of the company that arises or will become due in terms of a contract or agreement that exists at commencement of proceedings;[360]

- remove a director by application to court;[361]

- seek approval, if a business rescue plan is rejected, to prepare and publish a revised plan;[362]

- apply to court to set aside the result of the vote of creditors or shareholders against adoption of the proposed business rescue plan on the grounds that it was inappropriate.[363]

In addition to the above powers and duties the business rescue practitioner has an overarching obligation to act ethically, honesty and with the highest level of integrity. This is explored in more detail below.

8.8 The investigation of the affairs of a company by the practitioner

A business rescue practitioner has a duty to investigate the company's affairs, business, property and financial situation as soon as practicable after being appointed.[364] The main aim of this is to establish and continue to assess whether there is a reasonable prospect of rescuing the company. This seems logical and simple enough as the practitioner will require a thorough and detailed understanding of the business and affairs of the company in order to properly prepare a business rescue plan and conclude that there is a reasonable prospect of rescue.

The investigation normally starts prior to commencement and appointment as the business rescue practitioner should do an assessment of whether the company is a candidate for rescue prior to accepting an appointment. The practitioner will at this stage review information and engage with the directors and management to understand if and why the company is distressed and what has caused this distress.

The investigations necessarily continue throughout the business rescue process as the practitioner becomes acquainted with the company, its assets, its operations and liabilities. It is these investigations that allow the practitioner to comply with the requirements of section 150 of the Act and ensure that the business rescue plan contains the required information.

Section 141(2) places an onus on business recue practitioners to regularly or continuously assess whether there is a reasonable prospect of rescuing the company. It is important not to overlook the interplay between this requirement and the obligations place on a practitioner to confirm that there is a reasonable prospect of rescue at the first meeting of creditors and the meeting to consider the proposed plan. To make the statement without having investigated or commenced

[360] *Idem*, s 136(2)(2A).
[361] *Idem*, s 137(5).
[362] *Idem*, s 153(1)(a)(i).
[363] *Idem*, s 153(1)(a)(ii).
[364] *Idem*, s 141(1).

the investigations required in terms of section 141, will at best be a breach of office as contemplated in section 139(2)(a) and (b), and at worst be considered reckless. A business rescue practitioner who no longer believes that the company can be rescued, must inform all affected persons, the company and the court and must apply for the proceedings to be converted into liquidation proceedings.[365] If the business rescue practitioner concludes that the company is no longer financially distressed, steps must be taken to terminate the proceedings.[366]

Many creditors extrapolate the implied mandate created by section 141(2)(c) and conclude that the investigations should be solely focussed on identifying voidable transactions, the failure by the company or any director to perform any material obligation in relation to the company, reckless trading, fraud or the contravention of any laws. While this is one aspect of the investigations, it is not the main focus of these investigations which is to establish and confirm that there is a reasonable prospect of rescuing the company.[367]

A business rescue practitioner who finds such evidence is required to take steps to rectify the matter, direct management to take appropriate steps including to recover any misappropriated assets of the company.[368] The practitioner is also required to forward evidence to the relevant authority for further investigation,[369] but is curiously not required to include or report the irregularities in a proposed business rescue plan unless the recovery of misappropriated assets constitutes property that is to be available to pay creditors claims.[370]

When discharging the obligation to investigate the affairs of the company, business rescue practitioners must remain independent. This despite the fact that business rescue practitioners will often be investigating the very board that appointed them and the team they are working with to rescue the company. The relationships that form during the pre-rescue investigations and during the process cannot be allowed to influence judgement or create bias in this investigation.

The obligation to convert the proceedings to liquidation or terminate proceedings can create another ethical test for business rescue practitioners who must put their personal interests to one side and act strictly as they are obliged to by the provisions of the act.

8.9 Directors of the company and their duty to co-operate with and assist practitioner

Directors remain directors whilst the company is in business rescue, retain their duties of care towards the company and are obliged to assist the practitioner throughout the process.

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[365] *Idem*, s 141(2)(a).
[366] *Idem*, s 141(2)(b).
[367] *Idem*, s 141(1).
[368] *Idem*, ss 141(3)(c)(i) and 141(c)(ii)(bb).
[369] *Idem*, s 141(3)(ii)(aa).
[370] *Idem*, s 150(2)(b)(iv).

As mentioned above in paragraph 8.7, the Companies Act 2008 and case law provides guidance on the differing roles of a business rescue practitioner as opposed to a director during business rescue proceedings.

During business rescue a director must continue to exercise the functions of a director and has a duty to the company to exercise any management function within the company in accordance with the express instructions and direction of the practitioner.[371] The above-mentioned obligations are reinforced in section 137(3), which repeats directors obligations to always attend to the requests of the business rescue practitioner, and to provide the business rescue practitioner with any information about the company's affairs as may be reasonably required. These provisions are clearly designed to try and ensure that the practitioner has access to information and the support of the directors during the business rescue process.

In addition to what has already been dealt with above in paragraph 8.7, section 142 of the Companies Act 2008 obliges directors to disclose information to a practitioner and provides that a practitioner has full access to all of the company's books and records. These obligations are onerous as the directors must, within five days of commencement of business rescue proceedings, provide the practitioner with a statement of affairs containing at a minimum the following information:

- material transactions that took place in the 12 months preceding the business rescue proceedings;
- all court, arbitration, enforcement or administrative proceedings involving the company;
- the assets and liabilities of the company including the obligations of debtors to the company and any rights that creditors may have against the company;
- the company's income and disbursements for the 12 months preceding the business rescue proceedings; and
- the number of employees, details of collective agreements or other agreements relating to the rights of employees.

As mentioned in paragraph 8.7 above, the courts have confirmed that the provisions of sections 137 and 142 do not conflict with those of section 140, which confer full management control of the company on the business rescue practitioner in substitution for its board and pre-existing management. Rather, the two sections work together to provide powers to the practitioner and place obligations on the directors in respect of their roles. The courts have confirmed that the directors retain certain internal (governance) powers, whereas the business rescue practitioner has external (management) powers.

[371] *Idem*, s 137(2)(a) and (b).

8.10 Ethics and the business rescue practitioner

Given the importance of the functions and duties of business rescue practitioners, coupled with the fact that they are officers of the court,[372] act in a fiduciary relationship to the company[373] and, because the practitioner must balance the rights and interests of all affected persons,[374] ethics should and does play a major role when business rescue practitioners discharge their duties and obligations as such.

The business rescue provisions set out in Chapter 6 of the Companies Act 2008 contain certain limited provisions which require ethical standards and high levels of honesty by business rescue practitioners. These provisions oblige business rescue practitioners to adhere to a set of ethical standards and provide for sanctions or removal if certain minimum standards are not met. The applicable jurisprudence indicates that the courts are uncompromising in their endorsement of the high ethical standard required of business rescue practitioners.[375]

The wording of section 140(3)(b) provides that the office of a business rescue practitioner carries with it the responsibilities, duties and liabilities of a director. Section 76 of the Companies Act 2008 has now codified most (but not all) of the common law duties of directors, as follows:

> "**76. Standards of directors conduct.**
> (3) Subject to subsections (4) and (5), a director of a company, when acting in that capacity, must exercise the powers and perform the functions of director–
> (a) in good faith and for a proper purpose;
> (b) in the best interests of the company; and
> (c) with the degree of care, skill and diligence that may reasonably be expected of a person–
> (i) carrying out the same functions in relation to the company as those carried out by that director; and
> (ii) having the general knowledge, skill and experience of that director."

The judgement in the *Knoop* case[376] indicates that whilst a business rescue practitioner does not become a director, there can be no doubt that business rescue practitioners are required to behave ethically and with a high level of integrity, honesty, skill and diligence in discharging their duties. Further, the full bench in the case of *Van Den Heerden NO and Others v Van Tonder*[377] held that taking into consideration the context of Chapter 6, and specifically the

[372] *Idem*, s 140(3)(a).
[373] *Idem*, s 140(3).
[374] *Idem*, s 7(k).
[375] *Knoop and Another v Gupta and Another* All SA 726 (SCA); *African Banking Corporation of Botswana Ltd v Kariba Furniture Manufacturers (Pty) Ltd and Others,* 2015 (5) SA 192 (SCA); *CSARS v Louis Pasteur Investments (Pty) Ltd* (12194/17) [2021] ZAGPPHC 89 (4 March 2021)*; and EBM Project (Pty) Ltd and Another v Barak Fund SPC Ltd In re: The Holland Insurance Company Ltd v The Master of the High Court and Others* (2021/18884) [2021] ZAGPJHC 384 (14 June 2021).
[376] *Knoop and Another v Gupta and Another* All SA 726 (SCA).
[377] (A5076/2018; 407461/2015) [2021] ZAGPJHC 486 (20 April 2021).

intention of the legislature to afford business rescue practitioners tailor-made protection when they perform their duties as business rescue practitioners, the words "other than" in section 140(3)(c), were in the court's view intended to mean that apart from the liabilities which a business practitioner may incur in terms of section 77, business rescue practitioners will also be liable if they fails to perform their duties as business rescue practitioners in the circumstances set out in 140(3)(c)(ii) of the Companies Act 2008. The duties of a business rescue practitioner would for instance include the failure to convene meetings or to develop or implement the business rescue plan, or a failure to report to the creditors and other affected parties.

8.10.1 *Accepting an appointment*

One of the more important ethical considerations that arises in business rescue is what a business rescue practitioner should do if at the pre-business rescue assessment stage it becomes apparent that the business rescue will not be a traditional rescue, but rather an alternative rescue (or wind down). In the latter instance, the entity is put into business rescue solely for the purpose of realising a better outcome for creditors and employees than in a liquidation, and is the alternative aim or purpose of business rescue as defined.

If business rescue practitioners are not reasonably certain that the wind-down will be successful (that is, that a higher distribution than a liquidation dividend can be achieved) and will not devolve into a traditional liquidation during business rescue, they should not take the appointment. However, if a return to solvency is not possible but a wind-down in business rescue can achieve a higher distribution for creditors than what would have been achieved in a liquidation, then there is nothing wrong with accepting such an appointment given that an alternative rescue is recognised by section 128(1)(b)(iii) of the Companies Act 2008.

Certainly, in reaching any decision in this regard, business rescue practitioners must act solely in the interests of affected persons and the company. They must have no regard to their personal position or potential to earn fees by taking the appointment. This is the ethical duty business rescue practitioners will have to discharge.

8.10.2 *Personal financial interests*

The Companies Act 2008 is clear that a person should not accept an appointment as a business rescue practitioner of a company if they are not independent of the company. The wording of section 138(1)(e) reinforces the notion that a business rescue practitioner is expected to uphold only the highest ethical standards, as the provision requires that a business rescue practitioner of a company must not have any other relationship with the company such as would lead a reasonable and informed third party to conclude that the integrity, impartiality or objectivity of that person is compromised by that relationship.

The inclusion of a reference in section 140(3)(b) to section 75 (which deals with directors personal financial interest and conflicts and how to deal with such conflicts) seems superfluous. It appears that the purpose of this repetition is to ensure that when business rescue practitioners deal with the business of a company and the sale of its assets or business, they must avoid any

form of conflict in the sense that they must not act in a manner in which they personally gain or family members or friends personally gain in the matter to the detriment of the company and / or affected persons.

8.10.3 Balancing rights of all affected persons

Section 7(k) sets out one of the purposes of the Companies Act 2008, which is to provide for the efficient rescue and recovery of financial distressed companies, in a manner that balances the rights and interest of all relevant stakeholders. Whilst this obligation is clear, in practice it can become quite difficult to achieve.

An example of a difficult situation that often arises is where the sponsor to a rescue dictates the terms of the funding that is to be provided or the terms of the business rescue. These terms might favour the sponsor over employees and other creditors, but without such funding the entity may not be saved and many employees' jobs lost as result. One can also imagine how difficult it would become at times to balance the interests of shareholders with those of employees and creditors.

This is another example of why a practitioner will always need to act with integrity, honesty and high ethical standards.

Self-Assessment Questions for Chapter 8

Where necessary, refer to the Case Study in Chapter 1 of these notes when answering the questions below.

Question 1

It was discovered that Mr V bad, unbeknown to the board, was found guilty in disciplinary proceedings brought against him by the professional body to which he belonged, with the result that his membership was revoked. On the basis that Mr V Bad was no longer a member in good standing of a legal, accounting or business management profession accredited by the CIPC, and as such, Mr V Bad was removed as the business rescue practitioner of Fast Flights and was replaced by Mr A Float, following certain court processes.

How, by whom and on what grounds, with reference to statute and case law, was Mr V Bad removed from his position as business rescue practitioner of Fast Flights? Who would have been entitled to replace Mr V Bad with Mr A Float?

Question 2

Mr A Float requested Ms C Clerk to furnish him with a brief legal opinion, setting out the pertinent provisions of the Companies Act 2008 relating to the remuneration of business rescue practitioners, as he wanted to know whether the amounts he had been earning to date were in accordance with the Companies Act.

How will Mr A Float's remuneration be calculated and agreed? On what basis, with reference to case law, can Mr A Float agree a contingency fee, and with whom?

Question 3

Mr A Float published a business rescue plan which was approved by the requisite majority of creditors' voting interests and proceeded to implement the business rescue plan. The business rescue proceedings of Fast Flights continued over a protracted period of time but, despite this, Mr A Float was of the view that it would be completely unnecessary to report on the progress of the business rescue proceedings, given that to do so would be very onerous.

With reference to case law and statute, and the standard of conduct expected of a business rescue practitioner, is Mr A Float's obligations in the business rescue of Fast Flights being fulfilled? You are also required to express a considered view on whether or not a court will likely order the removal of Mr A Float.

Question 4

After the business rescue proceedings of Fast Flights had gone on for 18 months, it became apparent that Fast Flights was un-rescuable, despite the best efforts of Mr A Float and the board of directors. Consequently, Mr A Float began exploring the different avenues in terms of which the business rescue proceedings of Fast Flights could be terminated. He engages a firm of attorneys to explore ways in which to exit the business rescue process and to place Fast Flights into liquidation. The firm of attorneys furnish him with legal advice.

The board of Fast Flights does not, however, agree with the advice given to Mr A Float and demand from Mr A Float that he follows their instructions. What powers does Mr A Float have in the business rescue of Fast Flights, as compared with the powers of the board?

For feedback on this self-assessment exercise, see the document "Comment and Feedback on Self-Assessment Questions", which is made available to you as a separate document.

CHAPTER 9

PARTICIPATION BY CREDITORS

9.1 The rights of and the participation by creditors in the business rescue process

9.1.1 General

Whilst the rights of affected persons, including creditors, are dealt with throughout Chapter 6 of the Companies Act 2008, section 145 provides specifically for the participation by creditors in the business rescue process. It explains their rights and entitlements in general terms. Section 145 also seeks to provide clarity in regard to the voting rights of each creditor. This is critical as a creditor's ability to participate in and influence decisions made during the business rescue process will depend on his right to vote and the magnitude of his voting interest in relation to other creditors.

Creditors play a critical role in the business rescue process. In particular, they determine whether any business rescue plan will be accepted or rejected, with shareholders[378] having a say in this regard only where the business rescue plan contemplates altering their rights.[379]

The business rescue practitioner must prepare a business rescue plan only after consulting with creditors (and other affected persons).[380] Aside from the fact that the creditors have the right to be consulted, the business rescue practitioner will want to know whether the plan that he intends publishing will enjoy the support of the larger creditors. Without this support, the plan is unlikely to be approved. Early and ongoing engagement with creditors is therefore sensible. A business rescue process where creditors are engaged and collaborative is generally more likely to succeed.

9.1.2 Notification

Section 145(1)(a) of the Companies Act 2008 provides that every creditor is entitled to notice of each court proceeding, decision, meeting or other relevant event concerning the business rescue proceedings. In addition, many provisions in Chapter 6 of the Companies Act 2008 specifically require notice to be given to creditors. By virtue of section 145(1)(a) the notice requirement must be observed, even where a provision does not specifically call for notice to be given.

In relation to court proceedings, the requirement to give notice to creditors does not necessarily mean that they must be joined to those proceedings.[381]

[378] More specifically, the holders of any class of the company's securities.
[379] Companies Act 2008, s 152(3).
[380] *Idem*, s 150(1).
[381] *Timasani (Pty) Ltd (in business rescue) and Another v Afrimat Iron Ore (Pty) Ltd* [2021] 3 All SA 843 (SCA), at para 19.

The courts have confirmed that the notice requirement in section 145 is prescriptive.[382] Notice to creditors is a jurisdictional fact which must be satisfied.[383] Consequently, any conduct that has the effect of preventing participation of affected persons is unlawful as it defeats their express statutory rights.[384] The courts have therefore held that it is not permissible for a business rescue practitioner to approach a court on an *ex parte* basis and without compliance with notification requirements.[385] Such an application must fail purely on the basis of the failure to give notice.[386] The notice requirement in section 145(1)(a) is regulated by regulation 125(2) of the Companies Regulations 2011. This prescribes that the business recue practitioner must give notice to creditors by:

- either:
  - delivering a copy of the notice to each creditor in accordance with regulation 7 of the Companies Regulations 2011; or
  - informing each creditor of the availability of a copy of the notice, in the manner contemplated in section 6(11)(b)(ii) of the Companies Act 2008 and regulation 6 of the Companies Regulations 2011; and
- conspicuously displaying a copy of the notice:
  - at the registered office of the company, the principal places of conducting the business activities of the company and any workplace where employees of the company are employed;
  - on any website that is maintained by the company and intended to be accessible by affected persons; and
  - if it is a listed company, on any electronic system maintained by the relevant exchange for the communication and inter-change of information by and among companies listed on that exchange.

If the business rescue practitioner elects to deliver the notice to a creditor in accordance with regulation 7 of the Companies Regulations 2011, it may be delivered:

- as contemplated in section 6(10) or (11) of the Companies Act 2008; or
- as set out in Table CR 3 of the Companies Regulations 2011.[387]

[382] *EBM Projects (Pty) Ltd and Another v Barak Fund SPC Ltd; In re: The Hollard Insurance Company Ltd v The Master of the High Court and Others* (2021/18884) [2021] ZAGPJHC 384 (14 June 2021), at para 43.
[383] *Idem,* at para 44.
[384] *Idem*, at para 48.
[385] *Idem*, at para 49.
[386] *Idem*, at para 53.
[387] Companies Regulations 2011, reg 7(1).

Alternatively, if the business rescue practitioner elects to give notice by informing each creditor of the availability of a copy of the notice in the manner contemplated in section 6(11)(b)(ii) of the Companies Act 2008 and regulation 6 of the Companies Regulations 2011, the following is relevant:

- The notice announcing the availability of a document is required to be in writing and delivered to each intended recipient in paper form at the intended recipient's last known delivery address, alternatively, electronically at their last known electronic mail address.[388]

- The notice is required to clearly stipulate the title of the document being made available, the extent of the period during which the document will remain available, and the manner in which the recipient may obtain the document.[389]

- The notice must include a statement that succinctly summarises the purpose of the document.[390]

- The document (the availability of which is being announced) must be made available to the intended recipients either in paper copy or electronically in a form that can easily be accessed and printed within a reasonable time and at a reasonable cost.[391]

9.1.3 Participation in any court proceedings

Section 131(3) of the Companies Act 2008 provides that each affected person has a right to participate in the hearing of an application to court by any other affected person for an order placing the company under supervision and commencing business rescue proceedings.

Once business rescue proceedings have commenced, there are various provisions in Chapter 6 of the Companies Act 2008 that provide for the right of creditors to participate in specific legal proceedings. In addition, section 145(1)(b) makes provision for a general right of creditors to participate in any legal proceedings that arise during the business rescue process.

The right to participate in legal proceedings is the same, whether specifically provided for in a section in Chapter 6 of the Companies Act 2008, or whether a creditor relies on the general right in section 145(1)(b).[392] The principles applicable to the right of affected persons to participate in legal proceedings under section 131(3) are also equally applicable to the general right provided for in section 145(1)(b).[393] In both instances the leave of the court to intervene in the

[388] *Idem*, reg 6(1)(a)(i) and (ii).
[389] *Idem*, reg 6(1)(b)(i) to (iii).
[390] *Idem,* reg 6(1)(c).
[391] *Idem*, reg 6(2)(a) and (b).
[392] See Henochsberg 526(74F).
[393] *Idem*, at 526(75) and *Timasani (Pty) Ltd (in business rescue) and Another v Afrimat Iron Ore (Pty) Ltd* [2021] 3 All SA 843 (SCA), at para 18.

proceedings is not required. However, the court may need to regulate the procedure to be followed if a creditor wishes to file affidavits.[394]

It must be noted that the right of creditors to participate in legal proceedings does not give rise to the requirement that creditors be joined in all litigation.[395] Joinder only becomes necessary where the legal proceedings relate to an approved business rescue plan or otherwise directly affect creditors' rights.[396]

9.1.4 Formal and informal participation in the business rescue proceedings

Whilst section 145(1)(c) provides that each creditor is entitled to formally participate in a company's business rescue proceedings to the extent provided for in Chapter 6 of the Companies Act 2008, section 145(1)(d) provides that each creditor is also entitled to participate informally in those proceedings by making proposals for a business rescue plan to the business rescue practitioner.

Accordingly, it is recognised that participation may also take place in a less formal manner by way of approaches to the business rescue practitioner specifically to make proposals regarding the business rescue plan that he is required to prepare. It would self-evidently be very useful for major creditors to approach the business rescue practitioner with proposals that those creditors support. If any such proposal meets with the business rescue practitioner's approval, it can be incorporated in a business rescue plan.

Every business rescue plan is required to include a statement recording whether it includes a proposal made informally by a creditor.[397]

9.1.5 Rights in the adoption of the business rescue plan

Section 145(2) provides that in addition to the rights set out in section 145(1), each creditor has:

- the right to vote to amend, approve or reject a proposed business rescue plan (in the manner contemplated in section 152 of the Companies Act 2008); and
- if the proposed business rescue plan is rejected, a further right to:
    - propose the development of an alternative plan (in the manner contemplated in section 153 of the Companies Act 2008); or

[394] *Timasani (Pty) Ltd (in business rescue) and Another v Afrimat Iron Ore (Pty) Ltd* [2021] 3 All SA 843 (SCA), at para 18.
[395] *Idem*, at para 19.
[396] See the discussion in para 9.3 in this regard below.
[397] Companies Act 2008, s 150(2)(a)(vi).

- present an offer to acquire the interests of any or all of the other creditors (in the manner contemplated in section 153 of the Companies Act 2008).

9.1.6 Creditors' committee

Section 145(3) of the Companies Act 2008 provides that the creditors of a company are entitled to form a creditors' committee, and through that committee are entitled to be consulted by the business rescue practitioner during the development of the business rescue plan.

The appointment of the creditors' committee is regulated by section 147(1)(a). At the first meeting of creditors they must determine whether or not a committee should be appointed and if so, they may appoint the members of that committee.[398]

The functions, duties and membership of the committee are provided for in section 149 of the Companies Act 2008. The committee:

- may consult with the business rescue practitioner about any matter relating to the business rescue proceedings, but may not direct or instruct the business rescue practitioner;

- may, on behalf of the general body of creditors, receive and consider reports relating to the business rescue proceedings; and

- must act independently of the business rescue practitioner to ensure fair and unbiased representation of creditors' interests.

A person may be a member of a committee of creditors or employees, respectively, only if the person is:

- an independent creditor of the company;

- an agent, proxy or attorney of an independent creditor, or other person acting under a general power of attorney; or

- authorised in writing by an independent creditor to be a member.

If reference is had to section 149, it is clear that the committee has limited power. In particular, it may not direct or instruct the business rescue practitioner in any way. However, properly utilised, a creditors' committee can be very valuable to both the general body of creditors and the business rescue practitioner. It is able to provide an effective means of communication between the business rescue practitioner and the larger body of creditors. This is particularly so when a large number of creditors is involved. The creditors' committee can channel queries and concerns to the business rescue practitioner to prevent the business rescue practitioner being inundated with calls and correspondence. The business rescue practitioner can also use the

[398] *Idem*, s 147(1)(b).

committee to communicate progress in the business rescue process and to understand the concerns common to many of the creditors.

It is important to note that the existence of a creditors' committee does not preclude creditors from engaging with the business rescue practitioner individually should they wish to do so. Additionally, queries or concerns that are related to a particular creditor or small group of creditors only should not be channeled through the creditors' committee. Instead, the committee should deal primarily with issues that concern the wider body of creditors.

9.1.7 *Creditors' voting interests*

Many decisions to be made in the course of business rescue proceedings are made on the basis of a vote by creditors. It is therefore critical that each creditor is aware of and afforded the voting interest to which it is entitled.

Section 128(1)(j) contains a definition of "voting interest". It defines it as "an interest as recognized, appraised and valued in terms of section 145(4) to (6)".

Section 145(4) of the Companies Act 2008 explains how a creditor's voting interest is determined. It stipulates that a:

- secured or unsecured creditor has a voting interest equal to the value of the amount owed to that creditor by the company; and

- concurrent creditor who would be subordinated in a liquidation has a voting interest, as independently and expertly appraised and valued at the request of the business rescue practitioner, equal to the amount, if any, that the creditor could reasonably expect to receive in such a liquidation of the company.

Both secured and unsecured creditors have a vote equal to the value of the amount owed to them by the company. The only exception to this is "a concurrent creditor who would be subordinated in a liquidation".[399]

The Companies Act 2008 does not define "secured creditor" or "unsecured creditor". Under South African law the term "unsecured creditor" would usually denote any creditor that does not hold security and would include a concurrent creditor. However, a specific reference to concurrent creditors follows the reference to unsecured creditors in section 145(4), suggesting that there is a distinction between unsecured and concurrent creditors. This has caused some confusion.[400]

Section 145(4)(b) prescribes that "a concurrent creditor who would be subordinated in a liquidation" is only entitled to a voting interest equal to the amount they could reasonably expect

[399] *Idem*, s 145(4)(b).
[400] See Henochsberg 526(76).

to receive in a liquidation of the company. In *The Commissioner, South African Revenue Service v Beginsel NO*[401] the court accepted that the reference to "a concurrent creditor who would be subordinated in a liquidation" does not include all concurrent creditors, but rather only "those concurrent creditors who have subordinated their claims in a liquidation in terms of a subordination or back-ranking agreement".[402] This amount must be independently and expertly appraised and the creditor must be notified in writing of the appraisal at least 15 days before the date of the meeting to be convened to consider the published business rescue plan.[403] In practical terms a creditor who has subordinated his claim would not reasonably expect to receive any dividend in a liquidation (unless all other creditors are to be paid in full) and will therefore have no voting interest.

No form of preferential voting right or interest is afforded to creditors by virtue of the fact that they would be preferent in a liquidation scenario. In particular, the South African Revenue Service enjoys no preference.[404]

The business rescue practitioner is also required to determine whether a creditor is "independent" for the purposes of Chapter 6 of the Companies Act 2008 and to give notice in writing to the creditor concerned at least 15 business days before the date of the meeting to be convened to consider the published business rescue plan.[405]

Should a creditor not be satisfied with the appraisal or valuation referred to above, the creditor is entitled to apply to court within five business days of having received the written notice in order to have the voting interest reviewed, re-appraised and re-valued or the determination reviewed (as the case may be).[406]

The level of support that is required for a business rescue plan to be approved is specifically dealt with in section 152 of the Companies Act 2008. A plan requires the support of more than 75% of the creditors' voting interests that were voted; and the votes in support of the plan must include at least 50% of the independent creditors' voting interests that were voted.

At any meeting of creditors other than the meeting called for the purpose of considering a business rescue plan and determining the future of the company,[407] a decision supported by the holders of a simple majority of the independent creditors' voting interests voted on a matter, is the decision of the meeting on that matter.[408]

[401] 2013 (1) SA 307 (WCC).
[402] *Idem*, para 30.
[403] Companies Act 2008, s 145(5)(b) and (c).
[404] *The Commissioner, South African Revenue Service v Beginsel NO* 2013 (1) SA 307 (WCC).
[405] Companies Act 2008, s 145(5)(a) and (c).
[406] *Idem*, s 145(6).
[407] As contemplated in the Companies Act 2008, s 151.
[408] *Idem*, s 147(3).

9.2 The first meeting of creditors

9.2.1 Introduction

The business rescue practitioner must convene and preside over a first meeting of creditors within 10 business days of his appointment.[409]

At the first meeting of creditors the business rescue practitioner:

- must inform the creditors whether he believes that there is a reasonable prospect of rescuing the company; and

- may receive proof of claims by creditors.[410]

At the first meeting the creditors may also determine whether or not a committee of creditors should be appointed and, if so, may appoint the members of the committee.[411]

The business rescue practitioner must give notice of the first meeting of creditors to every creditor of the company whose name and address is known to, or can reasonably be obtained by, him, setting out the:

- date, time and place of meeting; and

- agenda for the meeting.[412]

At the first meeting of creditors a decision supported by the holders of a simple majority of the independent creditors' voting interests voted on a matter, is the decision of the meeting on that matter.[413]

The first meeting of creditors provides an opportunity for creditors to engage with the business rescue practitioner and to ask any questions they may have. Given that this meeting takes place very soon after the business rescue practitioner is appointed, he may have limited information at his disposal. However, the business rescue practitioner is certainly able to fully explain the business rescue process and the rights of all stakeholders. Many creditors have very little understanding of the process and require guidance in this regard.

9.2.2 Reasonable prospects of rescuing the company

The courts have yet to consider the interpretation of the term "reasonable prospect" in the context of the business rescue practitioner's obligation to inform the first meeting of creditors

[409] *Idem*, s 147(1).
[410] *Idem*, s 147(1)(a).
[411] *Idem*, s 147(1)(b).
[412] *Idem*, s 147(2).
[413] *Idem*, s 147(3).

whether he believes that there is a reasonable prospect of rescuing the company. However, the same term has been extensively considered in relation to section 131(4) of the Companies Act 2008 (where it is used in relation to the requirements for the commencement of business rescue proceedings).[414] There is no reason why the term should not be interpreted in the same manner in relation to section 147(1).

Considering that the business rescue practitioner would only have been appointed for a period of 10 business days or less, he may not practically be in a position to state definitively that there is a reasonable prospect of rescuing the company. That said, if there is obviously no reasonable prospect of rescuing the company, the business rescue practitioner would be obliged to inform the creditors of this fact at this first meeting. The business rescue proceedings should then be terminated and converted to liquidation proceedings.[415]

9.2.3 *Proof of claims*

Chapter 6 of the Companies Act 2008 does not stipulate any formal procedure for the proof of creditors' claims against the company, nor does it expressly state that creditors are required to prove their claims. However, the fact that section 147 contemplates the receipt of proofs of claim at the first meeting suggests that claims may, or perhaps even should, be proved by creditors.

The fact that no format for claims and no process for their proof is set out in Chapter 6 of the Companies Act 2008 has the effect that claims must be proved in the manner and form required by the business recue practitioner. Business recue practitioners should then examine the claims submitted in comparison with the company's own records to determine whether they are valid.

The process for proof of claims that have not yet been proved is usually dealt with in the business rescue plan. However, by the time a plan is published many creditors will already have submitted claims for proof. Most business rescue practitioners provide a claim form very early on in the process to encourage creditors to submit their claims as soon as possible.

A business rescue plan will usually provide for the manner in which any claims that are disputed by the business rescue practitioner (whether that dispute relates to the quantum or nature of the claim or any security claimed) must be resolved.

9.2.4 *Notice of the first meeting of creditors*

Section 147(2) does not set out the manner in which notice of the date, time, place and agenda for the first meeting of creditors is to be given to the creditors. Accordingly, the general notice requirements in regulation 125 of the Companies Regulations 2011 are those that apply.

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[414] See the discussion in para 2.3.2.2 above.

[415] In terms of the Companies Act 2008, s 141(2)(a).

9.2.5 Independent creditors

"Independent creditor" is defined as a person who is:

- a creditor of the company, including an employee of the company who is a creditor in terms of section 144(2); and

- not related to the company, a director, or the business rescue practitioner, subject to section 128(2).[416]

Section 128(2) provides that an employee is not related to a company purely by virtue of being a member of a trade union that holds securities[417] of the company. It is also clear from the first part of the definition of "independent creditor" that an employee who is a creditor of the company is regarded as an independent creditor and is not excluded purely by virtue of being an employee.

The term "related" is defined in the Companies Act 2008.[418]

9.3 Joinder of creditors in legal proceedings arising during the business rescue proceedings through case law

The test for joinder in legal proceedings generally is whether a party has a direct and substantial interest in the subject matter of the litigation which may prejudice that party if it is not joined.[419] If an order cannot be sustained without necessarily prejudicing the interest of third parties that have not been joined, then those third parties have a legal interest in the matter and should be joined.[420]

Applying this general test, the courts have confirmed that where an application is brought to set aside a business rescue plan that has been adopted by creditors, all creditors should be joined to those legal proceedings.[421] The position of creditors would be prejudicially affected if a plan that they have voted for is set aside. In *Absa Bank Ltd v Naude NO and Others*[422] the specific prejudice referred to was that money that creditors had anticipated would be paid to them to extinguish debts owing to them would not be paid; they would be required to repay the money they had received to date, and the benefit that concurrent creditors would have received pursuant to the adopted plan might be lost should the company go into liquidation.[423]

[416] *Idem*, s 128(1)(g).
[417] "Securities" is defined in the Companies Act 2008, s 1.
[418] Companies Act 2008, s 1 defines it as "when used in respect of two persons, means persons who are connected to one another in any manner contemplated in section 2(a) to (c)".
[419] *Absa Bank Limited v Naude NO and Others* 2016 (6) SA 540 (SCA), at para 10.
[420] *Gordon v Department of Health Kwazulu-Natal* 2008 (6) SA 522; *Absa Bank Limited v Naude NO and Others* 2016 (6) SA 540 (SCA), at para 10.
[421] *Absa Bank Ltd v Naude NO and Others* 2016 (6) SA 540 (SCA), at para 10.
[422] 2016 (6) SA 540 (SCA).
[423] *Idem, at* para 10.

As to the position of creditors where a business rescue plan has been published but not yet adopted, the courts have expressed the view that the position of these creditors differs materially from creditors where a plan has already been adopted.[424] This is so because the adoption of a business rescue plan has critical consequences for creditors and their claims against the company. Once adopted, a business rescue plan is binding on all creditors whether or not they voted in favour of it.[425] Each creditor's pre-existing rights in respect of the debt owed to them is novated and becomes framed by the terms of the business rescue plan. In this sense the adoption of a plan has a direct effect on the substantive legal rights of creditors. It follows that any litigation to set aside or amend the plan will have a direct effect on their substantive financial interests as creditors.[426] In contrast, where a business rescue plan has not yet been adopted, any legal proceedings seeking to set aside the business rescue process will have no effect on the creditors' pre-existing substantive rights. If the application succeeds they simply retain their entitlement to claim what is owing to them, unaffected by the intervening business rescue proceedings.[427] They will not be prejudiced by the setting aside of the business rescue proceedings as this will not affect their existing legal rights.[428] Whilst creditors may well have an interest in litigation even before a business rescue plan is adopted, this does not necessarily translate to a legal interest in the outcome of the proceedings requiring their joinder.[429]

The court has also emphasised that there may be cases where, because of the specific facts involved, joinder under the common law (that is, because creditors have a direct and substantial interest) is necessary even though a business rescue plan has not yet been adopted.[430]

In accordance with these principles, in a matter where it was sought to interdict the section 151 meeting, the courts held that joinder of creditors was not necessary,[431] but remarked that once a business rescue plan has been adopted, creditors must be joined.[432]

The fact that there is no requirement to join the creditors to the legal proceedings in a particular instance does not mean that creditors are not able to participate should they so wish. Creditors are entitled to notice of, and participation in, each court proceeding that arises during business rescue proceedings (irrespective of whether or not a business rescue plan has been adopted). The fact that they have not been joined to the proceedings does not prejudice their rights to participate in the court proceedings. They remain entitled to intervene in those proceedings.[433]

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[424] *Blue Nightingale Trading 709 (Pty) Ltd v Nkwe Platinum South Africa (Pty) Ltd (in business rescue) and Others*, [2021] JOL 51985 (GJ), at para 18.
[425] *Ibid*.
[426] *Idem*, at para 19.
[427] *Idem*, at para 24.
[428] *Ibid*.
[429] *Idem*, at para 17.
[430] *Idem, at* para 26.
[431] *Cooper NO and Another v Knoop NO and Others* (3860/2019) [2019] ZAGPJHC 552 (28 January 2019).
[432] *Ibid*, relying also on *Absa Bank Limited v Naude NO and Others* 2016 (6) SA 540 (SCA).
[433] *Blue Nightingale Trading 709 (Pty) Ltd v Nkwe Platinum South Africa (Pty) Ltd (in business rescue) and Others*, [2021] JOL 51985 (GJ), at para 25.

Self-Assessment Questions for Chapter 9

Where necessary, refer to the Case Study in Chapter 1 of these notes when answering the questions below.

Question 1

Indicate whether the following statements are **TRUE** or **FALSE**. Furnish reasons for your answers.

Question 1.1

Mr A Float is required to convene the first meeting of creditors within 15 business days after his appointment as business rescue practitioner.

Question 1.2

At the first meeting of creditors, Mr A Float is required to inform the creditors whether he believes that there is a reasonable prospect of rescuing the company.

Question 1.3

At the first meeting of creditors, a decision supported by the holders of at least 75% of the independent creditors' voting interests voting on a matter, is the decision of the meeting on that matter.

Question 1 4

Following the publication of the business rescue plan, the creditors of Fast Flights are entitled to be joined to any legal proceedings.

Question 1.5

Due to the fact that Big Money Bank holds security for its loan facilities, its vote will carry more weight than creditors who do not hold security when it comes to voting for the adoption of a proposed business rescue plan.

Question 2

Prior to the adoption of the business rescue plan, Mr Fuel of Aero Gasoline Proprietary Limited, one of the major creditors of Fast Flights, wishes to make suggestions towards the business rescue plan. Which provision of the Companies Act 2008 can Mr Fuel rely on in this regard, and explain the operation of the provision?

Question 3

What is an "independent creditor" in terms of the business rescue provisions of the Companies Act 2008?

Question 4

Section 145(3) of the Companies Act 2008 provides creditors with the entitlement to form a creditors' committee. What are the functions and duties of the creditors' committee and what are the requirements for membership in the creditors' committee?

For feedback on this self-assessment exercise, see the document "Comment and Feedback on Self-Assessment Questions", which is made available to you as a separate document.

CHAPTER 10

THE BUSINESS RESCUE PLAN

10.1 Introduction – what is a business rescue plan?

10.1.1 The Companies Act 2008

Section 150(1) of the Companies Act 2008 requires that the business rescue practitioner "prepare a business rescue plan for consideration and possible adoption at a meeting [of creditors and any other persons holding a voting interest] held in terms of section 151". The same section requires that the business rescue plan should be prepared "after consulting the creditors, other affected persons, and the management of the company".

Section 150(2) requires that the business rescue plan should contain "all the information reasonably required to facilitate affected persons in deciding whether or not to accept or reject the plan". The content requirements of the business rescue plan are dealt with below. Section 150(5) requires that a business rescue practitioner publish a business rescue plan within 25 business days following the date on which the business rescue practitioner was appointed. Section 150(5) further provides that this publication period can be extended by:

(a) the court, on application by the company; or

(b) the holders of a majority of the creditors' voting interests.[434]

Regulation 125(3) provides for the manner in which the business rescue practitioner is to publish the business rescue plan:

- The business rescue practitioner must inform each affected person of the availability of the business rescue plan as contemplated in section 6(11)(b)(ii) of the Companies Act 2008 and regulation 6 of the Companies Regulations 2011.

- Each affected person must receive a written notice announcing the availability of the business rescue plan, delivered in paper form at his or her last known address or in

[434] In *DH Brothers Industries (Pty) Ltd v Gribnitz NO and Others* [2014] 1 All SA 173 (KZP) it was held that if a business rescue plan was not published within the 25-business day period or the extended period in terms of s 150(5) of the Companies Act 2008, the business rescue proceedings lapse by operation of law. In *Shoprite Checkers (Pty) Ltd v Berryplum Retailers CC and Others* (47327/2014) [2015] ZAGPPHC 225 (11 March 2015) a contrary conclusion was reached in that the court held that the failure of a business rescue practitioner to publish a business rescue plan within the prescribed time periods did not of itself put an end to the business rescue process. The court held that no provision is made in s 132(2) of the Companies Act 2008 for the termination of business rescue proceedings as a result of the failure to file a plan within the prescribed time periods.

electronic form, and containing the title, period of availability and method of obtaining a copy of the business rescue plan, as well as a summary of its contents.

- A notice of the availability of the business rescue plan must also be "conspicuously displayed":
  - at the registered office of the company, principal places of conducting its business activities and any workplace where its employees are employed;
  - on any website maintained by the company and intended to be accessible by affected persons; and
  - if it is a listed company, also on SENS.[435]
- A free copy of the business rescue plan must be provided to any affected person who requests a copy.

10.1.2 In practice

In plain English, a business rescue plan is prepared by a business rescue practitioner for two primary purposes:

- before adoption, to provide affected persons with sufficiently detailed information to enable them to formulate an appropriately considered opinion as to how they should vote and / or otherwise act in respect of the rescue proposals put forward by the business rescue practitioner; and
- once adopted, to provide a binding contract between the company, the business rescue practitioner and the affected persons as to how the rescue will be implemented.[436]

Business rescue plans are often too focused on the second purpose noted above (the legal contract) and lose sight of the first purpose (the clear explanation of the plan). Many affected persons (in particular trade creditors and employees) have a limited understanding of the legal principles and practices applicable in relation to Chapter 6 of the Companies Act 2008. A

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[435] SENS is the acronym for the "Stock Exchange News Service", being the news service provided by the Johannesburg Stock Exchange (JSE) for listed companies to publish company announcements and news to the markets.

[436] In *Golden Dividend 339 (Pty) Ltd and Another v Absa Bank Ltd* (569/2015) [2016] ZASCA 78 (30 May 2016), the Supreme Court of Appeal held that the effect of an approved business rescue plan is that such plan becomes binding on all creditors. Therefore, creditors are entitled to be joined to court proceedings involving the business rescue plan where their rights are affected, on the basis that they have a "direct and substantial interest" in the subject matter of the litigation. See also *Industrial Development Corporation South Africa Ltd v Van den Steen NO and Others,* (9935/18) [2018] ZAGPJHC 70 (6 April 2018) where the court held that the non-joinder of creditors in an application to set aside a business rescue plan was fatal to the relief claimed in such application.

business rescue plan that is full of legalese and constructed like a typical commercial agreement would serve the second purpose well, but would fail to deliver the first purpose for many (arguably most by number) readers. This could potentially create unnecessary animosity driven by these same creditors' perception that the business rescue plan has been (deliberately or otherwise) drafted in an obtuse manner.

Striking an appropriate balance between the above two purposes is therefore critical for a business rescue practitioner when preparing a business rescue plan. Consultation with all affected persons prior to the development and publication of a business rescue plan is essential. Obviously the views, opinions, needs and desires of affected persons are critical to the business rescue practitioner achieving a "balanced" outcome as prescribed by section 7(k) of the Companies Act 2008. It makes infinite sense for the business rescue practitioner to canvass creditors, shareholders and to the extent necessary, the employees, prior to the drawing up and publishing of a business rescue plan to give the plan the greatest probability of being approved and adopted. Case law has strongly emphasised the statutory requirement for the business rescue practitioner to consult with affected persons during the formulation of a business rescue plan.[437]

The Companies Act 2008 provides for a 25-business day period during which a business rescue plan should be prepared and published. This period can be extended if approved by a simple majority vote of creditors (or by the court), and such extensions are typical in practice. Such an extension should ideally be requested and voted on early on in the process (see the suggestion below). For large and complex business rescues (groups of companies, listed companies, multi-national companies, *etcetera*), where it would be practically impossible for a business rescue practitioner to follow all required statutory procedures, assimilate all of the relevant information and formulate a credible and sufficiently detailed business rescue plan in a five-week period, business rescue practitioners would typically request an extension of the business rescue plan publication date at the first meeting of creditors (held in terms of section 147 of the Companies Act 2008).

When is the right time to publish a business rescue plan? In practical terms, business rescue practitioners need to strike a balance between time (affected persons are entitled to expect a rescue to progress and be completed within a reasonable period of time) and practical progress (publishing a business rescue plan which is light on detail but long on speculation is not in the best interests of affected persons). For a small, simple rescue the 25-day period prescribed in the Act is reasonable and generally achievable. For complex rescues it is not uncommon for the publication date of the business rescue plan to be extended (at the first meeting of creditors) to five to six months after the commencement date of the business rescue process.

The statutorily prescribed content of a business rescue plan is discussed below.

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[437] See *Hlumisa Investment Holdings (RF) Ltd and Another v Van der Merwe NO and Others* (77351/2015) [2015] ZAGPPHC 1055 (14 October 2015), at paras 21 to 24 where the issue of consultation between the business rescue practitioner and affected persons was dealt with.

10.2 Contents of a business rescue plan

10.2.1 The Companies Act 2008

As noted above, section 150(2) of the Companies Act 2008 provides that a business rescue plan "must contain all the information reasonably required to facilitate affected persons in deciding whether or not to accept or reject the plan". Section 150(2) requires that the business rescue plan must be divided into three sections, namely:

- Part A, which deals with the background;
- Part B, which deals with proposals to creditors on how the company will be rescued; and
- Part C, which deals with the assumptions and conditions upon which a proposed business rescue plan will come into effect.

The Companies Act 2008 requires that the parts noted above must, at a minimum, have the following prescribed information:

- Part A – Background:
    - A complete list of all material assets of the company, as well as an indication as to which assets were held as security by creditors as at commencement of the business rescue proceedings.
    - A complete list of creditors of the company as at the commencement date of business rescue proceedings, as well as an indication as to which creditors would qualify as secured, preferent and concurrent in terms of the insolvency laws.
    - The probable dividend that would be received by creditors, in their specific classes, if the company were to be placed in liquidation.
    - A complete list of the holders of the company's issued securities.
    - A copy of the written agreement concerning the business rescue practitioner's remuneration.
    - A statement as to whether (or not) the business rescue plan includes a proposal made informally by a creditor of the company.
- Part B – Proposal:
    - The nature and duration of any moratorium maintained in terms of the proposed business rescue plan.

- The extent to which the company is to be released from the payment of its debts, and the extent to which any debt is proposed to be converted to equity in the company, or another company.
- The ongoing role of the company, and the treatment of any existing agreements.
- The property of the company that is available to pay creditors' claims in terms of the business rescue plan.
- The order of preference or payment waterfall in which the proceeds of the property will be applied to pay creditors if the business rescue plan is adopted. In this regard it is noted that section 135 of the Companies Act 2008 provides that, to the extent that there are funds available for distribution to creditors, the distribution to creditors is made in the following order of priority while the company is under business rescue:
  - business rescue remuneration and expenses;
  - claims arising out of the costs of the business rescue proceedings;
  - employees in respect of any remuneration, reimbursement for expenses or other amount relating to their employment during business rescue;
  - secured post commencement claims;
  - unsecured post commencement claims;
  - employees in respect of any claims for any remuneration prior to the commencement of business rescue proceedings; and
  - unsecured creditors.
- The benefits of adopting the business rescue plan as opposed to consequences of liquidation.
- The effect that the business rescue plan will have on the holders of each class of the company's issued securities.

- Part C – Assumptions and Conditions:
  - The conditions that must be satisfied for the business rescue plan to come into operation and be fully implemented.
  - The effect that the business rescue plan will have on employees and their terms and conditions of employment.

- Circumstances in which the proposed business rescue plan will end, for example in terms of section 132(2) of the Companies Act 2008.
- Projected balance sheet and statement of income and expenses, including financial forecasts for the ensuing three years.

Section 150(3) of the Companies Act 2008 requires that the projected balance sheet and statement required in Part C of the business rescue plan:

- must include a notice of any material assumptions on which the projections are based; and
- may include alternative projections based on varying assumptions and contingencies.

Section 150(4) of the Companies Act 2008 requires that the proposed business rescue plan must also include a certificate signed by the business rescue practitioner stating that any actual information provided appears to be accurate, complete and up to date, and the projections provided are estimates made in good faith on the basis of factual information and assumptions.

10.2.2 In practice

Business rescue plans have evolved over time from being legal agreements littered with legal jargon to being more commercial documents which are easier to read and understand, but sufficiently concise to deal with the legal binding nature of the document.

The Companies Act 2008 prescribes the matters / content that the business rescue plan should at a minimum address. In practice, what goes into the business rescue plan is dependent on the specific circumstances of that rescue, the complexities of that business, and the nature and specifics of the proposed restructuring plan – subject to the minimum "required contents" (as noted above) being addressed.

A useful tool for business rescue practitioners is to have a check list of required contents to ensure, once a business rescue plan is ready for publication, that it has at least met with the minimum legislated requirements. On the other hand, there is no limitation in terms what not to include in a business rescue plan. Business rescue practitioners are at liberty to include whatever they believe to be appropriate in the busines rescue plan, with the obvious proviso that they may not include something that is deliberately untrue or unlawful in any way. There are no hard and fast rules as long as the proposed business rescue plan, at a minimum, has the "required contents" and sufficient detail to enable an affected person to make an informed decision as to whether or not to vote for or against the approval and / or adoption of the plan.

The business rescue plan does not necessarily have to follow the sequence or order as prescribed in the Companies Act 2008, as long as the information is referenced and at a

minimum it includes all the information as envisaged in section 150(2).[438] It has become standard practice for experienced business rescue practitioners to incorporate a dispute resolution mechanism in the business rescue plan. The inclusion of a dispute resolution process has a similar effect to including such processes in legal agreements – with the parties thereto being bound to follow the dispute mechanisms for matters such as disputes in claim recognition, disputes relating to the terms of the business rescue plan, *etcetera*.

Business rescue practitioners generally engage an independent third party or consultant to calculate the probable distributions that would be received by the various classes of creditors if the company was to be immediately placed in liquidation. This is good practice as it provides credibility and prevents a conflict of interest where a business rescue practitioner could deliberately calculate a lower estimated liquidation dividend to incorrectly present business rescue as a better scenario than liquidation.

The business rescue plan should ideally be structured flexibly to allow for possible amendments during the creditors' approval process. For example, if a concept is repeated, list it as a definition so that in the event it is to be amended, it only requires one amendment to the business rescue plan (in the definitions) and not multiple amendments throughout the document. Ultimately, the contents of a business rescue plan must show the reader that there is, in fact, a commercially sensible and achievable plan to rescue the company. However, it should be noted that there is no one size fits all solution to a business rescue plan. It all depends on the circumstances and the challenges that the specific company and the business rescue practitioner are facing.

10.3 Requirements for the adoption of a business rescue plan

10.3.1 The Companies Act 2008

Section 152(2) of the Companies Act 2008 provides that a proposed business rescue plan will be deemed to be approved on a preliminary basis if:

(a) it was supported by the holders of more than 75% of the creditors voting interests who voted; and

(b) the votes in support of the proposed business rescue plan included at least 50% of the independent creditors voting interests, if any, that voted.

Section 152(3) provides that if the proposed business rescue plan **does not** alter the rights of the holders of any class of the company's securities or shareholders, then the approval of that

[438] In *Commissioner of South African Revenue Services v Beginsel NO and Others* 2013 (1) SA 307 (WCC), the court held that substantial compliance with the provisions of s 150(2) of the Companies Act 2008 is sufficient and it is not necessary for a business rescue plan to contain an exact description of each item listed in s 150(2). All that is required is that the business rescue plan contains sufficient information to enable interested parties to make informed decisions about the business rescue plan. See also *Golden Dividend 339 (Pty) Ltd and Another v Absa Bank Ltd* (569/2015) [2016] ZASCA 78 (30 May 2016) - sufficient information must be provided to enable an interested person to make an informed decision to vote to accept or reject the plan.

plan on a preliminary basis will also constitute the final adoption of that plan, subject to satisfaction of all the conditions that the plan may be contingent upon.

Section 152(3) requires that if the proposed business rescue plan **does** have the effect of altering the rights of any class of holders of the company's securities or shareholders, the business rescue practitioner must immediately hold a meeting of holders of the class or classes of securities whose rights would be altered by the plan and call for a vote by them to approve the adoption of the proposed plan. If the (simple) majority of shareholder voting rights that were exercised support the adoption of the business rescue plan, the plan would be deemed to have been finally adopted subject to the satisfaction of any conditions that the plan may be contingent upon. Conversely, if the majority of the voting rights who voted opposed the adoption of the business rescue plan, the plan would be deemed to have been rejected.

10.3.2 In practice

At the meeting to consider and vote on the published business rescue plan,[439] the business rescue practitioner will, after presenting the plan to creditors, ask the creditors to cast their votes for or against the adoption of the business rescue plan. The voting process is normally conducted by way of a ballot form with proxies for those who are not able to cast their votes in person at the meeting. These meetings can also be held virtually and the necessary technology and systems required to facilitate this exist and are often used in practice.

It is important to note that the Companies Act 2008 states that all creditors are entitled to vote on the plan; however, the Act does not fully define who may or may not be considered to be a "creditor" in this sense (for example, do unproven claims and / or contingent claims and / or as-yet unmeasured / unascertained claims rank equally with due, proven, measured and documented claims that have been accepted by the business rescue practitioners)?[440]

This matter is not fully clear in law. Through interpretation, it appears that only creditors whose claims have been approved by the business rescue practitioners will be allowed to vote and the claim measurement is based on the creditor's claims as per the company's records. Claims that have not been verified will generally not have a vote; however, some exceptions have been made in practice, for example with regard to contingent claims. One could, for example, provide a contingent claim with a voting right to the extent that the claim can be quantified. This is often open to debate and can be challenged. An advantage to allowing all possible "creditors" to vote (at least to some extent) is that the business rescue plan would be binding on them once adopted (this concept will be dealt with below).

[439] In terms of the Companies Act 2008, s 151, dealt with below.

[440] In *Commissioner of South African Revenue Services v Beginsel NO and Others* 2013 (1) SA 307 (WCC), the court held that the Companies Act 2008 does not create a statutory preference as is the case under the Insolvency Act. The court also held that concurrent creditors rank alongside secured creditors and are able to vote at value for the approval or rejection of the business rescue plan. It is noteworthy that the SARS enjoys no preferential status in business rescue.

Creditors with disputed claims will generally not be allowed to vote, or at least the disputed portion of their claim will not be considered. Disputed claims should ideally be dealt with in terms of the dispute resolution mechanism contained in the business rescue plan.

Post-commencement finance (PCF) creditors may be allowed to vote based on their post-commencement claims. This view has been obtained through practice, where senior counsel have advised that all creditors must vote, and this would include post-commencement finance creditors. This is not, however, a universally held view and, until the voting rights of post-commencement finance creditors are settled in law, the inclusion or non-inclusion of post-commencement finance creditors in the voting universe remains a matter for the business rescue practitioner's judgement and interpretation. A consideration that business rescue practitioners should be aware of is whether the post-commencement finance provider's claim holds significant weight due to the quantum of the post-commencement finance provided. In such a case, the post-commencement finance creditor may be able to control the outcome of the business rescue plan vote.

For the business rescue plan to be approved:

(a) it must be supported by 75% of the creditors' voting interests who voted either by way of ballot form or proxy; **and**

(b) to the extent that "independent creditors" voted as part of the 75% noted above, at least 50% of those independent creditors must have voted in favour of the business rescue plan.

The business rescue plan will then be deemed to have been finally adopted if it does not have the effect of altering the rights of the shareholders. In the event where the business rescue plan is adopted by the requisite number of creditors but does have the effect of altering the rights of the shareholders, then the business rescue practitioner must "immediately" hold a meeting with shareholders to present the business rescue plan to the shareholders for approval.[441]

In practical terms, the shareholders' meeting can take place on the same day after the creditors' meeting, or on a separate day. The shareholders' meeting can only happen, however, once creditors have voted, and not *vice versa*. In the shareholders' meeting to consider the business rescue plan, the business rescue practitioner will ask the shareholders to vote either by way of a ballot form or proxy. For the business rescue plan to be adopted by shareholders, a simple majority of the voting interests of the shareholders must vote in support of the plan.

If shareholders require an amendment to the business rescue plan before they will support it, the business rescue practitioners (assuming they support the amendments) are required to amend the business rescue plan, re-run the vote of creditors, and then re-run the vote of

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[441] See *South African Bank of Athens Ltd v Zennies Fresh Fruit CC and a Related Matter* [2018] 2 All SA 276 (WCC), 2018 (3) SA 278 (WCC) where the court dealt with the consequence of no vote being taken to approve a business rescue plan and whether this justified a conclusion that the plan had been rejected. The court held that s 153 (discussed below) only applies in instances where a business rescue plan has not been approved and is subsequently rejected.

shareholders. Therefore, in circumstances where the business rescue plan does have the effect of altering the rights of the shareholders it makes sense to have the section 151 meeting with all affected persons present, and to fully discuss the plan before voting. If it is apparent that an amendment will be required by either a creditor or a shareholder before the plan would be capable of acceptance by both of those bodies, it would be advisable to make such amendment before the approval vote (by creditors) and, after the approval vote, immediately open the shareholder meeting and conduct the adoption vote (by shareholders).

10.4 Meeting to vote on a business rescue plan

10.4.1 The Companies Act 2008

Section 151(1) of the Companies Act 2008 requires that a meeting must be held so that "the creditors and any other holders of a voting interest" can consider the business rescue plan and vote on whether to adopt or reject the business rescue plan. This meeting must be held within 10 business days of the business rescue plan being published (that is, the business rescue plan being delivered and / or made available to affected persons) in terms of section 150 of the Companies Act 2008.

Section 151(2) requires that the business rescue practitioner must deliver a notice of this meeting to all affected persons at least five business days before the meeting. This notice must set out the following:

- the date, time and place of the meeting;
- the agenda of the meeting; and
- a summary of the rights of affected persons to participate in and vote at the meeting.

Regulation 125(2) of the Companies Regulations 2011 requires that this notice must:

- be served on the relevant trade union at its head office (in terms of section 144(3)(a) all notices to which a trade union is entitled must be served at its head office);
- be delivered to other affected persons (or they must be informed of its availability in the prescribed manner);
- be conspicuously displayed at the company's registered office, principal places of business activities and any workplace where employees of the company are employed;
- be conspicuously displayed on the company's website (if it has one); and
- be published on SENS if it is a listed company.

Section 151(3) of the Companies Act 2008 provides that this meeting may be "adjourned from time to time, as necessary or expedient, until a decision regarding the company's future has been taken in accordance with sections 152 and 153."

Section 152(1) requires that **at this meeting**, the business rescue practitioner must:

- introduce the business rescue plan for consideration by the creditors and, if applicable, by the shareholders;

- inform the meeting whether the business rescue practitioner continues to believe that there is a reasonable prospect of the company being rescued;

- provide an opportunity for the employees' representatives to address the meeting; and

- invite discussion on the business rescue plan.

If the discussions noted above do not result in any proposals to amend the business rescue plan, the business rescue practitioner should call a vote of creditors for preliminary approval of the business rescue plan. If the discussions noted above result in any proposals to amend the business rescue plan, the business rescue practitioner is required to:

- entertain and conduct a vote (simple majority) on any motions to amend the proposed business rescue plan, in any manner moved and seconded by holders of creditors' voting interests **and** satisfactory to the practitioner; or

- adjourn the meeting to revise the business rescue plan for further consideration at a later date.[442]

To summarise the process at this meeting, once the business rescue practitioner has presented the business rescue plan, informed the creditors that he believes there is a reasonable prospect of a successful rescue, answered any questions that may arise relative to the content, context or implementation of the plan, and allowed employee's representatives (and any other relevant person who chooses to do so) to address the meeting, the following can occur:

- The discussion on the business rescue plan may result in sufficient holders of creditors voting interests indicating their acceptance of the plan and then a vote for approval may be called; **or**

[442] See *Booysen v Jonkheer Boerewynmakery (Pty) Ltd (in business rescue) and Another* [2014] 1 All SA 862 (WCC), (10999/16) [2016] ZAWCHC 192 (15 December 2016) where the court dealt with the issue of amendments to a business rescue plan by a practitioner after such plan has been adopted. The court held that there is no room for a business rescue practitioner to reserve the right to unilaterally amend a business rescue plan and thereby circumvent the procedures set out in the Companies Act 2008. The court held that the business rescue practitioner did not have the power to impose on creditors a plan which they had not voted on and discussed in the manner contemplated by s 152.

- The discussion on the business rescue plan may result in an affected person proposing an amendment to the plan:
    - If the amendment is acceptable to the business rescue practitioner, the amendment may be put to the meeting for support by means of a seconder, and thereafter the business rescue practitioner can call a vote on the amended business rescue plan; or
    - If the amendment is unacceptable to the practitioner and / or sufficient creditors will not accept the plan unless the plan is amended, the practitioner may adjourn the meeting and reconsider the business rescue plan in terms of section 153 of the Companies Act 2008 (this is dealt with below).

10.4.2 In practice

The section 151 meeting is key to any rescue, therefore it is extremely important that in the preparation and conception of "the plan", proper consultation is undertaken with the voting universe. Going into this meeting, the practitioner must be properly prepared and ideally should (through their consultations) have a certain level of confidence that the business rescue plan will be approved.

Those affected persons sure to be the most vocal at these meetings are those who object to the business rescue plan or have personal agendas with respect to the business rescue plan. The business rescue practitioner needs to be appropriately prepared for likely questions, proposals and objections. Proxys should be obtained for those affected persons who would be expected to vote in favour of the business rescue plan but who may not be willing or able to attend the meeting. Proxys must cater for both the acceptance of the business rescue plan as well as the acceptance of any amendments (subject to the business rescue practitioner's discretion) that are made to the business rescue plan at the meeting.

It is important for the business rescue practitioner to ensure that there is an appropriate manner of measuring the vote at the meeting that is simplistic and convenient in order to enable the business rescue practitioner to quickly and accurately calculate and communicate the outcome of the votes at the meeting. This may include printed voting ballots being created for each affected person voting on the business rescue plan, which can then be easily collected and included on a spreadsheet with pre-recorded proxy votes.

Preparation for the meeting should also include some methodology to make small amendments to the business rescue plan which can be displayed to attendees should amendments be required / possible at the meeting. It is generally recommended that business rescue practitioners have their legal counsel present at the meeting in case an opinion is required for matters included in the business rescue plan itself, or for matters related to the actual process of the meeting and how it is run.

A piece of advice: hosting the meeting at a community centre or place of worship can often take the sting out of potentially volatile meetings, as creditors tend to act more appropriately in such environments.

10.5 The consequences of a failure to adopt a business rescue plan

10.5.1 The Companies Act 2008

Should the business rescue plan not be approved and / or adopted in accordance with section 152 of the Companies Act 2008 (see paragraph 10.3 above), section 153 then applies.

Section 153(1) requires that:

(a) the business rescue practitioner must either:

- request a vote from all holders of voting interests for the business rescue practitioner to prepare and publish a revised business rescue plan; or
- advise the meeting that the company will apply to the courts to set aside the votes of vote holders who rejected the business rescue plan (creditors and / or shareholders), on the grounds that their vote was inappropriate.[443]

(b) if the business rescue practitioner does not take either of the above actions, any affected person may:

- (if present at the meeting) request a vote from all holders of voting interests requiring the business rescue practitioner to prepare and publish a revised business rescue plan; or
- (if present at the meeting) apply to court to set aside the votes of voters who rejected the business rescue plan (creditors and / or shareholders) on the grounds that their vote was inappropriate; or
- make a binding offer (by themselves or in combination with other affected persons) to purchase the voting interests of one or more persons who voted against the approval or adoption of the business rescue plan (see below).

[443] See *Advanced Technologies and Engineering Company (Pty) Ltd (in business rescue) v Aeronautique et Technologies Embarquees SAS and four Others* 2012 JDR 0345 (GNP) where the court was tasked with determining whether a vote against the adoption of a plan was inappropriate in the circumstances. See also the discussion of this judgment in Levenstein 9-134(19) - 134(21). See also *Copper Sunset Trading 220 (Pty) Ltd t/a Build It Lephalale (in business rescue) v Spar Group Ltd and Normandien Farms (Pty) Ltd* 2014 (6) SA 214 (LP). See also *Shoprite Checkers (Pty) Ltd v Berryplum Retailers CC and Others* (47327/2014) [2015] ZAGPPHC 225 (11 March 2015). Take note that a court may not set a vote aside merely because it is "inappropriate", but only if it is just and reasonable to do so based on the criteria set out in the Companies Act 2008.

Section 153(2) of the Companies Act 2008 requires that should the business rescue practitioner or the affected persons wish to apply to court to set aside the votes of those who rejected the plan, the business rescue practitioner must adjourn the meeting:

- for five business days, (unless the application is made to the court during that time); or
- until the court has disposed of the application.

Section 153(3) requires that should the business rescue practitioner or affected persons hold the vote for the business rescue practitioner to prepare and publish a revised business rescue plan, the business rescue practitioner must:

- conclude the meeting after the vote; and
- prepare or publish a new or revised business rescue plan within 10 business days.

Section 153(5) notes that in the absence of:

- a successful vote to amend the business rescue plan;
- a proposed application to court to set aside the votes of vote holders who rejected the business rescue plan; or
- the making of a binding offer to purchase the voting interests of one or more persons who voted against the adoption of the business rescue plan, then

the business rescue practitioner must "promptly file a notice of the termination of the business rescue proceedings".[444]

Should any affected person(s) present at the meeting make a binding offer (as noted above in relation to section 153(1)(b)) to purchase the voting interests of one or more persons who voted against the approval or adoption of the business rescue plan:

- the value of the voting interests must be "independently and expertly determined, on the request of the practitioner, to be a fair and reasonable estimate of the return to that person, or those persons, if the company were to be liquidated";
- section 153(6) states that the holder(s) of the voting interest, or the person(s) acquiring the voting interests, may apply to a court to review, re-appraise and re-value a determination by an independent expert;

[444] See *Commissioner of South African Revenue Services v Primrose Gold Mines (Pty) Ltd and Others* (A932/14) [2016] ZAGPPHC 737 (23 August 2016) for a discussion on the termination of business rescue proceedings pursuant to s 153(5). The court held that the business rescue proceedings will come to an end upon filing of the notice of termination, and not automatically after a business rescue plan is rejected.

- section 153(4) provides that the business rescue practitioner must:
  - adjourn the meeting for no longer than five business days (this is to allow the business rescue practitioner to make any necessary revisions to the business rescue plan to reflect the results of the offer); and
  - set a date for the resumption of the meeting, without further notice.

Section 153(7) states that when a business rescue practitioner or affected person applies to the court to set aside the votes of vote holders who rejected the business rescue plan, on the grounds that their vote was inappropriate, a court may order that the vote on a business rescue plan be set aside if the court is satisfied that it is reasonable and just to do so, having regard to the following considerations:

- the interests represented by the person(s) who voted against the proposed business rescue plan;
- the provision, if any, made in the proposed business rescue plan with respect to the interests of that person(s); and
- a fair and reasonable estimate of the return to that person(s) if the company were to be liquidated.[445]

10.5.2 In practice

If a business rescue plan needs only minor revisions in order for it to be approved and adopted, it is better that this is done at the same meeting (see paragraph 10.4 above). If not, the business rescue plan needs to be amended, re-published, new notices sent, and the meeting reconvened. Business rescue practitioners should always be prepared to make reasonable amendments at the section 151 meeting if so requested.

[445] In *First National Bank v KJ Foods CC (in business rescue)* (734/2015) [2017] ZASCA 50 (26 April 2017) the Supreme Court of Appeal held that a determination by a court that a vote is to be set aside is a value-based judgment that is to be made after all the facts and circumstances are considered. Once it is determined that a vote against the adoption of a business rescue plan is inappropriate and falls to be set aside, there is no requirement for the vote to be retaken. In other words, once a vote is set aside, the business rescue plan is considered to have been adopted by operation of law, with no further voting required. See also *Ex parte Target Shelf 284 CC; Commissioner, South African Revenue Services and Others v Cawood NO and Others (in business rescue)* [2017] JOL 37690 (GP) where the court also dealt with the issue of an inappropriate vote and held that a court need not find a vote to be inappropriate first before it can consider whether it would be reasonable and just to set the vote aside. Take note that the term "inappropriate" must be given its ordinary dictionary meaning, ie "unsuitable, unfitting or improper" and that a *bona fide* vote cast by a creditor in the genuine belief that such vote would advance such creditor's interests, will not fall within the category of an inappropriate vote. See also *Collard v Jatara Connect (Pty) Ltd* (23510/2016) [2017] ZAWCHC 48 (14 March 2017).

Bear in mind that when a section 151 meeting results in the calling of a fresh section 151 meeting at a later date, the provisions of sections 151 and 152 and 153 of the Act apply afresh (in the same manner as they did in respect of the first such meeting).

The consequence of not reaching some equitable decision at a section 151 meeting (approving and adopting a business rescue plan or approving a process for the business rescue practitioner to amend the business rescue plan and recall the meeting) or the receipt of offers to acquire voting rights are either that:

- the business rescue practitioner or affected persons must head to court to challenge the vote; or

- the business rescue practitioner must "promptly file a notice of the termination of the business rescue proceedings".

It must be noted that inappropriate vote challenges in court are not easy. The courts have held differing views and are sympathetic to affected parties who are focused on their own outcomes, even if such focus is at the expense of other affected persons. The key consideration is comparing the outcome for the party that voted against the adoption of the plan in the business rescue *versus* the outcome in a liquidation.

The Companies Act 2008 is clumsy and not clear in its drafting as to how a "binding offer" works, who it is binding upon, the sequence of events, *etcetera*. Until this matter is clarified through amendments to the Companies Act 2008 or legal precedent, it remains something of a minefield.[446] An interesting feature of the Companies Act 2008 is that it specifically does not require that a "binding offer" should come from an affected person who was present at the meeting. Extrapolating this, a shareholder whose rights would not be affected by the business rescue plan and would thus have no vote, could potentially "buy" votes in this manner.

As with much of Chapter 6 of the Companies Act 2008, process and procedures are important. Business rescue practitioners should carefully follow the required procedures set out in section 153, as legal challenges to business rescue proceedings will often be founded on strict non-

[446] See *African Bank Corporation of Botswana Ltd v Kariba Furniture Manufacturers (Pty) Ltd and Others* [2013] 4 All SA 432 (GNP), 2013 (6) SA 471 (GNP) and *African Bank Corporation of Botswana Ltd v Kariba Furniture Manufacturers (Pty) Ltd and Others* [2015] 3 All SA 10 (SCA), 2015 (5) SA 192 (SCA) where the courts were tasked with determining the binding effect of the offer contemplated in s 153(1)(b)(ii) of the Companies Act 2008. The Supreme Court of Appeal in this case held that in order for an offer to be binding it had to be accepted by the offeree. Accordingly, a binding offer made to a creditor who opposes a business rescue plan is not automatically binding on such creditor and there is therefore no summary divestment of such creditor's rights. See also the full discussion of these judgments in Levenstein 9-136 - 140. See also *DH Brothers Industries (Pty) Ltd v Gribnitz NO and Others* [2014] 1 SA 173 (KZP) and *Absa Bank Ltd v Caine NO and Another* (3813/2013, 3915/2013) [2014] ZAFSHC 46 (2 April 2014) for further discussions on the meaning of a "binding offer". In *Absa Bank Ltd v Caine NO and Another*, the court held that a "binding offer" should be regarded as an offer binding on the offeror and not the offeree, who should have the discretion to either accept or reject the offer. This view accords with the current legal position.

compliance of such procedures rendering certain acts as invalid.[447] An example in this regard may be the taking of a vote to amend a business rescue plan – a vote is required. The business rescue practitioner should clearly note in a section 151 meeting whether this is an informal (show of hands) vote, or a formal (voting ballots) process.

10.6 The binding effect of an approved and adopted business rescue plan

10.6.1 The Companies Act 2008

Section 152(4) of the Companies Act 2008 provides that once a plan is adopted, it is binding on the company and on each of the creditors of the company and every holder of the company's securities, whether or not such a person was present at the meeting, voted for or against the adoption of the business rescue plan or in the case of creditors, or had proven their claims against the company.

Section 154(2) provides that if a plan is approved and implemented in accordance with the Companies Act 2008, a creditor is not entitled to enforce any debt owed by the company immediately before the beginning of the business rescue process except to the extent provided for in the plan.[448]

10.6.2 In practice

The law is clear that, unless amended or set aside (in an appropriately legal manner), the business rescue plan in effect becomes a binding agreement / arrangement on the business rescue practitioner and all affected persons. This often creates confusion amongst creditors and other affected persons, especially those with limited knowledge or understanding of business rescue proceedings, as they believe that the business rescue plan is not binding on them (as they did not vote for the business rescue plan), or they were not aware of the commencement of business rescue proceedings.

The binding effect of the business rescue practitioner plan is also applicable to regulatory bodies and other institutions who are creditors of the company such as the South African Revenue Service (SARS), *etcetera*. Normally SARS will participate in the business rescue proceedings and their claims will often get compromised like any other concurrent / unsecured creditor, but other government institutions (including government agencies / departments such as the Unemployment Insurance Fund, the Department of Labour and the Compensation for Occupational Injuries and Diseases Act) and regulatory bodies tend not to participate in business rescue proceedings and often believe that the Companies Act 2008 and the business

[447] See *Kransfontein Beleggings (Pty) Ltd v Corlink Twenty Five (Pty) Ltd and Others* (624/2016) [2017] ZASCA 131 (29 September 2017) where the court held that after the adoption of a business rescue plan, those with a direct and substantial interest in litigation involving such plan and who may be prejudiced by such legal proceedings, must be joined to the relevant proceedings.

[448] See *Stalcor (Pty) Limited v Kritzinger NO and Others* [2017] JOL 37785 (FB) for a discussion on the binding effect of an approved business rescue plan. In terms of s 152(4) of the Companies Act 2008, an approved plan is binding on every creditor.

rescue plan is not binding on them. This is mainly due to a lack of understanding of the business rescue process and the legislative prescripts.

In practice, certain "blackmail creditors" will use their position as a dominant / monopoly supplier to exclude themselves from the binding nature of an adopted business rescue plan. For example, municipalities will insist on the payment of the full amount due (including pre-business rescue debt) and if no payment or arrangement is made, they disconnect the services (for example, electricity).

Noting that an approved business rescue plan is binding on pre-business rescue creditors, the "timing" of a creditor's claim becomes important. For example, if a claim only becomes apparent after the commencement of business rescue proceedings but it relates to a matter or legal agreement that pre-dates the commencement of business rescue proceedings, it is a pre-commencement claim that is bound by the business rescue plan.

10.7 Implementation of a business rescue plan and a reasonable prospect of rescuing a company

10.7.1 The Companies Act 2008

Section 152(5) of the Companies Act 2008 requires the company, under the direction of the business rescue practitioner, to take all the necessary steps to:

- attempt to satisfy any conditions on which the business rescue plan is contingent; and
- implement the business rescue plan as adopted.

Section 152(6)(a) of the Companies Act 2008 provides a business rescue practitioner with the power, to the extent necessary in order to implement an adopted business rescue plan, to determine the consideration for, and issue of, any authorised shares for the company, notwithstanding the otherwise restrictive provisions of sections 38 and section 40 of the Companies Act 2008.

If the business rescue plan was approved by shareholders of the company in accordance with section 152(3), section 152(6)(b) further empowers the business rescue practitioner to amend the company's memorandum of incorporation (MOI) to authorise and determine the preferences, rights, limitations and other terms of any securities that are not otherwise authorised but are contemplated to be issued in terms of the approved business rescue plan, notwithstanding the otherwise restrictive provisions of sections 16, 36 or 37 of the Companies Act 2008.

Section 152(7) provides that a pre-emptive right of any shareholder of the company, as per section 39 of the Companies Act 2008, does not apply with respect to an issue of shares by the company in terms of an approved business rescue plan (unless the business rescue plan states otherwise).

Section 112(1)(a) excludes fundamental transactions (that is, a company disposing of all or more than half of its assets or undertakings, merging with another company, *etcetera*) pursuant to an adopted business rescue plan from the otherwise restrictive requirements of sections 112 and 115 of the Companies Act 2008.

Section 152(8) requires the business rescue practitioner to file a notice of the substantial implementation of the business rescue plan when the business rescue plan has been substantially implemented.

10.7.2 In practice

During the implementation phase of an adopted business rescue plan, it is important to note the continued application of section 141(2)(a) of the Companies Act 2008 which requires that if a business rescue practitioner concludes **at any time** during the business rescue proceedings that there is no reasonable prospect for the company to be rescued, the business rescue practitioner must:

- inform the court, the company and all affected persons in the prescribed manner; and
- apply to the court for an order discontinuing the business rescue proceedings and placing the company into liquidation.

Of equal application, during the implementation phase of an adopted business rescue plan it is important to note the continued application of section 141(2)(b) of the Companies Act 2008 which requires that if a business rescue practitioner concludes at any time during the business rescue proceedings that the company is no longer financially distressed, the business rescue practitioner must:

- inform the court, the company and all affected persons in the prescribed manner; and
- terminate the business rescue proceedings.

Noting the provisions of section 152(8) of the Companies Act 2008, requiring the business rescue practitioner to file a notice of the substantial implementation of the business rescue plan when the business rescue plan has been substantially implemented, it is noted that the Companies Act 2008 does not define "substantial implementation". It is generally considered good practice, therefore, for the business rescue practitioner to set out in the business rescue plan the requirements for substantial implementation to have been achieved.

It is unlikely in most circumstances that a business rescue plan will, during implementation, go exactly "according to plan". Small deviations are likely to crop up. It is for this reason that it may be necessary for the business rescue practitioner to build into their business rescue plan appropriate provisions for the amendment of the plan. The Companies Act 2008, it is noted, is silent on the amendment of a business rescue plan after its adoption. However, in light of case

law on the issue, it is submitted that should a business rescue plan contain provisions for the amendment of such plan, the relevant provisions should not (i) permit unilateral amendments by the business rescue practitioner and (ii) attempt to circumvent the procedures contemplated under sections 152, 145 and 146 of the Companies Act 2008.[449]

The provisions of sections 152(6) and 152(7) noted above empower the business rescue practitioner to amend the company's memorandum of incorporation, authorise shares and issue shares (in accordance with the provisions of those sections), notwithstanding the otherwise restrictive provisions of sections 16, 36, 37, 38, 39 and 40 of the Companies Act 2008. However, no similar relief is provided in section 152(6) and 152(7) from the operation of section 41(3) of the Act.

Section 41(3) reads "An issue of shares, securities convertible into shares, or rights exercisable for shares in a transaction, or a series of integrated transactions, requires approval of the shareholders by special resolution if the voting power of the class of shares that are issued or issuable as a result of the transaction or series of integrated transactions will be equal to or exceed 30% of the voting power of all the shares of that class held by shareholders immediately before the transaction or series of transactions."

The inference from the above is that business rescue practitioners may, without the approval of shareholders by way of a special resolution, issue new shares, but only provided that the new shares to be issued do not confer voting rights which exceed the 30% threshold. It is unclear at this time if this was deliberate or a drafting error by the drafters of Chapter 6 of the Companies Act 2008.

Additional complications to the implementation of an approved and adopted business rescue plan arise if the company in question is listed on the Johannesburg Stock Exchange (JSE). Specific issues that need to be addressed with the JSE would include:

- **Suspension of trading in the company's shares**: Previously confidential financial information is impossible to keep tight during business rescue proceedings. Post-commencement finance funders want cashflow forecasts, as do lenders and contract counterparties. Such counterparties want assurances and often detailed information. There are lawyers and advisors all over the place. Business rescue practitioners are obliged by the Companies Act 2008 to consult with creditors (of which there are often thousands) and other affected persons when preparing and crafting a business rescue plan. Price sensitive information thus finds its way into many hands and is very difficult to control. Most business rescue practitioners and affected persons are unversed in what constitutes "price sensitive information". It is therefore recommended that business rescue practitioners engage early with the JSE and request a suspension of trading of the company's shares at the earliest opportunity.

[449] See *Kransfontein Beleggings (Pty) Ltd v Corlink Twenty Five (Pty) Ltd and Others* (624/2016) [2017] ZASCA 131 (29 September 2017).

- **Categorised transactions**: Whilst the Companies Act 2008 provides relief from the need to obtain shareholder approvals for certain actions (for example, significant disposals, share issues, fundamental transactions (section 112), *etcetera*) which may be contemplated in the implementation of an adopted business rescue plan – the JSE regulations do not currently provide such relief. It is therefore recommended that business rescue practitioners engage with the JSE at an early stage to ensure that the company and its directors are not censured by actions approved by the business rescue practitioner (and the business rescue plan), and that such actions may be implemented without unnecessary regulatory hindrance.

  This matter is particularly relevant as transactions are categorised by the JSE relative to the market capitalisation of the company on the exchange. Distressed companies tend to have a low market capitalisation – meaning that most modest sales not in the ordinary course of business fall to be treated by the JSE as categorised transactions.

- **Other regulations**: Early engagement with the JSE with regard to the company's likely compliance / non-compliance with the numerous JSE regulations, is recommended.

Self-Assessment Questions for Chapter 10

Where necessary, refer to the Case Study provided in Chapter 1 when answering the questions below.

Question 1

Section 150(2) of the Companies Act 2008 provides that a business rescue plan "must contain all the information reasonably required to facilitate affected persons in deciding whether or not to accept or reject the plan". How many sections is the business rescue plan divided into and what is the prescribed minimum information that each part or each section in the business rescue plan must contain?

Question 2

The Companies Act requires the business rescue practitioner to appoint an independent consultant to calculate a probable liquidation dividend. What is the reason for including a liquidation calculation in the business rescue plan?

Question 3

For the business rescue plan to be approved or adopted, what is the requisite threshold for approval / adoption of the business rescue plan? What happens if the business rescue plan is not approved and is rejected by creditors? What are the options available to the business rescue practitioner?

Question 4

(a) Who is eligible to vote for the adoption of the business rescue plan?

(b) Are employees allowed to vote for the adoption of the business rescue plan? Provide reasons for your answer.

(c) If a creditor has a disputed claim, is he or she allowed to vote for or against the approval or adoption of the business rescue plan?

(d) In practice, how are disputed claims normally resolved?

Question 5

What happens if the business rescue plan is approved by the requisite majority of creditors and Jumbo Jet has voted against the business rescue plan? Is the approved business rescue plan binding on Jumbo Jet?

Question 6

Fast Flights' aircraft lessors are all foreign companies domiciled outside of South Africa. One of these lessors is owed a substantial amount of money by Fast Flights for rental periods prior to the commencement of business rescue, under a lease agreement that states its governing law to be that of the foreign lessor's country of domicile. The foreign lessor (creditor) is of the opinion that the statutory moratorium imposed as part of Fast Flights' business rescue proceedings does not apply to it because it is not a South African company / creditor and because its lease agreement with Fast Flights is not governed by South African law. Thus, it is insisting that Fast Flights either settle its debt in full, or return the leased aircraft. Note that Fast Flights is up to date with rental payments relating to periods post the commencement of its business rescue proceedings; Fast Flights would like to continue leasing the aircraft in question for the foreseeable future.

Question 6.1

Briefly provide your opinion on the validity of the foreign lessor's (creditor's) viewpoint? What other considerations should Mr A Float (the business rescue practitioner) be aware of in terms of this (and other) foreign creditor(s).

Question 6.2

Draft a section for inclusion in the business rescue plan that deals with the binding nature of the business rescue plan once adopted, while making reference also to foreign domiciled creditors.

Question 7

The airline catering company that Fast Flights acquired prior to 2019 operates as a wholly owned subsidiary of Fast Flights. While the catering company has strong future prospects and is expected to be profitable in the long-term, it will require a significant amount of funding for the initial 12 to 18 months of Fast Flights' business rescue proceedings to cover working capital shortfalls (that is, the catering company subsidiary will require short to medium-term financial assistance from Fast Flights). Thereafter, the catering company is expected to provide substantial returns to Fast Flights, which should ultimately improve creditor dividends.

Question 7.1

Given Fast Flights' current financial distress (business rescue), comment on whether you believe Fast Flights is permitted to provide financial assistance to its catering company subsidiary in terms of section 45 of the Companies Act 2008?

Question 7.2

Draft a section for inclusion into the business rescue plan that deals with Fast Flights' subsidiary catering company and the provision of financial assistance by Fast Flights to cover its 12 to 18 month working capital shortfall.

Question 8

Big Money Bank expressed its concern about the status of the facilities made available by it prior to the commencement of business rescue proceedings, and whether such facilities would be treated differently than any new facilities provided during the business rescue proceedings. Comment on whether you believe that Mr A Float can address Big Money Bank's concerns by reflecting the unutilised portion of the bank facility at the commencement of business recue as post-commencement finance in the business rescue plan, if fully utilised post-business rescue.

Question 9

Considering Mr A Float's discussions with the lenders and shareholders of Fast Flights, is it fair to state that all post-commencement finance is considered as equal in these business rescue proceedings?

Question 10

Mr A Float published the Fast Flights business rescue plan on 1 August 2020. With reference to the provisions set out in section 150 of the Companies Act 2008:

Question 10.1

Explain why this stated date of publication is problematic in terms of the statutory requirements and legal factors associated with the publication of a company's business rescue plan.

Question 10.2

Offer a solution that details the process that Mr A Float could have undertaken, in order to negate any legal challenges in this regard.

Question 11

The commencement of a section 189(3) large-scale retrenchment process is one of the primary ways in which a financially distressed company in business rescue can reduce overhead costs and operating expenditure. Accordingly, if determined as necessary, commencing this process as soon as possible after the commencement of business rescue proceedings would be of significant benefit to any company that has commenced business rescue. When Mr A Float began preparing and drafting Fast Flights' business rescue plan, he included provisions that contemplated the retrenchment of a large portion of Fast Flights' employees. With reference to the applicable sections of the Companies Act 2008 and relevant case law, explain the following:

Question 11.1

Soon after his appointment, Mr A Float determined that a reduction in Fast Flights' employee headcount would significantly assist the company in its cost-reduction initiatives. Why then did Mr A Float only consider such a critical cost-saving initiative in the business rescue plan and not as a part of his immediate cost-reduction initiatives?

Question 11.2

With reference to your response to question 11.1 above, discuss the problematic aspects that this determines in the context of business rescue. Ensure that your answer critically examines the failings of the relevant case law in terms of the precedent set regarding the treatment of employees in a business rescue process.

Question 11.3

It is noted that Mr A Float's business rescue plan did not specify the status of the employees' unpaid salaries. With reference to the applicable provisions of the Companies Act 2008, explain why this is extremely problematic and how employees claims should be treated in a business rescue and dealt with in a business rescue plan.

Question 12

Under what conditions will employee costs sit above post-commencement finance in the waterfall of payments in business rescue?

Question 13

Considering the totality of Fast Flights' creditors, comment on the manner in which an approval of voting on the business rescue plan can be achieved. You are required to specifically comment on relevant considerations pertaining to related-party and subordinated creditors.

Question 14

In relation to the Fast Flights business rescue practitioners' remuneration, what additional disclosure in the business rescue plan is required in terms of the Companies Act 2008?

Question 15

Jumbo Jet Proprietary Limited, a minority creditor, voted against the plan on the basis that it genuinely believed that the plan would impose financial risks on itself as well as other creditors, and as a result was of the view that it was not bound by the terms of the approved business rescue plan at all. Fully discuss and substantiate the legal principles applicable to the above statement, indicating whether they are valid and supported by the applicable law.

Question 16

Consider the offer made by Engines Proprietary Limited to Jumbo Jet Proprietary Limited. Discuss the implications on both parties. Substantiate your answers by specific reference to all applicable and relevant sources.

For feedback on this self-assessment exercise, see the document "Comment and Feedback on Self-Assessment Questions", which is made available to you as a separate document.

CHAPTER 11

UNDERSTANDING FINANCIAL FORECASTS IN A BUSINESS RESCUE CONTEXT

11.1 The requirements of section 150

Per section 150(2)(c)(iv) of the Companies Act 2008, a published business rescue plan must include, *inter alia*, a projected:

- balance sheet of the company in business rescue; and
- statement of income and expenses for the ensuing three years.

The above must be prepared on the assumption that the proposed business plan and income statement is adopted. Further, per section 150(3)(a) and 150(3)(b), the projected balance sheet and statement required must include a notice of any material assumptions on which the projections are based and may include alternative projections based on varying assumptions and contingencies.

Whilst it is not clear from the drafting of the aforementioned section of the Companies Act 2008, it is generally accepted practice that a projected balance sheet should also be prepared for the ensuing three years.

It is clear that the Companies Act 2008, by virtue of the requirement to provide affected persons with the underlying and supporting assumptions of the financial forecasts, envisages that there is an element of inherent uncertainly with respect to such forecast projections. Such projections should however reflect that which is proposed in the rescue plan itself, for example the refinancing of debt, a new capital injection or a proposed dividend amortisation plan. It is critical that such projections reflect the business on completion and with effect from the exit from business rescue and for the next three years on the basis that the proposal within the rescue plan is successfully adopted and implemented. The Companies Act 2008 is unequivocally clear in this respect of the forecast financial information.

It is also worth noting that the Companies Act 2008 does not specifically make reference to a cash flow statement, although it is the view of the authors of this chapter that cash flow is critical, and hence that the projections prepared by the appointed business rescue practitioner should be carefully considered and include a cash flow statement(s) in the published business rescue plan. This is discussed later in this chapter.

It is clear that sections 150(2)(c)(iv), 150(3)(a) and 150(3)(b) together require certain financial information to be presented in the rescue plan, but these sections however provide no further guidance as to the level of detail required. In this context, the business rescue practitioner is therefore required to exercise an element of professional judgement and assess what level of information, in the context of forecast financial projections, may be required in order to allow the various stakeholders to make an informed decision (on the rescue plan and pursuant to any

vote to accept, amend or reject the rescue plan as may be applicable). The business rescue practitioner must however ensure that he has "substantially complied"[450] with the provisions of Chapter 6 and specifically sections 150(2)(c)(iv), s 150(3)(a) and 150(3)(b).

The financial forecasts provide a critical component to the overall proposal(s) contained within a business rescue plan and may also, in certain instances, form the basis of reliance on which future dividends will be paid to creditors. In addition, such forecasts are by necessity required by the business rescue practitioner to assess the future solvency of the business which is a precursor to successful implementation and conclusion of business rescue proceedings. The importance of such financial forecasts of the company in business rescue cannot therefore be emphasised enough.

11.2 A basic understanding of the different financial statements (balance sheet, income statement and a cash flow statement)

Balance sheets, income statements and cash flow statements are the three primary elements of financial statements (and that are required, *inter alia*, in audited financial statements). Whilst each of the aforementioned statements seek to provide different information and are prepared for a different purpose, the relevant financial statements are also prepared on the basis that they are read in conjunction with each other, and that they allow a reader to form an overall view of the financial health of the company in question.

Financial statements are also subject to, and a function of, the relevant accounting policies, standards and professional judgement applied by the relevant preparer. As such, a reader of financial statements should be aware of and understand the implications of such policies and standards and how this has, where applicable, impacted that which is being reported.

A basic outline of each statement, namely a balance sheet, income statement and cash flow statement is set out below.

11.2.1 Balance sheet

A balance sheet reflects the overall financial position of a company at a point in time which can be historic or in the future. It reflects whether the company is or may forecast to be in a net asset (solvent) or net liability (insolvent) position. In other words, it reflects the value of shareholder equity, essentially the "book value" of the business.

The solvency of a company is critical in the context of business rescue. This is because section 128(f)(ii) of the Companies Act 2008 includes in its definition of financially distressed the likelihood that a company will become insolvent within the immediately ensuing six months. This section does not distinguish between commercial (cash flow) and technical (balance sheet) insolvency, and accordingly the balance sheet position as described above becomes an important source of information and by extension any forecast balance sheet position.

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[450] Henochsberg 150.

A balance sheet typically provides for a breakdown of all the key assets owned or leased by a company. By way of example, this may include land and buildings, plant and equipment and intangible assets such as cash, debtors and trademarks. Liabilities typically comprise short-term liabilities such as trade creditors, taxes, lease liabilities and the short-term portion of lender debt, whilst long term liabilities often comprise the likes of bank debt and pension provisions.

11.2.2 Income statement

In contrast to the balance sheet, an income statement provides an indication as to the level of profitability of that business over a given period of time. It highlights the revenue or income of a business less expenses, the latter of which also includes items such as increases in provisions and bad debt write-offs. The income statement is in part a function of accounting policies and regulations and as such does not always reflect the cash flows of a business.

Like a balance sheet, an income statement also provides the reader with insight into the financial health of a business, albeit over a defined period of time (for example a year in annual financial statements).

11.2.3 Cash flow statement

In line with an income statement, a cash flow statement provides information in respect of cash inflows and outflows over a given period in time. Closing cash or an overdrawn position, which is the result of the cash flows, is highlighted in the balance sheet.

Cash flow statements are typically broken down into the following main components, namely:

- Cash flows from operations (including the net impact of working capital);
- Cash flows from investing activities; and
- Cash flows from financing activities.

The above categories further provide detail on, *inter alia*:

- Cash inflows over the period, for example debtor collection and cash sales;
- Cash outflows such as operating expenses settled in cash;
- Working capital movements, for example the impact of debtor collections and creditor payments;
- Non-operating cash outflows such as capital expenditure on a new building; and
- Non-operating cash income, such as the proceeds from a capital raise or new bank loan.

Cash flow, or liquidity, is critical and is often considered the most important indicator of financial health or potential failure of a company. A principal reason for companies entering into business rescue in South Africa (whether by court order or a voluntary filing) is an immediate lack of liquidity (or expected lack of short-term liquidity such that it is reasonably likely that the company will not be able to pay all their debts as they become due and payable within the immediately ensuing six months).[451] Cash flow forecasts are by definition therefore extremely important and particularly so in the context of the viability of and voting on a business rescue plan.

Whilst a loss-making company typically suffers (or will suffer) from a cash shortfall, a company may also sometimes report a profit as reflected in the income statement whilst concurrently reporting a decrease in cash flows or a cash shortfall. This can occur, for example, when a company has a long or adverse working capital cycle, where creditors require settlement ahead of customers paying for their goods or services albeit that the business is generating sufficient gross margin and / or profit.

11.3 The purpose of the different financial statements

As highlighted above, the three core financial statements seek to explain to a reader the overall financial position and health of a business and should be read in conjunction with each other, and in the context of the purpose for which they were prepared.

A balance sheet provides a summary of the overall risk of a company – the extent to which its assets exceed its liabilities (or *vice versa*) provides, whilst not definitive, an indication of how much risk that company's creditors may be exposed to:

- The balance sheet provides a summary of whether a company is technically solvent or insolvent, the latter of which provides heightened risk of the business collapsing. This is explained by way of illustration, whereby a board of directors may seek to place an insolvent company under their watch into business rescue. This type of action is typically triggered due to cash flow problems (see the cash flow section above) but nonetheless illustrates one potential risk associated with balance sheet insolvency; and

- In the event that that there is an insolvency, the question is then whether there will be sufficient assets to settle all creditors in full following completion of the insolvency process.

An income statement also acts as an important indicator of the financial health of a business, often indicating potential future trends. It highlights what has happened over the period in question, for example how different products have performed and whether the company is making sufficient margin from the sale of its goods or services.

It also provides information in respect of key expenses and whether such expenses are covered by the relevant gross margin or income of the business. Expenses of a business are generally categorised into two main components, namely operating and non-operating expenses.

[451] Companies Act 2008, Ch 6.

Examples of such expense classifications are salaries and legal fees, respectively. The relevance and therefore one purpose of this statement is an understanding of the structure of costs in a business, for example whether they are fixed or variable. This in turn may in certain instances highlight potential risks where, for example, a business which has a high level of fixed expenditure which may not in the event of a sudden downturn of revenue or cash income be able to be reduce its costs sufficiently in the short term and may as a result suffer cash flow problems.

Income statements further usually highlight earnings before interest, tax, depreciation and amortisation (EBITDA), which is a key metric that stakeholders such as lenders and investors use to monitor the performance of a company.

A business cannot survive without cash and, in the absence of access to sufficient facilities, is likely to eventually face closure or collapse. As previously highlighted, a lack of cash or a forecast cash (or funding) shortfall is a very common reason for companies to file for business rescue. In other words, a lack of liquidity is a critical risk factor in companies failing and being placed into or voluntarily filing for business rescue. Cash flow is therefore a vital indicator of the financial health of a business, its stability and potential short-term risks.

11.4 Considerations to bear in mind when drafting the forecast financials for inclusion in the section 150 plan

The forecast financials form an important part of the overall business rescue plan and in particular in relation to the proposal within such a plan.[452] Affected persons are therefore inherently interested in and reliant on such forecast information to inform their decision on whether to vote for (or have amended) or reject the business rescue plan in question.

Whilst the content of financial forecasts will depend on a number of factors such as the complexity of the business (for example different product types or revenue streams or businesses that operate across multiple geographies), consideration should be given to the audience when preparing and presenting such forecasts. In this context the business rescue practitioner should consider the purpose of the financial forecast information, namely a commercially based decision-making tool for affected persons and not necessarily a requirement to be fully aligned to the purpose of other financial statements, for example audited financial statements.

The following factors, whilst not exhaustive, provide an illustration of what may need to be considered in this context:

- Who the affected persons are and their ability to understand and interpret such forecasts;

- Whether the impact of the proposal as contained within the business rescue plan is reflected in the forecasts;

[452] This "link" is specifically required and set out clearly in the Companies Act 2008, s 150(2)(c)(iv).

- The starting point (point in time) for the forecasts;

- The level of detail required to allow an affected person to make an informed decision about the plan in a relatively short period of time;

- How key numbers or variables within the financial forecasts have been derived, for example the number of units that will be sold, average selling prices or margins, whether working capital requirements have been correctly understood and captured, etcetera;

- A list of written supporting assumptions that provide sufficient explanation for the forecast financials (for example growth trends, expansions into new markets and the proposed use of fresh capital) and the context in which they have been presented; and

- An explanation of key cash flows and cash utilised for future dividend payments where applicable.

Forecasts, by their nature, are predicated on a number of assumptions and unknown events. Therefore, whilst not specified within the Companies Act 2008, the business rescue practitioner will also, in the context of section 150 of the Companies Act 2008, need to consider key risks associated with the forecast financials and highlight such risks within the relevant section of the rescue plan.

11.5 Common pitfalls and practical challenges in preparing the necessary financial forecasts

Preparation of the forecast financials for inclusion into a business rescue plan can be complicated, with a number of factors such as poor information, time pressures, the availability of sufficiently skilled and knowledgeable resource and complex forecast assumptions exacerbating the situation if in existence.

In many instances, a business rescue practitioner is dependent on the co-operation and the provision of accurate and complete information from management, in the absence of which the preparation of financial forecasts may increase in difficulty.

Further, trading during a business rescue is often distinct from that, post-exit from business rescue. This is explained further by way of illustration whereby a company loses all credit terms during business rescue proceedings but may, subject to certain conditions and the implementation of the adopted business rescue plan, come to enjoy the reinstatement of such terms post-rescue and which therefore may impact the forecast financial period. In this example, the business rescue practitioner will need to apply judgement and give due consideration to the potential impact of such supplier trading changes if potentially material to forecast trading results.

Common pitfalls in respect of forecast financial information provided within a business rescue plan may include, but are not limited to:

- ***Insufficient granularity and detail*** – forecasts are prepared at a very high level to the extent that an affected person cannot reasonably assess the forecasts and risks attaching thereto. In this context, key variables such as unit sale assumptions, selling prices, cost structures and growth assumptions are often omitted or insufficiently disclosed and explained. The more detail that is provided to enable stakeholders to assess the reasonableness of the underlying assumptions, the more confidence stakeholders can have in the forecast information;

- ***Insufficient written assumptions and a lack of context to the presented forecast financials***. For example, growth in revenue and profit assumptions should be explained in the context of the presented turnaround plan, working capital assumptions should be explained if there is a material impact on cash flows, etcetera. Affected persons should be able to assess the overall context of the forecast financials and how trading may be forecast to change from historic trading;

- ***Lack of cash flow information or correctly analysed and presented cash flow information***. As highlighted in the earlier sections to this chapter, cash flow is critical to the survival of a business and its ability to continue trading on a solvent basis following its exit from rescue. Business rescue practitioners require an in depth understanding of cash flows and how these differ from profit and loss (income) statements;

- ***Financial forecasts are out of date***; financials should essentially commence for a three year period from (approximately) the date of exit from rescue or from when the plan is adopted. In this context, the business rescue practitioner should also ensure that the correct opening balance sheet is prepared (for example, where creditors are to be compromised, the impact on the balance sheet should be incorporated into a "*pro forma*" balance sheet);

- ***Insufficient consideration is given to the impact of the proposal which forms the core of the business rescue plan*** (for example the impact of new funding should be shown, new operating arrangements such as new lease agreements may need to be considered). Use of historic trading (or "run rates") without due consideration of how trading and the environment may have changed increases the risk of forecast financials being materially misstated; and

- ***Key risks are not articulated sufficiently or at all*** – in the context of providing sufficient information to an affected person to make a reasonably informed decision. In this context, best practice dictates that the business rescue practitioner give due consideration to the potential impact (or range of impacts) in the event of a certain events occurring or a downside and / or stressed scenario(s) occurring, especially where dividends as proposed within the rescue plan are assumed to be settled over the course of several months or a period after adoption of the rescue plan.

11.6 Evaluation of the forecast financials by key financial stakeholders

As a general principle, most stakeholders directly utilise the financial forecast information contained with the published business rescue plan to assess the overall proposal and the extent to which they may vote on such a plan (namely whether to agree to it, request an amendment, or reject the plan). Accordingly, and as highlighted above, the financial forecast information referenced in this chapter plays an important and integral part of stakeholder decision-making.

Notably there are a number of different stakeholders or persons interested in a business rescue plan, in particular the forecast financial information. The main categories of stakeholders likely to be interested in the financial information include, but may not be limited to, those listed below. The degree of financial sophistication of the stakeholder is also directly correlated to the degree to which the forecasts will be scrutinised. The credibility of the business rescue plan (and consequently the business rescue practitioner) can often depend on the veracity of the forecast information provided.

Illustrative examples have been provided to explain further why certain stakeholder groups may be interested in the financial forecast information presented in a business rescue plan:

- Employees, including where employees are also creditors: in this instance, employees will be interested in the security of their jobs. Financial forecast information provides insight into the future anticipated financial health and sustainability of the business. Financial information often read in context with the contents of the proposal section in the business rescue plan may further provide information in respect of assumed employee numbers, salary levels as well as any intended proposed retrenchments (which need to be clearly presented in the published business rescue plan);[453]

- Secured creditors such as bank lenders and finance lease providers: such creditors, whilst potentially in a more beneficial position than unsecured creditors, will be particularly interested in the forecast financial information where such lenders or finance providers have agreed to continue lending to the company post business rescue. In this instance, the ability of the business to continue trading solvently as a going concern with sufficient cash generation to settle such debts as they become due (especially in the context of such creditors having already been subject to increased risk and rescue proceedings) will be pivotal to such creditors' assessment of the financial information and hence also their decision making. Bank lenders may also in his context seek to gain a deep understanding of the financial information in question (and in particular cash flows) in order to be able to agree and monitor banking covenants, further highlighting the importance of financial forecast information for this stakeholder group;

- Preferent creditors, such as employees (employee costs incurred during the business rescue proceedings which remain unpaid) and post commencement finance providers (who

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[453] *National Union of Metalworkers of South Africa (NUMSA) obo Members and Others v South African Airways (SOC) Ltd and Others* (2021) 42 ILJ 1256 (LC).

may also be secured): whilst such creditors enjoy preferential status afforded to them by virtue of section 135 of the Companies Act 2008 their recovery may be subject to some dividend recovery over a period of time. As such the feasibility of the financial forecast information becomes of paramount importance;

- Unsecured creditors, such as trade suppliers and SARS: whilst some of these creditors may not intend to trade with the business going forward, a number of such creditors will seek to continue trading with the business post its exit from business rescue. Ongoing income tax, value added tax (VAT) and other agency tax collections also provide an important consideration for SARS in this context; and

- Shareholders: shareholders remaining in the business, new shareholders, or existing shareholders who may have the opportunity for some value recovery through mechanisms such as earn out clauses or trade out periods may also be interested in this forecast financial information.

Self-Assessment Questions for Chapter 11

Where necessary, refer to the Case Study and financial statements contained in Chapter 1 of these notes in order to answer the questions below.

Question 1

Section 150(2)(c)(iv) of the Companies Act 2008 requires only a projected balance sheet for the company and income statement for the ensuing three years. Briefly discuss this requirement and what can be done from a "best practice" perspective to enhance the information available to affected persons.

Question 2

Section 150(3)(a) of the Companies Act 2008 requires that a "notice" of any material assumptions on which the projections are based **must** be included. In terms of Fast Flights, list five assumptions that you believe will be material to the affected persons in understanding the financial projections.

Question 3

Section 150(3)(b) of the Companies Act 2008 states that alternative projections may be included based on varying assumptions and contingencies. In the context of Fast Flights, discuss a situation where this may be applicable and how you would incorporate the alternative projections into the business rescue proposal.

Question 4

What, in your opinion, is the purpose of including a balance sheet and income statements in the business rescue proposal?

Question 5

Who are the stakeholders / audience of the financial statements and what are they most interested in seeing in these financial forecasts?

Question 6 (this question is a variation on Question 1)

In terms of section 150(2)(c)(iv) of the Companies Act 2008 no cash flow forecast is required by the Companies Act. In your opinion, describe the importance of the cash flow forecast and how this could enhance an affected person / reader's understanding of the situation?

For feedback on this self-assessment exercise, see the document "Comment and Feedback on Self-Assessment Questions", which is made available to you as a separate document.

CHAPTER 12

THE PSYCHOLOGY OF BUSINESS RESCUE

12.1 What is the context and relevance of discussing the "psychology" of business rescue?

Whilst business rescue is a "process" and is governed by the application and interpretation of the rules and all the relevant sections of the of the Companies Act 2008, business rescue is in many ways as much a process involving people who are affected and who will ultimately engage, respond and react at a human level both emotionally and intellectually. Below is a brief and limited summary of some of the key people, parties or groupings involved in a business rescue, noting that some of whom will have a history with the company and others who will only become involved upon the commencement of the business rescue process – their individual interests, perspectives and motivation will vary greatly (and this too will change throughout the process and is neither uniform nor a static position):

- the board, executives, management, staff and contractors;
- creditors and shareholders;
- clients and customers;
- regulators;
- unions and bargaining councils;
- legal representatives and / or professional advisors (of any of the parties listed here);
- the business rescue team and the business rescue practitioner(s).

Given the above, it should be quickly apparent as to why business rescue is only really "procedural" at a legal and practical application of the Act level, but beyond that, each and every step of the way is surrounded by a host of people-related actions, considerations and consequences.

This section of the course notes seeks to take a practical and experience-based review of the principle considerations of some of the common challenges, threats and approaches to the people-orientated aspects of a business rescue. Whilst this is specifically around the psychology of "business rescue", there is much that goes on in "informal restructuring", which is consensual (that is, not a legal or statutory process as is the case in business rescue) typified by fewer stakeholders (more a restructuring between the company and their capital providers). For

business rescue practitioners this too is a good reference point for "managing the personalities" involved and how to de-personalise the situation and get a deal done.[454]

12.2 The required skills, experience, traits and attributes of the business rescue practitioner

The Companies Act 2008 sets out the rules and regulations pertaining to the experience and powers of the business rescue practitioner, with the CIPC as the custodian of licencing and monitoring (of aspects) of the rescue and certain actions of the business rescue practitioner. Nothing in these processes considers the attributes of successful business rescue practitioners; although these are somewhat subjective, it is nonetheless safe to say they are in the first instance similar to that of high calibre Chief Executive Officers (CEOs) or other executive board roles. A good / efficient business rescue practitioner must engender trust and provide authentic leadership. The business rescue practitioner role requires the highest level of integrity, independence, impartiality, drive and a sense of urgency and purpose – sometimes they must be a calming force and, equally, will need to be a catalytic force in different circumstances. The term "chameleon" is sometimes used to describe these qualities and other abilities to switch seamlessly between roles, modes and moods. Situational experience of turnarounds, financial and operational restructurings are a prerequisite in this role, but are not covered further in this Chapter beyond the referencing of these as critical or core skills.

Highly successful business rescue practitioners typically have high EQ (emotional quotient) which, when coupled with the above, equips them well in the challenges that often surround negotiations and interactions in business rescue proceedings and all its protagonists. They require patience, negotiation and motivational skills, plus they will need to hold themselves to the highest standards of transparency, inclusivity and be consultative when required (but equally will need to be able to, where necessary, switch from being consultative to being singularly driven, resolute and action-orientated). These skills and attributes require an innate subtlety so as to be able to "switch" between such roles without being seen to "play games", which could cause mistrust or come across as being disingenuous.

12.3 Majoring in business rescue practitioner "independence"

This is a really useful tool within the business rescue practitioner's grasp – when consulting with various stakeholder groups, particularly at the beginning of the rescue, business rescue practitioners often experience a high degree of scepticism, entrenched or embittered views from the (trade) creditors' recent dealings with the company in the lead up to rescue, and also resulting from the realisation that a rescue may result in significant shortfalls on pre-commencement obligations. In addition, creditors may believe (especially in voluntary business rescues) that the board and the business rescue practitioner are 100% aligned and that bias exists. Further down the line in the process (especially where a counter party sale is contemplated), the business rescue practitioner may face further preconceptions that they are "aligned" with the interests of the bidder.

[454] For additional reading material on informal restructuring, see R Marney and T Stubbs, *Corporate Debt Restructuring in Emerging Markets: A Practical Post-Pandemic Guide* (2021, Palgrave Macmillan).

This is entirely understandable; however, frequent verbalisation of the business rescue practitioner's obligation to be independent and actions that demonstrate this, goes a long way to curbing such suspicions and bias. An ongoing dialogue that explicitly makes verbal and written reference to the business rescue practitioner's independence and need to act in the interests of the affected persons, can turn the tide of such rhetoric and suspicion.

Building trust takes time, but in business rescue things need to progress faster than in the ordinary course – add to this the increase in virtual meetings then the task requires conscious and exponential effort. Language is a vital part of this quest for accelerating trust – making assumptions is risky, so rather pose questions that engender a feeling of inclusivity (without implying that everything is open to debate or consultation).

12.4 The business rescue practitioner's right to set boundaries

During business rescue proceedings there is extensive interaction with various stakeholders and affected parties (see paragraph 12.6 below). Very few of the meetings that take place in a business rescue are stipulated or codified by the Companies Act 2008 – many more are organic and arise during the progression of the business rescue process and therefore the business rescue practitioner is often the convener of such meetings and should be consistent, efficient and cautious with both the attendees and the agenda followed.

Section 145(3) of the Companies Act 2008 entitles creditors to form a creditors committee and that committee is entitled to "be consulted by the business rescue practitioner during the development of the business rescue plan" – this does not mean anything other than at the business rescue practitioner's discretion and for the contemplated purpose. Creditors (and their advisors) often misconstrue this as a "right" for them to convene meetings throughout the business rescue process and further to suggest or tell the business rescue practitioner what they think should happen throughout the process, but it is clear that creditors cannot "direct" the business rescue practitioner. Furthermore, there is nothing whatsoever that compels the business rescue practitioner to consult beyond the statutory requirements and, whilst in practice there are many more interactions and meetings, the agenda and attendees are entirely within the business rescue practitioner's remit and purview.

It should be noted that with reference to the business rescue practitioner's ability to meet with sub-sets of a creditor group, that this is perfectly permissible and commonplace. Outside of statutory creditor and affected persons meetings, the business rescue practitioner has free reign in this regard. For instance, where there are multiple landlords, it would not be unusual to have a landlords' meeting or even a sub-set of this if the scale of the number of landlords dictates. In multi-bank situations, again bi-lateral meetings between the business rescue practitioner and a lender are not unusual. That said, given earlier comments about "curiosity" and heightened levels of creditor sensitivity, thought must be given to the unintended consequences of such meetings being understood to have been held by a wider group of creditors.

12.5 Role played by the board and management (existing or new) in a rescue (including their statutory and practical role in assisting and reporting to the practitioner)

During the imposition of the control of a business rescue practitioner over a company and its affected parties, it is understandable that there is a need for the business rescue practitioner to provide early comfort around immediate concerns to a range of key stakeholders – and the board is no exception. As a point of departure, business rescue practitioners must understand and respect that in the lead up to the decision to file for business rescue, the cohesion of even a strong board and executive is strained. Risks and fears of reckless trading, and review of recent decisions and transactions, tend to split board cohesion into the beginnings of self-preservation and self-interest at director level. If this is true in well-run and cohesive boards, then it will be all the more apparent and acute in boards that are strained, or worse still, split into factions. The business rescue practitioner's powers and obligations of investigating the conduct of the board and the company, serves only to fuel such concerns.

Whilst the board in general will have likely taken significant strain in the lead up to filing for rescue, the business rescue practitioner needs to firstly assert control and authority – unless as a business rescue practitioner you have already had meaningful interaction with the board (as a result of performing what is referred to as "pre assessment"). This starts with a first meeting where it is important to set out the immediate priorities, whether you are allowing any of the board to retain authority or where you will want to make all decisions in the short term before delegating authority back to the board and / or individual directors. Bear in mind that section 140 – dealing with the general powers and duties of practitioners – says:

> "(1) During a company's business rescue proceedings, the practitioner, in addition to any other powers and duties set out in this Chapter –
>
> (a) Has full management control of the company in substitution for its board and pre-existing management;
>
> (b) May delegate any power or function of the practitioner to a person who was part f the board or pre-existing management of the company;
>
> (c) may
>
> (i) Remove from office any person who forms part of the pre-existing management of the company; or
>
> (ii) Appoint a person as part of the management of a company, whether to fill a vacancy or not subject to subsection (2)"
> [this subsection pertains to independence]

Be aware that many board directors and management will have been given legal advice and / or will have read the Companies Act 2008 to understand the impact of the process on them. As a result, a business rescue practitioner needs to be transparent but resist the urge to provide assurances that they do not plan on exercising these powers, only to find they may have to and thereby cause mistrust. A better approach (unless there is a pressing need to remove management or board members) is to talk openly about what is intended, but to be clear that

business rescue is a dynamic process where there are few, if any, absolutes. Take the board and management through the business rescue practitioner's obligations and powers and in that context apprise them of your opening stance, but be clear things may change and a business rescue practitioner will have to do what is necessary in any of those circumstances.

Talking to them regarding areas they themselves navigate (such as the fiduciary responsibilities of directors and prescribed officers) will remind them that they too have had to deal with such principles rather than codified or rule-driven situations. Building trust through a shared understanding and purpose is a critical point of departure for a business rescue practitioner's relationship with boards and management. In many instances a business rescue practitioner can benefit greatly from buildings trust with a board and leveraging their knowledge and capacity to perform functions (be clear on delegation and thresholds) allowing the business rescue practitioner to attend more broadly to the restructuring of the business.

12.6 The differing positions and psychology of various stakeholder groups

In paragraph 12.1 we covered a broad list of stakeholders. To be clear, this is wider than the Companies Act 2008-defined terminology of affected parties. See below for this definition; however, in the wider context of stakeholders it is important to balance transparency and disclosure with avoiding "over-reach". Humans exhibit natural curiosity, especially in unfamiliar and new circumstances, and business rescue is no exception. business rescue practitioners are well advised to be cautious not to either over-consult, over-answer or over-include more parties than are necessary (for example, shareholder meetings are not creditor meetings, which are not employee meetings – other than as provided for in the Companies Act 2008).

All-party meetings are difficult to manage and control, especially in a post-COVID 19 pandemic context with many such meetings held remotely. Breaking down stakeholder groups can be a useful way to "build up" a rescue plan by having plotted out what is needed from each group, and to meet to progress buy-in from their group and suggest / canvas what will be needed by them from other groups in order to make a deal (transaction) or process (such as trading out of rescue) palatable. The starting point for each group of stakeholders is that they often believe that they have been worst affected by rescue and have a blurred perception of other groups who have been less affected.

There are far too many of these examples of juxtaposed stakeholders, so it is easiest to take the two classic "lenses" or "protagonists", being that of debt and equity – the lenders (debt) will have a view that the value of the business now in rescue has diminished and that in the capital structure where "debt" sits above "equity" that the now diminished value of the company (whether listed or private) breaks in the debt – this expression is used by lenders to notify equity holders (shareholders) that they need to recapitalise with new equity if they wish to participate (also referred to as "equity being out of the money") – equity holders in turn would argue that if the lender were to restructure their debt, then the company can be rescued.

The intention of this example is not to provide insight into how a financial restructuring is typically effected, but rather to show the power dynamics and arguments that polarise various

stakeholders – the business rescue practitioner role is sometimes as mediator and other times as agitator to get entrenched positions moving through dialogue and negotiation. This dynamic above is aided by section 146, which deals with the rights of securities holders (shareholders) who are afforded the right to attend all meetings but, importantly under section 146(d), only vote on a business rescue plan if "the plan would alter the rights associated with the class of securities held by that person".

Where a deadlock ensues, the BRP will need to use all their skills (EQ, negotiation, persuasion – counter-arguments, etcetera) as conveners, arbitrators and agitators to reset these entrenched positions – used cautiously, the threat of the counter-factual (being the failure to rescue and conversion to liquidation) often provides sufficient leverage as both debt and equity fare badly in these circumstances (unless lenders are heavily over secured with readily realisable assets). But again, the tools available to business rescue practitioners are to persuade the parties that self-interest has harm for the wider stakeholders (employees, trade creditors) and a far-reaching socio-economic downside and risk of reputational damage.

12.7 The psychology of corporate dishonesty in business rescues

Regrettably, business rescue either as a reason for filing or subsequently due to discoveries during the rescue, cannot escape the challenge of fraud and dishonesty and the spectrum is wide from large scale, orchestrated fraud and abuse through to cases where management and directors' "judgement" was poor and they had crossed the Rubicon in terms of breaches of their fiduciary obligations, despite being "well-intentioned".

The starting point for this is that corporate dishonesty is at best a misnomer, as dishonesty is in the actions or omissions of individuals. Despite this vital distinction, the situation of fraud and dishonesty creates a significant challenge for business rescue practitioners who have the invidious task of investigating such occurrences. Business rescue practitioners are well advised to use their powers in section142(1) and at the outset ensure that they have access to and secure the "books and records" of the company. Rather unhelpfully, this is an antiquated term that has little guidance for the digital environment that is vast, complex and evolving. Business rescue practitioners are well advised to secure the services of experts in this field given the risk of being dispossessed of the data and records. Here the previous comments in paragraph 12.5 are relevant again in first setting out the "rules of engagement" for business rescue by the business rescue practitioner to the directors and management. Again, circumstances around fraud or other forms of dishonesty will dictate the forum, attendees, recording of discussions versus the general approach to ensuring compliance and assistance.

Importantly, business rescue practitioners must not lose sight of the task in hand of the business rescue. Business rescue means proceedings to facilitate the rehabilitation of a company that is financially distressed by providing for the development and implementation, if approved, of a plan to rescue the company to return it to solvency or achieve a better outcome than liquidation. This means considering all affected persons (and stakeholders in the wider sense) when determining how to drive this – it cannot mean in the event of fraud or misconduct losing the ability to achieve the above rescue goals solely to investigate fraud; this is the domain of

liquidation enquiries (section 417 of the Companies Act 1973) and the like (the interests of all affected persons need to be served in the widest sense). Here, business rescue practitioners must themselves tread the cautious path of dealing with a "broad church" of constituents and navigating the "grey".

12.8 Dealing with "hostage creditors"

In business rescue, creditors with "leverage" present real challenges and issues that require all the guile that a business rescue practitioner can muster. Examples in the context of the case study of an Airline is a classic – for example, the suppliers of aviation fuel are registered and regulated to operate onsite and, therefore, if such a creditor had a pre-commencement debt owing to them, as with all creditors with pre-commencement debt, the business rescue moratorium would freeze these amounts and be held over until dealt with in the business rescue plan. Unfortunately, from a negotiating standpoint the business rescue practitioner is at a disadvantage. This is because while the moratorium is legally sound and binding, commercially the registered and regulated aviation fuel supplier has commercial leverage. They can refuse to supply and the business rescue practitioner having no alternative supplier is faced with "treating one creditor differently to others". However, if they refuse to negotiate then they can be "starved out" by the hostage creditor.

A huge amount of experience and expertise is required to navigate the minefield of bargaining with a hostage creditor and avoiding other creditors crying "foul", or worse still realising they too have commercial leverage and exercising it, causing what is described colloquially as "a run on the bank". This refers to a situation where a bank is expected to collapse and investors withdraw their funds for fear that they will be trapped and the bank suffers accelerated outflows, accelerating the very event they, their advisors and the regulators are seeking to avoid. In this context, it merely means that if all creditors with leverage hold out for the payment of their pre-commencement debts then the rescue may fail as quickly as it started. These situations require immense experience, caution, strategic thinking and a strong dose of good fortune or luck.

12.9 Summary views on the psychology of business rescue

This chapter seeks to explore a very wide subject area. While internet search engines return a plethora of definitions of "psychology", the one that strikes the right chord here is "the scientific study of the human mind and its functions, especially those affecting behaviour in a given context".

The context business rescue practitioners must stay focused on, is that the main purpose of business rescue is clear and business rescue practitioners must develop and possess acute skills in pre-empting, reacting and managing these "behaviours" in the context of rescuing businesses (not to be confused with rescuing companies) for the benefit of affected persons (as per the Companies Act 2008) and in the wider context of furthering socio-economic goals in the South African context.

Self-Assessment Questions for Chapter 12

Question 1

If significant numbers of Fast Flights' customers who have paid in advance for flights were acutely worried that they will lose their money if the company fails, how could the business rescue practitioner and team firstly pre-empt this and secondly manage customers to reduce such a cash outflow risk?

Question 2

Given the heavy staff complement (especially with extra growth in numbers pre-business rescue), how could the business rescue practitioner seek to manage and mitigate risk without promising what cannot necessarily be controlled in terms of a need to retrench?

Question 3

Following the acquisition of new aircraft through secured lending from Big Money Bank, how might the business rescue practitioner seek to persuade the bank not to place excessive pressure on them to immediately return all of these aircraft?

Question 4

Given that Mr L Block is removed by Mr A Float the business rescue practitioner, how should or might the business rescue practitioner seek to manage the immediate concerns (whether a rational or irrational thought) of the rest of the board that they too may be at odds with the business rescue practitioner? What steps and discussions might ensue to keep them aligned and motivated to assist with the business rescue?

Question 5

Given the decision to terminate the business rescue, how might the business rescue practitioner keep the remaining directors both incentivised, motivated and committed to assisting in the orderly wind down / liquidation?

For feedback on this self-assessment exercise, see the document "Comment and Feedback on Self-Assessment Questions", which is made available to you as a separate document.

CHAPTER 13

DISCHARGE OF DEBTS AND CLAIMS

13.1 Introduction

This chapter focuses on the discharge of debts and claims by way of a business rescue plan and how the business rescue process ensures that optimum results are produced not only for the company, but for its creditors as well.

In the first instance, this chapter considers the position of dissenting creditors where a business rescue plan has been adopted by the majority of the creditors through the "cram-down principle". The concept of a "fresh start" for financially distressed companies is then discussed, and finally, the position of sureties of the company in business rescue.

13.2 The cram-down principle

One of the duties of a business rescue practitioner is to prepare and propose a business rescue plan to the creditors and, if applicable, the shareholders of a company in financial distress for them to consider.[455] The plan will be put to a vote at a meeting of creditors, and approved on a preliminary basis if it is supported by more than 75% of all the creditors who voted, and at least 50% of the independent creditors' voting interests, if any. If the plan does not alter the rights of shareholders of any class, approval of that plan on a preliminary basis will also constitute the final adoption of that plan, subject to satisfaction of any conditions upon which the plan is contingent.[456] If the plan does alter the rights of shareholders but the majority of the affected shareholders nevertheless support the adoption of the plan, then the plan will be adopted.[457]

Once adopted, the business rescue plan is not only binding on the company, but it also binds both secured and unsecured creditors of the company, as well as shareholders. This is so regardless of whether or not the creditors and shareholders were present at the meeting in which the plan was adopted, whether or not they voted in favour of adoption of the plan; or in the case of creditors, whether or not they had proven their claims against the company.

The principle or phenomenon of imposing the business rescue plan upon dissenting as well as absent creditors is known as "cram-down", and it is provided for under section 152(4) of the Companies Act 2008. The court in *DH Brothers Industries (Pty) Ltd v Gribnitz NO and Others*[458] confirmed that the voting interests of the non-assenting creditors and absent parties upon which the business rescue plan is "crammed down" must not be more than 25%.

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[455] Companies Act 2008, s 152 (1)(a).
[456] D Davis *et al*, *Companies and other Business Structures* (3rd ed, Oxford University Press Southern Africa, Cape Town, 2013) at 399, para 12.7.3.
[457] Companies Act 2008, s 152(3).
[458] 2014 (1) SA 103 (KZP).

In *African Banking Corporation of Botswana Ltd v Kariba Furniture Manufacturers (Pty) Ltd and Others*,[459] the court noted that the cram-down principle is "indispensable to the successful implementation of a business rescue plan" due to the fact that it is binding on dissenting creditors and all shareholders, regardless of whether or not they were present or voted against the adoption of the plan. The court also explained that the principle effectively discourages creditors from refusing or holding out for better treatment, and it allows the business rescue to proceed, despite the objections of one or more disgruntled creditors.[460]

The cram-down principle originated in the Chapter 11 of the United States Bankruptcy Reform Act, 1978, commonly referred to as the US Bankruptcy Code (the Code). In terms of the Code, a majority of the creditors (both in value and in number of voting creditors) must vote in favour of the plan and the "group without the required majority will be deemed to have consented to the plan on condition that the creditors in this group will probably not be placed in a worse financial position by the insolvency plan than they would be without this plan". Under the Code, the dissenting creditors must have reasonable participation in further advantages flowing from the plan.[461] The objective behind the provision is the prevention of abusive or arbitrary obstruction of the plan by creditors.

The Companies Act 2008, on the other hand, does not contain the deeming provision in respect of dissenting creditors. However, the effects of the provisions in the Companies Act 2008 are similar since the dissenting creditors are bound to the plan as if they had agreed to it. It is also not a condition under South African law for the adoption of the business rescue plan that the dissenting creditors must not be placed in a worse financial position by the business rescue plan than they would be without the plan. In fact, a disgruntled party does not have a judicial remedy under the Companies Act 2008 to seek to set aside the adoption of a business rescue plan and, as such, it is not open to any affected person, after the plan has been adopted, to seek to set it aside.[462]

Section 154 of the Companies Act 2008 deals with the discharge of debts and claims. Subsection (1) provides that the adoption and implementation of the business rescue plan will result in the creditors losing their rights to enforce their debts or part of their debts on the basis that they have acceded to the discharge of such debts. This provision only applies to creditors who acceded to the discharge of their debts.[463] This should be contrasted against the legal position and rights of dissenting creditors under section 154(2), which is expanded upon below.

The provisions of section 154(2) of the Companies Act 2008 preclude creditors from enforcing debts against the company, save to the extent provided for in the business rescue plan. Unlike subsection (1), this subsection is not restricted to creditors who supported the business rescue plan - it applies to those creditors upon which the business rescue plan was "crammed down", thus ensuring that the business rescue plan effectively binds all the creditors.

[459] 2013 (6) SA 471 (GNP).
[460] 2014 (1) SA 103 (KZP).
[461] *Ibid*.
[462] 2013 (6) SA 471 (GNP).
[463] Companies Act 2008, s 154(1).

The Supreme Court of Appeal delivered a judgment during 2021 in the matter of *Van Zyl v Auto Commodities (Pty) Ltd*[464] which bears significant relevance to the issues dealt with in this chapter. It is therefore apposite to deal briefly with the facts in *Van Zyl*. The respondent, Auto Commodities (Pty) Ltd (Auto Commodities), supplied petroleum products on credit to Blue Chip Mining and Drilling (Pty) Ltd (BCM). BCM's chief executive officer (CEO) at the time – the appellant, Mr Van Zyl – bound himself as surety for its resulting debts. BCM was placed under business rescue in December 2014. A business rescue plan was adopted in June 2015 and subsequently implemented. After substantial implementation of the plan, business rescue terminated during January 2017. Subsequently, Auto Commodities sued the appellant in his capacity as surety for the shortfall of BCM's original indebtedness. Auto Commodities succeeded with its claim. The matter was appealed to the Supreme Court of Appeal.

The broad question on appeal was whether the appellant was liable under the deed of suretyship to pay the amount claimed by Auto Commodities.

The Supreme Court of Appeal held that debts of dissenting creditors are not discharged under section 154(1) of the Companies Act 2008, and further, that "unlike the requirement in s 154(1) that the creditor accede to the plan, s 154(2) operates against the creditor even if they fought tooth and nail against the adoption of the business rescue plan".

The court in *Van Zyl* explained that section 154(1) of the Companies Act 2008 addresses the discharge of debts, while section 154(2) merely limits the ambit of enforcement of the debt. The debt owed to a dissenting creditor therefore continues to exist, but is enforceable only to a limited extent, and this limitation does not necessarily indicate that the debt is discharged. This point is dealt with further under paragraph 13.3 below in relation to the position of sureties.

In alignment with section 152(4), section 154 effectively ensures that the business rescue plan is binding on all creditors. It is also clear that the provisions of these sections aim to ensure that the interests of individuals do not trump those of the majority.

13.3 The fresh start for financially distressed companies

The fresh start is a concept which originated in American insolvency law and has been adopted and applied across different insolvency law regimes.[465] As the term suggests, the idea behind a fresh start is that debtors who are *bona fide* or honest in their conduct should be afforded the opportunity of a fresh start which ultimately results in the discharge of their debts entirely.[466] In South Africa, the fresh start principle insofar as it relates to individual consumer debtors is governed by section 129(1)(b) of the Insolvency Act. This is contrasted to a fresh start for a financially distressed company through Chapter 6 of the Companies Act 2008. The principle as it applies to financially distressed companies, is dealt with below.

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464 2021 (5) SA 171 (SCA).

465 A Boraine and M Roestoff, "Fresh Start Procedures for Consumer Debtors in South African Bankruptcy Law", *International Insolvency Review* (2 March 2002) at 1-11, p 9.

466 *Ibid*.

In South Africa, the concept of a "fresh start" finds application through business rescue proceedings. Business rescue allows the financially distressed company to reach compromises on certain debts with its creditors, whilst still allowing creditors to recover monies due to them – which, albeit less than the original debt, typically represents more than what the creditor would recover in a liquidation scenario. Business rescue thereby affords a meaningful fresh start to the company, giving the company an opportunity to act responsibly towards its creditors whilst continuing to operate.

A further benefit afforded to financially distressed companies through the business rescue provisions in the Companies Act 2008 is the general moratorium on the ability of creditors to enforce claims under section 133(1). The provisions afford the company space to carefully consider its affairs without the risk of enforcement proceedings being brought against it. In *Timasani (Pty) Ltd (in business rescue) and Another v Afrimat Iron Ore (Pty) Ltd*[467] the court confirmed that for purposes of business rescue proceedings, "it is generally accepted that a moratorium on legal proceedings against a company under business rescue is of cardinal importance since it provides the crucial breathing space for a period of respite to enable the company to restructure its affairs. This allows the practitioner, in conjunction with the creditors and other affected parties, to formulate a business rescue plan designed to achieve the purposes of the process".[468]

It is evident that South African law-makers considered that a necessary balance must be struck between the interests of the creditor to the proper recovery of its claims, weighed against those of the debtor in having its debts discharged and returning to economic activity.

13.4 The position of sureties

The Supreme Court of Appeal in *Van Zyl v Auto Commodities (Pty) Ltd*[469] confirmed that a suretyship is accessory in nature, and that as a result, the liability of a surety depends upon the existence of the obligations that a principal debtor may have. As such, since the discharge of a debt under section 154(1) of the Companies Act 2008 results in the company's debt itself being extinguished, in such a situation the surety would likewise be discharged given the accessory nature of a suretyship.

Conversely, it was noted in paragraph 13.1 above that the provisions of section 154(2) of the Companies Act 2008 preclude creditors from enforcing debts against the company, save to the extent provided for in the business rescue plan, but the provisions do not result in the discharge of the debt. The section is not restricted to creditors who supported the business rescue plan, but it also applies to those creditors upon which the plan was crammed down. The court in *Van Zyl* explained that insofar as a dissenting creditor is subject to cram-down, the debt continues to exist albeit that the creditor may only enforce the debt to the extent provided in the plan.

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[467] (91/2020) [2021] ZASCA 43 (13 April 2021).
[468] *Idem*, at para 25.
[469] [2021] 3 All SA 395 (SCA).

The continued existence of the debt implies that the balance of dissenting creditors' debts may still be enforced against sureties of the company. The court in *Van Zyl* noted that "[t]he distinction which the language of the section supports is a distinction between the discharge of a debt (ss(1)) and a personal protection in favour of the company against the enforcement of a debt (ss(2)). And since the practical effect, as between the creditor and the company, is the same, namely that the creditor cannot enforce the claim beyond the extent permitted by the plan, the change in wording in ss(2) is indicative of the legislative distinction having been drawn principally, although not necessarily solely, with claims against sureties in mind".

The court confirmed that section 154(2) went no further than precluding a creditor from pursuing claims against the company – it did not affect or extinguish the liability of a surety to a debt. The court added that "If the whole or a part of the debts of a company become unenforceable as a result of the adoption and implementation of a business rescue plan, the fact that some creditors may pursue the balance of their claims against sureties, who will have a right of recourse against the company, does not negate the purpose of business rescue".

It should be borne in mind, however - noting the accessory nature of a suretyship mentioned above - that the ability of dissenting creditors to enforce the balance of their debts by recourse to sureties is dependent upon the terms of the relevant deeds of suretyship.

Self-Assessment Questions for Chapter 13

Where necessary, refer to the Case Study contained in Chapter 1 when answering the questions below.

Question 1

Answer the statement below by stating whether it is **TRUE** or **FALSE**. Provide reasons for your answer.

The business rescue plan will not be binding on Big Money Bank as the existing fleet of 15 aircraft have been registered as security in their favour for the loan facilities provided to Fast Flights.

Question 2

Advise Jumbo Jet Proprietary Limited on what their legal position is as a minority creditor.

Question 3

What is the "requisite majority" of creditors that need to approve a business rescue plan?

Question 4

What is the benefit of the fresh start principle as it applies to Fast Flights? Do you think that Fast Flights can have a fresh start in these circumstances?

Question 5

It is clear that certain creditors have taken matters into their own hands pursuant to Fast Flights' failure to make payment of the amounts owed to them. What is the purpose of the general moratorium on creditors in business rescue proceedings and does this moratorium apply to the creditors in question?

Question 6

Set out the position of Mr B Sky in so far as he bound himself as surety for Fast Flights' debts. Are Mr B Sky's obligations relinquished pursuant to the commencement of Fast Flights' business rescue proceedings as he suggests?

For feedback on this self-assessment exercise, see the document "Comment and Feedback on Self-Assessment Questions", which is made available to you as a separate document.

CHAPTER 14

AREAS WHERE INSOLVENCY LAW AND BUSINESS RESCUE OVERLAP

14.1 Introduction

Both business rescue and liquidation provide means of dealing with financially distressed companies, depending on the extent of financial distress, and future prospects. The *UNCITRAL Legislative Guide on Insolvency Law* describes "striking a balance between liquidation and reorganization", as one of the key objectives of an effective and efficient insolvency law, and provides, *inter alia*, that:

> "The first key objective of maximization of value is closely linked to the balance to be achieved in the insolvency law between liquidation and reorganization. An insolvency law needs to balance the advantages of near-term debt collection through liquidation (often the preference of secured creditors) against preserving the value of the debtor's business through reorganization (often the preference of unsecured creditors and the debtor). Achieving that balance may have implications for other social policy considerations, such as encouraging the development of an entrepreneurial class and protecting employment. Insolvency law should include the possibility of reorganization of the debtor as an alternative to liquidation, where creditors would not involuntarily receive less than in liquidation and the value of the debtor to society and to creditors may be maximized by allowing it to continue. This is predicated on the basic economic theory that greater value may be obtained from keeping the essential components of a business together, rather than breaking them up and disposing of them in fragments. To ensure that insolvency proceedings are not abused by either creditors or the debtor and that the procedure most appropriate to resolution of the debtor's financial difficulty is available, an insolvency law should also provide for conversion between the different types of proceedings in appropriate circumstances."[470]

The *UNCITRAL Legislative Guide on Insolvency Law* also prescribes that insolvency laws ought to achieve a balance between, *inter alia*, the following:

- Private rights and public interests and the alternative means available to address those public interests;[471]
- The interests of individual creditors and those of the estate which, in terms of the recovery of assets through avoidance actions, coincide with the collective interests of all creditors;[472]

[470] *UNCITRAL Legislative Guide on Insolvency Law* at 11, para 6. Available at https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/05-80722_ebook.pdf.
[471] *Idem*, at 271, para 70.
[472] *Idem*, at 139, para 162.

- The desirability of facilitating high levels of creditor participation and the need to ensure that the creditor representation mechanism remains efficient and cost-effective and avoids creditors involving themselves in matters that will not have an impact on their interests;[473]

- The roles of the court, the insolvency representative, the debtor and creditors, in particular in terms of oversight and supervision;[474] and

- The extent to which supervision or approval by creditors is required (including defining both the acts and decisions that require approval and the procedure for obtaining that approval) and the independence of the insolvency representative and the desirability of speed and cost-effectiveness in the conduct of the insolvency proceedings.[475]

With the above in mind, what follows will deal with certain points of comparison between the two procedures available to deal with companies across the spectrum of financial distress, as well as points at which they intersect. When viewed as part of the same system of law, with the same policy basis and aims, it is fundamental that business rescue and liquidation are not treated as entirely distinct, and that insolvency legislation broadly speaking enables the two alternatives to supplement each other in achieving the overall aims of the overall insolvency system. It is important to appreciate the differences and interplay between the two.

Before looking at certain comparisons between business rescue and liquidation, and the interplay between the two procedures, it will be instructive to provide an overview of the law relating to the latter, which is not the primary focus of this course.

14.2 Law applicable in relation to liquidation

Liquidation may in many cases be a more appropriate solution to dealing with a company that finds itself in financial distress, particularly in cases where there is no reasonable prospect of rescuing the company. The appropriate procedure in such cases is set out in Chapter XIV of the Companies Act 1973, which remains applicable to insolvent companies.[476] Although the chapter provides for the "winding-up" of both solvent and insolvent companies, it now only has limited application to solvent companies.[477]

Section 339 of the Companies Act 1973 provides that "[i]n the winding-up of a company unable to pay its debts the provisions of the law relating to insolvency shall, in so far as they are applicable, be applied *mutatis* mutandis in respect of any matter not specifically provided for by

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[473] *Idem*, at 190, para 75.
[474] *Idem*, at 190, para 77.
[475] *Idem*, at 192, para 82.
[476] Companies Act 2008, Sch 5, item 9(1).
[477] *Idem*, Sch 5, item 9(2) – this item excludes the application of ss 343, 344, 346, and 348 to 353 of the Companies Act 1973 in respect of the winding up of solvent companies "except to the extent necessary to give full effect to the provisions of Part G of Chapter 2" (of the Companies Act 2008). See *Boschpoort Ondernemings (Pty) Ltd v Absa Bank Ltd* [2014] 1 All SA 507 (SCA). The Companies Act 2008, s 81 provides for the winding-up by the court of solvent companies.

this Act". This means that one must have regard to provisions of the Insolvency Act in so far as they may apply to the company under liquidation.

In the context of business rescue, one needs to be aware of the interplay between the two procedures (this will be discussed under paragraph 14.4 below), but the following are broadly relevant for the purposes of when an application for liquidation is brought.

14.2.1 Winding-up of insolvent companies by the court

In terms of section 344(f) of the Companies Act 1973, a company may be wound up by the court if it is unable to pay its debts as described in section 345. The latter section provides for two instances in which a company will be deemed to be unable to pay its debts if:

- a creditor (by cession or otherwise) to whom the company is indebted in a sum not less than R100 then due has served a demand on the company (by leaving such demand at its registered office) requiring it to pay the sum due;[478]
- any process issued on a judgment, decree or order of any court in favour of a creditor of the company is returned by the sheriff or the messenger with an endorsement that he has not found sufficient disposable property to satisfy the judgment, decree or order or that any disposable property found did not upon sale satisfy such process;[479] or
- it is proved to the satisfaction of the court that the company is unable to pay its debts.[480]

The court is required to take into account the contingent and prospective liabilities of the company in its determination of whether the company is unable to pay its debts for the purposes of the above.[481]

Where the court has ordered the winding-up of a company, the company's directors are required, within 14 days[482] of the order, to lodge two certified copies of a statement of the company's affairs (in the prescribed form) with the Master of the court.[483] Similarly to the context of business rescue applications, a winding-up of the company is deemed to commence at the time that the application for winding-up is presented to the court.[484]

During the course of a winding-up by the court, the liquidator is required to have regard to any directions that may be given by resolution of the creditors or members or contributories of the company at any general meeting.[485] Any person aggrieved by an act or decision of the liquidator

[478] Companies Act 1973, s 345(1)(a)(i).
[479] *Idem*, s 345(1)(b).
[480] *Idem*, s 345(1)(c).
[481] *Idem*, s 345(2).
[482] Or within such extended time as the Master may permit.
[483] Companies Act 1973, s 363(2).
[484] *Idem*, s 348.
[485] *Idem*, s 387(1)

may, on notice to the liquidator, bring an application to court, whereupon the court may make any such order as thinks just.[486]

14.2.2 Creditors' voluntary winding-up

It is also possible for a company (which is not an external company) to be wound up voluntarily by a special resolution of the shareholders.[487] Such resolution authorising the winding-up of the company may provide that the winding-up shall be a creditors' voluntary winding-up, in which case it must be registered in terms of section 200 of the Companies Act 1973.[488]

Prior to such a resolution for a creditors' voluntary winding-up being passed, the company's directors are required to place a statement as to the affairs of the company (in the prescribed form) before the meeting convened for the purposes of passing such resolution.[489]

A voluntary winding-up commences at the time of the registration of the resolution in terms of which it is authorised,[490] and – unless otherwise provided – the liquidator appointed may exercise all of the statutory powers given to him in the context of a winding up by the court, subject to any directions that may be given by the company's creditors.[491]

14.2.3 Appointment of liquidator

A provisional liquidator may be appointed after the granting of a provisional liquidation order, or – in the case of a voluntary winding up – registration of the resolution authorising the winding-up. [492]

After a final winding-up order is granted, or a special resolution has been registered (as described above), the Master will call first meetings of creditors[493] and members[494] for the purposes of *inter alia* nominating a person or persons for appointment as liquidator,[495] and thereafter appoint one or more liquidators for the purposes of conducting the winding-up proceedings. [496] Such person will replace any provisional liquidator appointed on such basis.

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[486] *Idem*, s 387(4).
[487] *Idem*, s 349.
[488] *Idem*, s 351(1).
[489] *Idem*, s 363(1).
[490] *Idem*, s 352(1).
[491] *Idem*, s 351(2).
[492] *Idem*, s 368.
[493] *Idem*, s 364(1)(a).
[494] *Idem*, s 364(1)(b).
[495] *Idem*, ss 364(1)(a)(iii) and 364(1)(b)(ii).
[496] *Idem*, s 367. Section 369 provides for the manner of determination by the Master of the person to be appointed as liquidator.

14.2.4 Powers of liquidators

The liquidator's powers are set out in section 368 of the Companies Act 1973. These are broader in certain respects than the powers given to a business rescue practitioner, although one should be mindful of the fact that they are given for a different purpose: whereas a practitioner's powers are granted in order to rescue a financially distressed company, a liquidator's mandate to wind-up a company will entail, *inter alia*, making payments in final settlement of claims before the company's existence will cease. A final liquidator's powers granted in terms of section 368(1) may be exercised without the sanction of any other party (including the Master).[497]

Section 69(3) of the Insolvency Act also provides a powerful tool that can be utilised in circumstances where it is suspected that any property, book or document belonging to a company under liquidation is concealed[498] or otherwise unlawfully withheld from the liquidator. In such circumstances, a magistrate with jurisdiction over the area where such thing is suspected to be may – based on finding reasonable grounds to arise from a statement made on oath – issue a warrant to search for and take possession of such property, book or document.

14.2.5 Voidable dispositions and other impeachable transactions

Section 340 of the Companies Act 1973, read with the relevant provisions of the Insolvency Act, provides that the certain transactions may be set aside by the court or the liquidator in the event of the company being wound up and unable to pay all its debts.[499] For the purposes of what follows, it should be noted that "disposition" is defined in the Insolvency Act to mean "any transfer or abandonment of rights to property and includes a sale, lease, mortgage, pledge, delivery, payment, release, compromise, donation or any contract therefor, but does not include a disposition in compliance with an order of the court".[500] The term thus has a broad meaning, and also includes the giving of a suretyship.[501]

14.2.5.1 Voidable preferences

Section 29 of the Insolvency Act provides generally that *any* disposition of property (i) made not more than six months before the company's liquidation which (ii) had the effect of preferring one of its creditors (or sureties)[502] above another, where (iii) immediately after the making of such disposition the liabilities of the company exceeded the value of its assets may be set aside; unless the person in whose favour the disposition was made proves that (a) the disposition was

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[497] M S Blackman *et al*, *Commentary on the Companies Act* at 14–328-2.

[498] The provision reads "… concealed upon any person, or at any place or upon or in any vehicle or vessel or receptacle of whatever nature, or is otherwise unlawfully withheld from the trustee concerned …".

[499] Companies Act 2008, s 340(1).

[500] Insolvency Act, s 2.

[501] E Bertelsmann *et al*, *Mars: The Law of Insolvency in South Africa* 10ed (2019) at 276; and *Swanee's Boerdery (Edms) Bpk (in liquidation) v Trust Bank of Africa Ltd* 1986 (2) SA 850 (A) at 859B-C. The authors of Bertelsmann state that "[a] wide meaning should be given to the word 'disposition' to include every act by which an insolvent parts with any asset in whatever form in his estate".

[502] Insolvency Act, s 30(2).

made in the ordinary course of business and that (b) it was not intended thereby to prefer one creditor above another.[503]

With regard to the effect of the disposition, it is only necessary to show, objectively,[504] that "one creditor has in consequence of the disposition received more pro rata than or payment earlier than another with equal rights".[505] The determination of whether the debtor's liabilities exceed its assets immediately after the disposition is similarly an objective test:[506] the liquidator must prove this "clearly and conclusively",[507] on a preponderance of probabilities.[508] In this regard, claim documents in relation to proved claims are considered *prima facie* proof of the company's liabilities, they cannot be used as evidence that the transactions reflected in them occurred.[509]

The effect of this provision is that once the liquidator is able to prove that there was a disposition (as defined) of property by the company made to a particular person, and the elements (i) to (iii) set out above are present, the court will set the transaction aside, unless the person in whose favour the disposition was made is able to show elements (a) and (b).[510] Thus, in order to succeed in having a voidable preference set aside in terms of section 29, the liquidator does not have to prove either that the disposition was *not* made in the ordinary course of business, nor that it was intended to prefer one creditor above another.

14.2.5.2 Undue preferences

A transaction may also be set aside by the court where the company made a disposition of property at a time when its liabilities exceeded its assets, with the intention of preferring one of its creditors (or sureties)[511] above another.[512] Such "undue preferences" are similar to voidable preferences, except that there is no requirement for the disposition to have been made within six months prior to the date of liquidation.

Although the absence of a time limit is in a sense less restrictive in that this element need not be proved, the liquidator will not benefit of the presumption in relation to the *intention* underlying the disposition, and will have "the onerous task of proving that the disposition was made with the intention of preferring one of the insolvent's creditors above the other" (not merely that this was the effect), as well as that the debtor was insolvent at the time of making the disposition.[513] Whereas the relevant party will be able to raise one of the two defences mentioned above once

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[503] *Idem*, s 29.
[504] *Simon NO v Coetzee* [2007] 2 All SA 110 (T) at 114.
[505] E Bertelsmann *et al*, *Mars: The Law of Insolvency in South Africa* 10ed (2019) *at 287; Isaacson & Son v Van Druten's Trustee 1930 GWL 33 at 36.*
[506] *Venter v Volkskas Ltd* 1973 (3) SA 175 (T) at 179A.
[507] E Bertelsmann *et al*, *Mars: The Law of Insolvency in South Africa* 10ed (2019) at 287.
[508] *Nicholls & Whitelaw NO v Akoo* 1948 (4) SA 197 (N); *Lipshitz NO v Landmark Consolidated (Pty) Ltd* 1979 (2) SA 482 (W) at 494.
[509] E Bertelsmann *et al*, *Mars: The Law of Insolvency in South Africa* 10ed (2019) at 287.
[510] *Idem,* at 284-5; and *Nicholls & Whitelaw NO v Akoo* 1948 (4) SA 197 (N) at 200.
[511] Insolvency Act, s 30(2).
[512] *Idem*, s 30(1).
[513] E Bertelsmann *et al*, *Mars: The Law of Insolvency in South Africa* 10ed (2019) at 284.

the elements of a voidable preference have been proved, once the elements of an undue preference are proved, no defence is available to the person who benefitted from the disposition.[514]

14.2.5.3 Collusive dispositions

If the company, in collusion with another person, disposed of its property prior to liquidation in a manner which had the effect of prejudicing its creditors or preferring one above another, this disposition may also be set aside be the court.[515] Moreover, in the event that the company had suffered a loss in consequence of such disposition, the person with whom the company colluded will be liable for the amount of such loss.[516]

To prove "collusion", more is required than simply the effect of the agreement underlying a disposition being to prefer one creditor over another; there must be some "agreement which has a fraudulent purpose".[517]

14.2.5.4 Dispositions not made for value

When a company has made a disposition whereafter its assets still exceed its liabilities, but such disposition was made without the company receiving adequate compensation (for example, a donation), it will be possible for such a transaction to also be impeached by the liquidator. It will be necessary to prove "(a) that there was a disposition of property; (b) that it was made by the insolvent [company]; (c) when it was made; (d) in whose favour or for whose benefit it was made; and € that value was not received".[518]

In the event that such disposition was made more than two years before the date of the company's liquidation, the liquidator will have to prove that the company's liabilities exceeded its assets (factual insolvency) after the disposition was made.[519] If the disposition was made less than two years prior to the date of liquidation, on the other hand, the transaction may be set aside on proof of this fact alone,[520] unless the person to whom the disposition was made can discharge the onus of proving that the company's assets exceeded its liabilities (factual solvency) after such disposition.[521] If it is proved that the liabilities of the company at any time after the making of the disposition exceeded its assets by less than the value of the property disposed of, such disposition may be set aside only to the extent of such excess.[522]

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[514] *Idem,* at 299.
[515] Insolvency Act, s 31(1).
[516] *Idem*, s 31(2) provides that parties to such collusion may be liable for loss and subjected to a penalty. E Bertelsmann *et al*, *Mars: The Law of Insolvency in South Africa* 10ed (2019) at 299; and *Estate Naidoo v Paruk* 1921 NLR 1; *Baldachin's Trustees v Sloman & Sloman* 1944 SR 55.
[517] E Bertelsmann *et al*, *Mars: The Law of Insolvency in South Africa* 10ed (2019) at 299; and *Meyer NO v Transvaalse Lewendehawe Koöperasie Bpk* 1982 (4) SA 746 (A) at 771C-D.
[518] E Bertelsmann *et al*, *Mars: The Law of Insolvency in South Africa* 10ed (2019) at 275.
[519] Insolvency Act, s 26(1)(a).
[520] E Bertelsmann *et al*, *Mars: The Law of Insolvency in South Africa* 10ed (2019) at 281.
[521] Insolvency Act, s 26(1)(b).
[522] *Idem*, s 26(1).

14.2.5.5 Other affected contracts

In addition to the above bases for setting aside transactions, the following are instances where the Insolvency Act provides for insolvency proceedings to impact certain pre-existing contractual arrangements with an insolvent, without requiring an application to court to have the relevant transaction set aside:

- If the company had entered into a contract for the acquisition of immovable property which was not transferred to it, the liquidator may elect to either enforce or abandon the contract.[523]

- If the company had received any movable property in terms of a contract of purchase and sale providing for payment of the purchase price to be upon delivery of such property, without paying the purchase price in full, the seller may be able to reclaim such property in terms of the provisions of section 36.

- Where the company is the lessee in a contract of lease, such contract is not automatically terminated, but the liquidator may determine the lease by notice in writing to the lessor, who shall be entitled to claim compensation for any loss which he may have sustained by reason of the non-performance of the terms of such lease.

- Where the company is the employer in a contract of service, such contracts are suspended with effect from the date of the granting of a liquidation order,[524] after which time neither any employee(s) in terms of such contract(s) so suspended be required to render service to the company,[525] and nor will any employment benefit accrue.[526] The liquidator may terminate such contracts of employment, subject to the requirements of subsections 38(5) and (7).[527]

- Where the company is an "authorised user", "participant", "clearing member", or "client", as defined in section 1 of the Financial Markets Act 2012, or a party to a transaction to which the "exchange rules", "depository rules", or "clearing house rules" (as defined) apply, if where the company's obligations in respect of which any such transaction (entered into prior to its liquidation) have not been fulfilled, the company's liquidator shall be bound by any termination of transactions or revocation of instructions (in terms of the relevant rules) by the market participant to which the company owes any such obligation.[528]

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523 *Idem*, s 35; the liquidator may be required, by written notice from the other party calling upon the liquidator to make such election (and give notice thereof) within six weeks, failing which such party may apply to court for cancelation of the contract.
524 *Idem*, s 38(1).
525 *Idem*, s 28(2)(a).
526 *Idem*, s 38(2)(b).
527 *Idem*, s 28(4).
528 *Idem*, s 35A.

- Where the company has unperformed obligations under any "master agreement"[529] concluded in accordance with standard terms such as those published by the International Swaps and Derivatives Association, or obligations arising out of such agreement(s) in respect of assets in which ownership has been transferred as collateral security, all such obligations shall terminate automatically at the date of its liquidation, the value of such obligations being calculated at market value as at that date, such values being netted, the net amount being payable by the company.[530]

14.2.5.6 Application of the actio Pauliana *at common law*

The *actio Pauliana* is a common law remedy that is a part of South African law, and although applicable more widely than instances of insolvency, may provide an additional basis on which transactions concluded by the debtor in fraud may be impeached. A claimant under this action would have to prove that "the disposition diminished the debtor's assets, that the recipient had not in fact received his own property, that the intention to defraud existed and that the fraud had had its effect".[531]

14.3 Comparisons with business rescue

Remembering the *UNCITRAL Legislative Guide on Insolvency Law* recommendations set out in the introduction to this chapter relating to maximisation and preservation of value, cost-effectiveness, the potential for abuse of process, the role of the court as well as that of the debtor and creditor in oversight and supervision, and the protection of the interests of creditors and their participation in the process, this part will draw comparisons between liquidation and business rescue in relation to supervision and oversight of the respective procedures, investigation into the conduct of the debtor company's management, and the possibility of accessing finance.

14.3.1 Supervision and oversight

Although there is professional oversight in relation to business rescue practitioners, which are required to be accredited in order to act as such, once in office, they are not under any supervision. Interference with the conduct of the practitioner is difficult, and will typically require recourse to the courts. This may be particularly unsatisfactory when there are concerns with the person holding office, and creditors or other interested parties seek their removal.

From a creditors' perspective, for example, it is easier to remove a liquidator than a business rescue practitioner, because the former does not require a court application. If creditors are dissatisfied with the provisional liquidator, he can be removed at the first meeting called by the Master, at which a final liquidator can be nominated. In the case of a final liquidator, removal

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[529] As defined in the Insolvency Act, s 35B(2).
[530] *Idem*, s 35A.
[531] E Bertelsmann *et al*, *Mars: The Law of Insolvency in South Africa* 10ed (2019) at 307; *Hockey NO v Rixom NO* 1939 SR 107; *Fenhalls v Ebrahim* 1956 (4) SA 723 (N); and *Kommissaris van Binnelandse Inkomste v Willers* 1999 (3) SA 19 (SCA) at 28-29.

and replacement can be done by requesting that the Master do so by way of a simple letter, setting out the basis on which the liquidator's removal is being sought, rather than needing to formally apply to court. Whereas an application to remove a practitioner can also be opposed, thus not only creating a significant hurdle for the person(s) seeking removal, but also having the potential to cause significant delays in obtaining an outcome. In the case of incompetent or dishonest liquidators, the Master has the power to remove such persons from office, whereas there is no similar power for the CIPC to remove a business rescue practitioner from office.

Section 417 of the Companies Act 1973 empowers the Master, in any winding-up of a company unable to pay its debts, to at any time after the winding-up order has been granted, summon a wide range of persons before him to provide information relating to the trade, dealings, affairs or property of the company being wound up.[532] A person so summoned may be examined by the Master under oath, either orally or by written interrogatories, which may be reduced to writing and signed. There is no similar practical oversight by the CIPC in the case of business rescue.

From an insolvency practitioner's perspective, the oversight of the Master limits the discretion exercised in dealing with the company under supervision. Interference by the Master may hinder a liquidator's ability to act expeditiously in attending to the company's affairs, often resulting in the process taking longer than the six months typically envisaged for the process to be brought to completion.

There are, however, obvious benefits to the Master's involvement and oversight: the liquidator is kept from acting in a manner unbecoming, because he knows not only can he be relatively easily removed, but he generally remains accountable to the Master, who will monitor his compliance with prescribed time limits, and who is able at any time to convene a meeting to interrogate any conduct called into question.

A problem for the company may arise "where a winding-up application has been brought by a creditor and the winding-up process is suspended by the launch of a business rescue application",[533] since the result will be that the company will be unable to operate pending the outcome of the business rescue application.[534]

14.3.2 Investigation into conduct of company's management

Although the business rescue practitioner is obliged to investigate the company's affairs for the purpose of determining whether a reasonable prospect of rescue exists as soon as practicable after his appointment,[535] and given full management control[536] of the company during his

[532] Companies Act 1973, s 417(1).
[533] Levenstein 10-34. See s 131(6) of the Companies Act 2008.
[534] Levenstein 10-34.
[535] Companies Act 2008, s 141(1).
[536] *Idem*, s 140(1)(a).

period of appointment (including powers of delegation[537] and removal[538] in respect of the existing management), his investigative powers are severely limited.[539]

It may be desirable to be able to ascertain the exact cause of the company's financial distress by interrogating directors and pre-existing management of the company under supervision, but there is no formal procedure provided in the context of the business rescue procedure for a practitioner to do so.[540]

Whereas a practitioner must engage with management on a more informal basis, a liquidator has a statutory power[541] to conduct a formal insolvency inquiry, during which he may interrogate directors, management and any other person who has knowledge of the trade, dealings and affairs of the company prior to its winding-up.[542] This may be particularly useful to elicit information from directors that they may be less willing to volunteer in the context of a business rescue, where directors anticipate remaining in office, and (hopefully, assuming the success of the procedure) continuing to run the business once it has been rescued. In a liquidation context, the directors will have essentially handed over the company to be wound-up and ultimately deregistered, whereas in business rescue, directors may have placed the company into business rescue to take advantage of the moratorium on claims in the hope that the company will be set back on its feet to give them another chance.

Knowing that they will not be opening themselves up to interrogation may encourage directors with something to hide to make use of business rescue rather than liquidation, which may be a more appropriate solution in some cases. The failure to provide more extensive investigative powers to a business rescue practitioner "also supports the perception that the rescue process serves to protect creditors from properly investigating the conduct of directors and management in support of claims for reckless conduct (section 22), and civil claims (section 218) provided for by the 2008 Companies Act".[543] Consequently, as pointed out by Levenstein,[544] recourse to business rescue is often had in order to avoid "the inquisitive focus of the liquidator on the conduct of directors before the liquidation application", and potentially being held personally liable[545] for debts of the company.

Aside from the business rescue practitioner not having the special investigative powers given to liquidators, a practitioner is also not able to set aside impeachable transactions in terms of the Insolvency Act. Given that the business rescue procedure is much newer than liquidation, the law relating to the powers of the practitioner is less clear, having had less time to be developed by court decisions on issues that arise in practice.

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537 *Idem*, s 140(1)(b).
538 *Idem*, s 140(1)(c).
539 Levenstein 10-33.
540 *Ibid*.
541 In terms of ss 417 and 718 of the Companies Act 1973.
542 Levenstein 10-33.
543 *Ibid*.
544 *Idem*, at 8-45, note 211.
545 In terms of s 424 of the Companies Act 1973, read with s 22 of the Companies Act 2008 (dealing with reckless trading).

14.3.3 Access to finance in winding down of company

Both liquidation and business rescue, with its secondary goal being obtaining a better return for creditors than would be obtained by an immediate liquidation, could be employed to wind a company down without restoring the business to profitability. For example, in either procedure, the company's business can be sold as a going concern to another entity.

Although the need for the administrator (whether the liquidator or business rescue practitioner) to obtain finance may less often arise in a winding-down context, this is far easier to do within the business rescue framework. Whereas section 386(5) of the Companies Act 1973 allows a liquidator to apply to court to borrow funds, a business rescue practitioner is able to borrow money without any formalities being involved. The result is a saving of time, effort and expenses in business recue when compared to liquidation. So-called "post commencement finance" in business rescue has been a topic of much discussion and is often a vital ingredient for the success of a rescue – particularly when the practitioner is in pursuit of the primary goal of rescue, being to enable to company to continue in existence on a solvent basis.

From a creditor's perspective, a business rescue practitioner may be more costly than a liquidator, and a practitioner's remuneration (not overseen by the Master, as is the case with a liquidator) is also given a statutory priority,[546] even over secured "pre-commencement" creditors.

14.3.4 Rights of employees

When a company is liquidated, its existence ceases and it is therefore a logical consequence that any contract of employment would terminate (although initially the contracts would merely be suspended). This will necessarily result in a loss of employment, and as far as creditors may be creditors in respect of salaries or wages that remain unpaid, they will rank alongside the company's other concurrent creditors.

In the case of business rescue under the Companies Act 2008, employees are given statutory protection in three important ways: first, their employment contracts are recognised, and the powers of the practitioner (or court) to encroach on their contractual rights is limited. Section 136(1)(a) provides that during a company's business rescue (and despite any provision of an agreement to the contrary), the company's employees immediately before the commencement of business rescue will "continue to be employed on the same terms and conditions, except to the extent that – (i) changes occur in the ordinary course of attrition; or (ii) the employees and the company, in accordance with the applicable labour laws, agree different terms and conditions". Whereas the business rescue practitioner ordinarily has the power to cancel or suspend contractual obligations due by the company for the duration of business rescue,[547]

[546] Companies Act 2008, s 135(3), which treats the practitioner's remuneration as part of the "post commencement finance".

[547] The practitioner may unilaterally suspend such obligations in terms of the Companies Act 2008, s 136(2)(a) and may apply to court for cancellation in terms of s 136(2)(b).

employment contracts are expressly excluded.[548] When a company is liquidated, the employees' contracts are suspended, and will then terminate.

Secondly, the Act expressly incorporates labour law protection, and requires that any retrenchments contemplated in the business rescue plan be subject to section 189 and 189A of the Labour Relations Act 1995 (dealing with dismissals based on operational requirements).[549]

Thirdly, where employees continue to render services to the company while under business rescue, they become post-commencement creditors in so far as their claims for remuneration arise during the course of business rescue. Section 135(1) provides that to the extent that any remuneration, reimbursement for expenses or other amount of money relating to employment becomes due and payable by a company to an employee during the company's business rescue proceedings, but is not paid to the employee – (a) the money is to be regarded as post-commencement financing; and (b) will be paid [in accordance with a preferential ranking].[550] Importantly, if a business rescue is superseded by a liquidation order, section 135(4) provides for the preference conferred in terms of that section to remain in force, except to the extent of any claims arising out of the costs of liquidation.

14.4 Interplay between two procedures

As already mentioned, business rescue and liquidation are two procedures that should complement one another; the former being applicable only to companies with a reasonable prospect of rescue. The following are instances of where there is interplay between business rescue and insolvency procedures.

14.4.1 Conversion from business rescue to liquidation

At the beginning of the business rescue process, whether commenced by resolution or by court order, it is possible for an affected person, on having received notice (as required),[551] to apply to court for an order in terms of section 132(2)(a) setting aside either the business rescue resolution, or the order placing the company under business rescue (as the case may be) and instead placing the company into liquidation. An application to, and also oversight by, the court is always necessary to convert business rescue to liquidation, because once under supervision, it is not possible for the company to place itself under liquidation by resolution.[552]

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548 Companies Act 2008, s 136(2A)(a)(i) and 136(2A)(b)(i).
549 *Idem*, s 136(1)(b).
550 *Idem*, s 135(1)(b) provides for payment "in the order of preference set out in subsection (3)(a)".
551 *Idem*, s 129(3)(a) requires that company, after having adopted a business resolution, must – within five business days thereof – publish a notice of such resolution to all affected persons. In the case commencement by court order, the affected persons will have received notice of the application in terms of s 131(2)(b), whereafter each affected person has the right to participate in the hearing of the application in terms of s 131(3).
552 See s 129(6), applicable when the company has commenced business rescue by resolution, and s 131(8), applicable when the court has placed the company under business rescue on application in terms of s 131.

"If reorganisation proceedings fail or implementation does not succeed, there may be a need for orderly conversion of proceedings to liquidation",[553] in which circumstances, business rescue will terminate once the court has concerted the business rescue proceedings to liquidation proceedings.[554] During business rescue, if a practitioner finds that there is no longer a such a reasonable prospect, he is obliged to inform the court, the company, and all affected persons,[555] and bring a court application for an order discontinuing the business rescue proceedings and placing the company into liquidation.[556]

Other grounds for such conversion include instances where the plan to rescue the company provided for in section 150 (or modifications thereto) cannot be approved, or has failed to be implemented; where there has been a successful challenge to, or substantial and material default by the debtor in respect of obligations under, such plan; and where creditors have decided, by majority vote at a meeting of creditors, to terminate the business rescue.[557]

Section 141(2) of the Companies Act 2008 provides that if, at any time during business rescue proceedings, the practitioner concludes that there is no reasonable prospect for the company to be rescued, the practitioner must so inform the court, the company, and all affected persons in the prescribed manner; and apply to the court for an order discontinuing the business rescue proceedings and placing the company into liquidation.

A question that may arise in the context of a conversion from business rescue to liquidation relates to the status of the practitioner's actions taken during office, and in terms of a partially implemented business rescue plan – for example, are any transactions effected by the practitioner void or otherwise impeachable? According to Levenstein:

> "Actions such as payments to creditors or sales of assets taken by a practitioner in good faith and in the best interests of the company cannot be overturned by a liquidator. The practitioner would have taken action in terms of the provisions of Chapter 6 and would thus be protected. In any event, the disposition sections set out in the Insolvency Act which deal with voidable transactions . . . are unlikely to apply to a business rescue process because there is no *concursus creditorum*".[558]

In the event that business rescue proceedings are superseded by a liquidation order, section 135(4) of the Companies Act 2008 provides that the preferences conferred by section 135 (which deals with the ranking of claims in business rescue) "will remain in force, except to the extent of any claims arising out of the costs of liquidation".[559] Although a business rescue

[553] Levenstein 5-105.
[554] Companies Act 2008, s 132(2)(a)(ii).
[555] *Idem*, s 141(2)(a)(i).
[556] *Idem*, s 141(2)(a)(ii).
[557] Levenstein 5-105.
[558] *Idem,* at 8-46 to 8-47, noting that "a *concursus creditorum* would be applicable only once a company is placed into liquidation".
[559] Companies Act 2008, s 135(4).

practitioner may not act as liquidator in a subsequent liquidation, the costs and remuneration of the practitioner is thus given preference both during and after business rescue.[560]

> "Section 135(4) provides the practitioner, after the conversion of business rescue proceedings into liquidation proceedings, with no more than a preference to claim remuneration against the free residue after the costs of liquidation. But this is before the claims of employees for post commencement wages, those who have provided other post commencement finance, whether those claims were secured or not, and of any other unsecured creditors."[561]

14.4.2 Conversion from liquidation to business rescue

Section 131(6) of the Companies Act 2008 clearly envisages conversion of liquidation to business rescue: the section provides for the suspension of liquidation proceedings in circumstances where "liquidation proceedings have already been commenced by or against the company at the time an application is made [for business rescue]". Such suspension will operate until either the court has adjudicated upon the application, or – in the case that the business rescue order is granted and the proceedings are converted – the subsequent business rescue proceedings end.

A court is empowered, in terms of section 131(7) of the Companies Act 2008 to place a company into business rescue at any time during the course of any liquidation proceedings.[562] This section allows the court a wide discretion to allow recourse to business rescue when it may present a more viable means of dealing with a financially distressed company.

In practice, "[b]usiness rescue proceedings are often initiated as a counter to a liquidation application" where a creditor has brought an application to court, based on an unpaid debt, for the winding-up of the company,[563] and it is easier for an affected person to intervene and ask the court to grant a business rescue order instead than to defend an indefensible claim.[564] Practitioners, therefore, initially took the view that conversion out of liquidation would only be possible at the interim stages, prior to the final liquidation order.

There is authority, however, to the effect that conversion to business rescue may take place, even at a later stage of the liquidation process, and even after the appointment of the final liquidator. In *Van Staden v Angel Ozone Products (in liquidation) CC*,[565] the court found that such conversion may take placed "no matter how far the liquidation and winding-up proceedings

[560] Levenstein 9-96.

[561] Per Khampepe J in the Constitutional Court decision of *Diener NO v Minister of Justice and Correctional Services and Others* 2019 (4) SA 374 (CC), at para 21, which effectively confirmed the decision of the Supreme Court (2018 (2) SA 399 (SCA)) to dismiss the appeal in respect of the finding made by the High Court in Pretoria as court of first instance ([2016] ZAGPPHC 1251).

[562] *Koen and Another v Wedgewood Village Gold & Country Estate (Pty) Ltd* 2012 (2) SA 378 (WCC), at para 8.

[563] Levenstein 8-45.

[564] *Ibid.*

[565] 2013 (4) SA 630 (GNP).

might have progressed".[566] The court in *Van Staden* based its finding on the policy underlying the procedures, noted that business rescue, on the one hand, aims to protect the rights and interests of all relevant stakeholders during the rescue process, liquidation proceedings "are meant to ensure that no one particular stakeholder (creditor) gains an advantage over other creditors".[567] The court concluded that: "if the rescue proceedings are a better option than the liquidation proceedings, I see no reason why such liquidation proceedings cannot be converted into supervision and rescue proceedings irrespective of how far advanced the liquidation or the winding-up proceedings might be".[568]

Subsequently, the Supreme Court of Appeal, in *Richter v Absa Bank*,[569] confirmed that an application for business rescue can be made after final order of liquidation, Dambuza AJA reasoning as follows:

> "I do not think the phrase 'liquidation proceedings' in any way alters the significance of what is meant by liquidation. In terms s 136 (4) of the Act if liquidation proceedings have been converted into business rescue proceedings, the liquidator is regarded as a creditor of the company to the extent of any outstanding amounts owing to him or her for any remuneration due for work performed, or compensation for expenses incurred before the commencement of business rescue proceedings. Under s 1 (1) and Schedule 5 (9) of the 1973 Act, which applies to liquidation of insolvent companies, the definition of 'liquidator' includes a provisional liquidator and a final liquidator. Consequently, the conversion of liquidation to business rescue even after a final liquidation order has been granted, was clearly envisaged by s 136 (4)." [570]

This means that, as the law stands, the Companies Act 2008 envisages that an application for business rescue may suspend any part of the proceedings occurring after the order of winding-up, until the point in time at which the company is deregistered.[571]

This approach has been criticised as being problematic in that it gives rise to the situation where a liquidators face a possible conversion to business rescue once they have already "sold portions of a business as a going concern and disposed of or realised assets and drawn up a liquidation and distribution account".[572] There is at least some consolation in the fact that the court is obliged to "take cognisance of the interests of all stakeholders and whether the conversion to business rescue will in fact result in the outcomes envisaged by section 128(1)(b)".[573] As mentioned in the introductory part of this chapter, there are policy reasons for an expeditious

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566 Henochsberg 471.

567 *Van Staden v Angel Ozone Products (in liquidation) CC* 2013 (4) SA 630 (GNP), at para 30.

568 *Ibid*.

569 2015 (5) SA 57 (SCA).

570 *Idem*, para 12; a footnote in the judgment here reading "See also: *Henoschberg on the Companies Act 71 of 2008* issue 9 at 479" (*sic*).

571 Levenstein 8-47.

572 *Idem,* 8-46. See also A Loubser, "The business rescue proceedings in the Companies Act of 2008: concerns and questions (part 1)", (2010) *TSAR* 501 at 511-512.

573 Levenstein 8-46.

liquidation in certain circumstances as much as they may form a basis for attempting to rescue a failing business in others.

Self-Assessment Questions for Chapter 14

Where necessary, refer to the Case Study contained in Chapter 1 when answering the questions below.

Question 1

Was Mr A Float correct in deciding to investigate routes to exit business rescue proceedings?

Question 2

Question 2.1

On what basis would business rescue proceedings in this context be terminated, and what would this involve?

Question 2.2

Would there be any potential advantage to this course of action over remaining under business rescue?

Question 2.3

What would the possible disadvantages be if this course of action is followed?

For feedback on this self-assessment exercise, see the document "Comment and Feedback on Self-Assessment Questions", which is made available to you as a separate document.

CHAPTER 15

SECTION 155 COMPROMISES WITH CREDITORS

15.1 Introduction

Although a compromise by a company with its creditors cannot be achieved whilst a company is in business rescue, ironically section 155 dealing with such a compromise is contained in Chapter 6 which deals with business rescue.

15.2 Meaning of "compromise"

The term compromise is not defined in the Companies Act 2008. Under the Companies Act 1973 there was a distinction drawn between a compromise by a company with its creditors and a scheme of arrangement by a company with its shareholders.[574]

Section 155 only allows for an arrangement or compromise by a company of its financial obligations with its creditors or the members of any class of its creditors. Schemes of arrangement with shareholders are now regulated by section 114 of the Companies Act 2008. A compromise has been held to be an agreement to settle a dispute over rights or to modify rights not in dispute where a difficulty exists with the enforcement of the rights.[575]

Arrangement by comparison is a category of agreements not involving any dispute over rights or difficulty in their enforcement, the only difficulty being getting the parties to agree.[576]

15.3 Requirements for a section 155 compromise

A compromise must not have the effect of it being *in fraudem legis*.[577] A compromise or arrangement must not involve a company in an *ultra vires* act and a creditor cannot be made a party to a compromise if it would be *ultra vires* for it to do so.[578]

Only the board of a company (which by definition includes the member(s) of a close corporation) or a liquidator of a company that is being wound-up may now propose an arrangement or a compromise of its financial obligations. They can make such a proposal at any time except when the company is engaged in business rescue proceedings. The proposal can thus be made even if the company is not financially distressed, before it is in liquidation, during its liquidation proceedings or after such proceedings have terminated.

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[574] See Companies Act 2008, ss 311 and 312.
[575] *Sneath v Valley Gold Limited* [1893] 1 CH 477 494 (CA); and *Ex Parte Bruyns: in re Coverite (Pty) Ltd* 1968 (1) SA 51 W (52).
[576] *Re Guardian Assurance Co* (1917) 1 CH 431 441 (CA); *Ex Parte Cyrildene Heights (Pty) Ltd* 1966 (1) SA 307 W 308.
[577] *Namex & Du Preez v Garber; In re: Die Boerebank Beperk* 1963 (1) SA 806 W at 813.
[578] *Namex & Mercian Investments (Pty) Ltd v Johannesburg City Council* 1990 (1) SA 560 (W) 573.

The reason why it cannot be brought during rescue proceedings is because rescue proceedings in effect amount to a compromise between a company and its creditors. These procedures are thus mutually contradictory or incompatible in the sense that one could not or should not during rescue proceedings invoke the provisions of section 155.

15.4 History of section 155 (predecessors found in earlier legislation)

Section 103 of the Companies Act 46 of 1926 was the predecessor to section 311 of the 1973 Companies Act. At its heart the section 311 scheme of arrangement provided for a court to approve a transaction between a company and its members or creditors even where all of those creditors or member and creditors did not agree to the transaction.

As long as the threshold of value of claims and number of creditors / members were achieved their decision was in the result binding on those who did not participate and even those who dissented.

The procedural requirements for a section 311 application were as follows:

- a liquidation order (usually an application to the High Court);
- an application by the provisional liquidator or liquidator to the High Court for leave to convene meetings of creditors or members;
- the holding of the meeting where essentially the votes were taken; and
- where the requisite thresholds were achieved then an application back to the High Court reporting on the outcome of the meeting on the vote and seeking the sanction of the High Court to the compromise or scheme and seeking the discharge of the company from provisional or final liquidation.

By their very nature these procedures were costly, cumbersome and thus not available to small and medium-sized companies and certainly not to close corporations.

15.5 The procedures in terms of section 155

In terms of this section a company may at any time (except whilst under business rescue) through its board, or if in liquidation by its provisional or final liquidator, propose by way of a letter an arrangement or a compromise of its financial obligations to all of its creditors or to all of the members of any class of its creditors. They simply now deliver a copy of this proposal in the form of a letter with a notice convening a meeting to consider the proposal as such.

The proposal is delivered to either every creditor of the company or every member of the relevant class of creditors who are going to be compromised and to the CIPC. There is no application to court as with section 311 of the Companies Act 1973.

Creditors or members of the class of creditors who are to be compromised then attend the meeting and vote thereat.

If the requisite threshold (dealt with later) is achieved, the company then applies to the High Court[579] for an order approving the proposal. This is the only time the court's involvement is required.

This application must be served on all creditors having an interest in the matter even those who voted in favour of the proposal.[580]

After the court sanctions the compromise the company must:

- within five business days file a copy of the order with the CIPC; and thereafter
- attach to each copy of the company's Memorandum of Incorporation (MOI) that is kept at the company's registered office or elsewhere a copy of the order.

The section 155 procedure is thus far less formalistic, far more practical to implement and far less costly when compared to the section 311 procedures. It also now applies to close corporations. From a cost and procedural perspective in terms of section 155 compromise is now within the reach of all companies and close corporations.

15.6 All creditors or any class of its creditors

The Insolvency Act identifies three classes of creditors. These three classes are:

(1) secured creditors – those who have security title against assets owned by the company;

(2) preferent creditors – those creditors who have preferences in an insolvency as created by the Insolvency Act;[581] and

(3) concurrent creditors – those are the unsecured and the non-preferent creditors.

With regard to classes of creditors and the determination thereof, our courts have held as follows:

> "it is objectionable as a general rule for creditors or different classes to deliberate and vote on a compromise together, and that is why separate

[579] As defined in the Companies Act 2008, s 128(1)(e).
[580] *The Commissioner of South African Revenue Services v Logikal Consulting (Pty) Ltd and Others* 2019 (6) SA 472 GP and *The Commissioner of South African Revenue Services v Cross Atlantic Properties (Pty) Ltd and Others* [2017] ZA GPPHC 554.
[581] Insolvency Act, ss 96, 98, 99, 101 and 102.

> meetings of secured, preferent and concurrent creditors are invariably convened"[582]

and further that:

> "there is authority for the proposition that, in the exercise of its discretion .... the court may refuse to sanction a compromise when it learns that a creditors meeting which was required to and did endorse the arrangement, though constituted in strict compliance with its earlier directions, was in truth an assembly of different classes."[583]

Further, as Steyn J held in *Ex Parte Venter and Another NNO; In re Rapid Mining Supplies (Pty) Ltd (in provisional liquidation); African Gate & Fence Works Limited Intervening*:[584]

> "in my opinion the responsibility for determining what creditors to summon to the different meetings as constituting separate classes rests ultimately with the applicant who applies for the holding of such meetings and thereafter for the sanctioning of a compromise agreed to by the requisite majority at those meetings. If such meetings are incorrectly convened or constituted and different classes of creditors are improperly brought together in one meeting, the applicant runs the risk of having his application refused."

Thus, classes of creditors should be determined according to creditors' various interests and rights. Those with the same rights and interests should vote in a class of creditors convened for them to vote on the compromise.

Applying then the three classes referred to in the Insolvency Act it is recognised that even in each class there are creditors who may have different interests and rights.[585] If so, these creditors should not vote together simply because they may be classified as secured or preferent or concurrent.

In the *Commissioner of South African Revenue Services v Logikal Consulting (Pty) Ltd*,[586] Van Der Linde J found that although the SARS and the employees of a company are classified in the Insolvency Act as preferent creditors, they may have different rankings as was the case in this matter. The employees (as preferent creditors) were per the offer / proposal to receive 100 cents in the rand on their claims, yet the SARS (also a preferent creditor) was going to receive 20 cents in the rand. In addition, SARS submitted that by law it was precluded from supporting a compromise of a tax debt. The judge, after referring to Raulinga J in the *The Commissioner of*

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582 *Ensor NO v South Pine Properties (Pty) Ltd* 1978 (2) SA 755 (N) 763A.
583 *Ibid*, 764G.
584 *Ex Parte Venter and Another NNO; In re Rapid Mining Supplies (Pty) Ltd (in provisional liquidation); African Gate & Fence Works Limited Intervening* 1976 (3) SA 267 (O) 276A.
585 *The Commissioner of South African Revenue Services v Logikal Consulting (Pty) Ltd and Others* 2019 (6) SA472 GP.
586 *Ibid*.

South African Revenue Services v Cross Atlantic Properties (Pty) Ltd and Others,[587] which found that SARS was precluded from entering into a compromise and not being persuaded that Raulinga J was wrong in arriving at his conclusion, considered himself bound by Raulinga J to the following effect:

> "[27] the applicant and the employees of the first respondent could not have formed one class of creditors, and could not validly have met and voted as one class of creditors under Section 155 of the Act. The procedure under Section 155 cannot be invoked if the first respondent would have achieved the same objective of a compromise between the first respondent, its employees and the applicant without the court's intervention. Moreover the applicant was precluded by Section 201 and 203 of the Tax Administration Act, 28 of 2011, from entering into the alleged compromise; it thus was not a valid compromise under Section 155 of the Act."

So concluded Van Der Linde J:

> "[60] in my view, the respondents have thus not shown that their grouping together of SARS with the five employees into one class complied with the requirements of 155(2) of the Act."

Thus notwithstanding that creditors are in the same grouping (that is, secured, preferent or concurrent), if their interests and rights are different then separate meetings should be held for those creditors so that creditors with the same interests and the same rights can engage, discuss and vote on whether to accept or reject the proposal.

In *Rosen v Bruyns NO*,[588] Cillie JP said:

> "it is clearly envisaged that creditors with conflicting interests but similar rights should come together to discuss the acceptance of the offer of the compromise."

With regard to contingent creditors it was held in *Namex (Edms) Bpk v Kommisaris Van Binnelandse Inkomste*[589] that every contingent creditor should be treated as a separate class of creditor. The court held further that SARS was not to be treated as a contingent creditor because of the peculiarity that tax is only paid after relevant assessments are issued and thus the assessment was a pre-requisite for the enforceability of a claim. The court found that because tax claims come into existence before assessments are issued SARS should not thereby be classified as contingent.

Where the rights of a particular class of creditors are not affected by the scheme (that is, where a particular class of creditor's rights are unaffected or may be paid one hundred cents in the Rand)

587 [2017] ZA GPPHC 554.
588 1973 (1) SA 815 (T) 820G.
589 1994 (2) SA 265 (A) 291.

it is not necessary to convene a meeting of such class to vote on the compromise. Certainly such creditors cannot object to the scheme as they are not allowed to object to schemes held in other classes.

If there is only one member in a particular class it is advisable that a meeting be held. However, in such a case the actual meeting may be dispensed with and the members' consent to the scheme filed in due course.[590]

Clearly then the proposal and the notice convening the meeting must be given to:

- every creditor of the company where all creditors are being compromised; or
- to all members of the relevant class of creditors if they only are to be compromised,

whose name or address is known to or can reasonably be obtained by the company.[591]

15.7 Content of the proposal

The proposal is dealt with in section 155(3) of the Companies Act 2008. It is self-explanatory and provides that:

- The proposal must be divided into three parts as follows:
  - Part A – background;
  - Part B – proposals; and
  - Part C – assumptions and conditions.
- The proposal must contain all information reasonably required to facilitate creditors in deciding whether or not to accept or reject the proposal.[592]

The required contents of each part is clearly set out in the Companies Act 2008.[593]

The content of the proposal is almost identical to the content of the proposal in a business rescue plan, save that it does not contain the details of a business rescue practitioner's fee nor when it is proposed that the company will exit rescue.

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[590] *Ex Parte Massing & Ingram (Pty) Ltd* 1942 WLD 204.
[591] Companies Act 2008, s 155(2)(a).
[592] *Idem*, s 155(3).
[593] *Idem*, s 155(3)(a), (b) and (c).

15.8 Requirements for the proposal to be adopted by creditors

All creditors if they are all being compromised, or creditors or members of relevant classes of creditors for successful adoption of the plan must achieve:

- 75% in value of the creditors in toto or in each class of creditors as the case may be; and
- the majority of creditors in number,[594]

present and voting in person or by proxy at the meeting called for the purpose of considering the proposal.[595]

The above requirements apply to only those creditors who vote at the meeting in person, or if they are not there in person by proxy. Those who do not vote have no say in whether the proposal is accepted or rejected. Thus, if only two creditors owning claims of small or relatively small value vote, their votes only are taken into consideration. Once the vote is adopted by the class it is binding on all creditors in that class.

The details of the meeting must be provided in a notice simultaneously with the proposal.

Although not specified in the Companies Act 2008, it is advisable that a chairman should be nominated to preside over the meeting. All of these details should be set out in the proposal.

The proposal may also stipulate for the appointment of a receiver, and this too is advisable. If the proposal does so stipulate, it must set out in detail the functions and duties of the receiver and his remuneration. Both roles (that is, of the chairman and receiver) should be set out in full detail in the scheme together with their duties and obligations. Certainly the courts when asked to sanction the proposal will require this information and will need to take all of this into consideration when exercising their discretion and in reaching its decision on whether or not to sanction the compromise as set out in the proposal.

The court must also take into consideration the number of votes and whether it is just and equitable at the end of the day to sanction the proposal. To assist the court a chairman must allow for those present to ask questions to evaluate the proposed compromise or arrangement. Those creditors present at the meeting are entitled to a reasonable opportunity to be heard. The chairman must ensure that these creditors' rights are catered for and given effect to.

As stated above, the chairman's powers are not set out in the Companies Act 2008 and regard should be had to the case law under, *inter alia*, section 311 of the Companies Act 1973 and the principles enunciated pursuant to these judgments as to their powers, duties, functions and roles.

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[594] In each class, as the case may be.
[595] Meaning that if there are 20 creditors, there should be at least 11 of them voting for approval of the proposal.

15.9 Adopted proposals – what is next?

The Companies Act 2008 specifies that a company may apply to court for an order approving the proposal.

A proposer would be ill-advised not to apply to court for an order approving the proposal. It is only once the courts have sanctioned the proposal that it is binding on everyone, including those who did not attend the meeting to vote, those who did not vote at all and those who voted against it.

If the proposer or any other party to the arrangement does not give effect to any of its terms or conditions after it has been made an order of court, such person is not acting in contempt of an order of court.

In this regard in *Buechel v Graf*[596] Selikowitz J said:

> "The effect of the sanctioning of a scheme of arrangement (in terms of Section 311) has been considered by our courts on several occasions … summarised the position in Parker v W G B Kinsey & Co (Pvt) Ltd 1988 (1) SA 42 (ZS)
>
> "To my mind, it is of fundamental importance to have regard to the effect of the sanctioning of a compromise or arrangement, subject, of course, to registration of the order pursuant to s 167(3) of the Act. I comprehend it to be this: the sanction is not an order of Court *ad factum praestandum*, a contravention of which is punishable by contempt of Court. It merely gives to the compromise or arrangement contractual force as between those bound by it, deriving such force, not from their actual consent, but by operation of law. The rights and obligations of the parties bound are determined by the terms of the compromise or arrangement, express or implied. They are not to be sought outside the confines sanctioned by the Court. Questions relating to validity and interpretation follow normal contractual principles, for the act of sanction does not convert the compromise or arrangement into an order of Court. The Court has no greater power over it than in any other sort of contract. It cannot judicially condone a default in performance, nor can it relieve a party bound by it from the consequences of its operation …
>
> Once it is appreciated that to sanction a compromise or arrangement does not mean that its intrinsic character is any less contractual - for its provisions do not become an order of Court - it seems to me to follow that a vital breach would enable an aggrieved victim, as with any other form of contractual relationship, to approach the Court for an order of cancellation. He has a right to do so. Indeed, in a situation where there are other interested parties, it would be normal and desirable to seek a judgment of cancellation so that the status of the contract is not left in doubt, but is well recognised."

[596] 2001 JDR 0706 (C) 6 to 7.

In *Cohen NO v Nel and Another*[597] the applicant, who had been appointed the receiver for the creditors of a company under a scheme of arrangement sanctioned by the court, sued respondent for monies alleged to be payable in terms of the scheme. At the hearing the respondents applied for leave to file further affidavits to prove that the arrangement had lapsed by reason of the failure of a condition precedent embodied therein. The application was opposed on the ground that the affidavits were entirely irrelevant. It was submitted that once the arrangement was sanctioned by the court, it became binding and that its consequences could only be avoided by the arrangement being set aside. Franklin J rejected the submission. He found that it was open to respondents to allege and prove, despite the court's sanctioning of the arrangement, that one of the conditions precedent had not been fulfilled, causing the offer to lapse.

Franklin J referred with approval to the remarks *Ex parte De Wet NO; In re Mackville Motors (Pty) Ltd (in liquidation)*[598] where Hiemstra J said:

> "To sanction the compromise does not mean that its terms become an order of Court. It means that the parties to the arrangement are authorised to go ahead with it, and they are bound to it. The liquidator is not relieved of his functions. On the contrary, the sub-section expressly says that the liquidator is bound to the terms of the compromise. In most compromises particular functions are entrusted to the liquidator in order carry out the arrangement. In this one, too, the liquidator still has duties to perform in regard to the proving of claims by creditors, and he became bound to perform them by the sanction. But he was only bound *inter partes*.
>
> ... As I have said the sanctioning of a compromise does not turn the compromise into an order of Court. To contravene its terms is not contempt of Court. The compromise is a contract which derives its binding force from the fact that it was approved by the Court in terms of a statute."

Franklin J thereafter continued:

> "I have come to the conclusion that, having regard to the approach of our Courts to a sanctioned compromise, i.e. that it is a contract binding on all concerned, it is not only permissible but essential to have regard to all its terms … Whilst I agree with Mr King that normally the binding effect of a compromise, if sanctioned, cannot be questioned, his argument overlooks the fact that para. 5.2 of the offer before me specifically states that:
>
> 'If the arrangement …. is not sanctioned or if accepted and sanctioned and any of the conditions precedent hereto shall fail, lapses …'."

[597] 1975 (3) SA 963 (W).
[598] 1971 (1) SA 256 (W) at 258A-C.

Henochsberg on the Companies Act[599] express the position as follows:

> "The registered order (i.e. sanctioning a compromise) does not, however, have the effect of converting the compromise into an order of court; it merely gives a compromise contractual force as between all those bound by it (*Ex Parte* De Wet NO: In re: Mackville Motors (Pty) Ltd 1971 (1) SA 256 (W) at 258; Cohen NO v Nel 1975 (3) SA 963 (W) at 968-969; Parker v WGB Kinsey & Co (Pvt) Ltd 1988 (1) SA 42 (ZSC) at 47."

These authorities are to the effect that an order sanctioning a scheme of arrangement or an offer of compromise does not constitute the debt a "judgment debt" nor an order of court. The court's order sanctioning the scheme is simply required to give legal effect to the scheme of arrangement which remains contractual in nature.

It is thus so advisable to apply to court for an adopted proposal to be made an order of court such that any proposer would be foolish and ill-advised not to. The application is not an *ex parte* application. It must be served on all creditors including those who voted in favour of the proposal.

It appears that notice should be given to all parties including those who voted in favour, in order to cater for the situation where those who voted in favour may establish in the application that there was certain relevant information which was not drawn to their attention, or of which they were not aware, or which would have affected their decision. They would be entitled to oppose the application to court on these grounds and to motivate to the courts that it should not make an order approving the proposal.

Certainly those who did not vote or those who opposed the vote should be given an opportunity to oppose the application and a failure to serve on them the application or give them notice of it so that they can put in an affidavit opposing it so that the judge hearing the application is then in a position to exercise his discretion and to determine whether it is just and equitable to make the proposal an order of court.

Where the compromise or arrangement has been made by a liquidator on behalf of a company being wound-up, then the report of the Master of the High Court required in terms of the laws contemplated in item 9 of Schedule 5 of the Companies Act 2008 is to be attached to the application.

The question might arise whether all creditors referred to above are to be made party to the application, or whether they should merely be served with the application. Case law[600] suggests that only notice of the application should be given to creditors. To the extent that they wish to oppose the application they would have to apply to the court for leave to intervene and thereafter once leave is granted file their answering or opposing affidavits.

[599] Henochsberg 628.
[600] *SARS v Logikal Consulting (Pty) Ltd and Others* 2019 (6) SA472 GP.

15.10 Just and equitable

Section 155(7)(b) of the Companies Act 2008 provides that a court may sanction a compromise as set out in an adopted proposal if it considers it just and equitable to do so. This term is not further described or defined in the Companies Act 2008. Section 155(7)(b)(i) does however assist in that it provides that in the deciding whether it is just and equitable to do so, a court must have regard to the number of creditors of any affected class of creditors, who were present or represented at the meeting and who voted in favour of the proposal. The only reported decision in South Africa dealing with this section is *SARS v Logikal Consulting (Pty) Ltd and Others*[601] (the *SARS* judgment).

In regard to section 155:

- it is important to note the legislature has singled out for the courts attention when determining whether it is just and equitable to sanction the proposal that the courts must have regard to the number of creditors of the affected class(es) who were present or represented at the meeting and who voted in favour of the proposal;

- the High Court when determining whether or not to sanction an adopted proposal exercises a discretion;

- the court's discretion is wide and unfettered although *prima facie* it appears that the legislature requires them, at the very least, to pay specific and particular attention to the number of creditors who were represented and who voted at the scheme meeting and the vote itself; and

- the number of creditors who voted is thus important. This is so as the vote reflects the affected creditors' will and express intentions with regards to the proposal. It is after all their claims which are being compromised and thus their views are of the utmost importance to the courts. Obviously the more creditors who vote the more reflective is their views. The strength and / or success of the vote will guide the court as to whether or not the proposal is fair and reasonable warranting the court's sanctioning. A number of reported decisions on section 311 of the Companies Act 1973 are of assistance. These authorities are to the effect that:

  - Per *Dundas & Miller (Pty) Ltd v Borton NO*[602] where the court held, *inter alia*, as follows:

    "Moreover the size of the majority vote can be a clear indication that the scheme is not unreasonable."

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[601] *Ibid*.
[602] 1971 (1) 106 E at 108D.

- Per *Ex Parte Utility Shoe Manufacturing Company: In re ABC Store (Pty) Ltd*[603] where the court also held as follows:

  "I am of the opinion that once the statutory majority of creditors have accepted a compromise at a properly convened and properly held meeting of creditors summoned for the purpose of considering an offer of compromise, the Court ought not to withhold its sanction at the instance of a minority creditor, unless the majority acted mala fide and their acceptance is in the nature of a fraud on the minority."

- Per *Du Preez v Garber in re Boerebank Beperk*[604]where the court held, *inter* alia, as follows:

  "The fact, however, that a scheme deprives creditors of rights, or is prejudicial in some way to their interests is not by itself an obstacle to its confirmation by the court, if the statutory majority of such creditors approve it. Very few schemes conceive when a company is in liquidation because of being unable to pay its debts, can never be perfectly satisfactory to all creditors ...

  How then should the court exercise its discretion in this case? The test usually adopted is that of Maughan, J …, namely whether the proposal is such that an intelligent and honest man, a member of the class concerned and acting in respect of his interests, might reasonably approve;

  But in regard to that and other tests which have been propounded in the decided cases I am inclined to agree with what BROOME J, said …, namely that they are:

  No more than considerations which Courts have found proper to be taken into account in particular cases, rather than as laying down the correct method of approaching all cases";

  In other words, they are guides to, but not fetters on, the Court's discretion. Compare too … where Solomon, J. said that Section 103(2) appeared to him to give a complete discretion to the Court in regard to sanction or otherwise."

  What is clear is that the Courts function is not merely to register the decision of the statutory majority of creditors on the arrangement …; it has to be satisfied that the arrangement is one that on its merits it ought to be rendered binding on all the creditors concerned that is, on those who did and those who did not attend the meeting, and the onus is on the applicant who seeks confirmation to so satisfy the court."

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603 1948 (4) SA 1 W at 5.

604 1963(1) SA 806 W at 823A to 823G.

It has also been held that generally, a court will not impose its own views over the views of the scheme creditors. The result of the scheme creditors' vote is very persuasive and constitutes on its own a sound challenge to the opposing creditors' views.

As stated previously there is at this time no reported case which defines with any precision other criteria and factors that the courts will take into account when exercising its discretion and in deciding whether it is just and equitable to sanction the compromise as set out in the proposal. In the *SARS* judgment (referred to above) after having set out the background to section 311 of the Companies Act 1973 and section 155 of the Companies Act 2008, Van Der Linde J held as follows:

> "[21] In conclusion then on this part of the background [a reference to Section 311] I believe it can safely be said, on the basis not only of ex parte Cape & Transvaal Printing and Publishing Co. Ltd but also the reported judgments in which objections were raised and heard on the sanctioning date, that under Section 311 the practice was firmly established that all Affected Parties were required to have knowledge of the report back, 'the sanctioning' date. This applied even to those creditors who voted in favour of the compromise and thus a fortiori to those who did not vote."

The following additional factors should also influence a court when exercising its discretion on whether or not to sanction the proposal, namely:

- the content and effect of the proposal;
- the nature of such opposition to the sanction application and the grounds of opposition;
- the quantum of each opposing creditors' claim when compared to the total of all claims compromised in terms of the proposal;
- the consequences to creditors and employees of the company if the proposal is not sanctioned; and
- whether the proposal makes imminent sound financial and commercial sense.

Certainly the courts in the exercise of its discretion may correct any mistakes in the proposal but cannot, as indicated above, alter the substance of the scheme or impose upon creditors any term or condition to which they did not agree.

If a court is not satisfied that procedural fairness[605] was properly applied it could surely in the exercise of its discretion refuse to sanction the adopted proposal.

[605] *Ibid*.

The courts have refused to sanction compromises where it had been shown that creditors voted in classes in which they should not have voted, or the classes should have been created for certain of the creditors given their rights and interests but were not and the creditors were thus not afforded an opportunity to vote in these classes.[606]

15.11 The new legislative arrangement

Under the Companies Act 2008, schemes of arrangement between companies and their members, and compromises between companies and their creditors have been separated. The former is now regulated by section 114 (which forms part of Chapter 5 that is entitled "Fundamental Transactions, Takeovers and Offers"), whereas the latter is regulated in section 155 (which forms part of Chapter 6 that is entitled "Business Rescue and Compromise with Creditors").

More fundamentally, as Cassim *et al* write (sic) in "an attempt to simplify the process the role of the court under the Act has been reduced". Before there were two applications: first, for leave to convene the meeting at which the vote would be taken; and second, if the vote is carried, the application for sanction. Under the Companies Act 2008 the convening of the meetings takes place without the prior court sanction, and it is only upon subsequent application that the court has the power to "sanction the compromise as set out in the adopted proposal …".[607]

But, as the authors point out, the fundamental reason for enlisting the court's assistance under these provisions has remained the same: "A compromise is appropriate in cases where the normal mechanisms for reaching an agreement between the company and its creditors or class of creditors are not available. It is intended to provide the machinery for overcoming the practical difficulty that a company, and particularly a company with a large number of creditors, may experience in obtaining the individual consent of every creditor of the company to the settlement of their claims. It also prevents, in appropriate circumstances, a minority from impeding a beneficial scheme or from obtaining special advantages for themselves".[608]

15.12 Final and binding on company's creditors

The court order sanctioning the compromise is final and binding on all of the company's creditors or all of the members of the relevant class of creditors, as the case may be as at the date on which it is filed with the CIPC.[609]

An arrangement or a compromise contemplated in section 155 of the Companies Act 2008 does not affect the liability of any person who bound himself as surety of the company for obviously debts incurred prior to the proposal being made and sanctioned.

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[606] *Ibid*.
[607] Cassim *et al, Contemporary Company Law*, (3rd ed, Juta, 2021) Ch 18, at 1272.
[608] *Idem*, at 1271.
[609] Companies Act 2008, s 155(8)(c).

Such sureties would thus, it appears per case law under section 311 of the Companies Act 1973, only be liable for the amount of the liability in terms of the compromise or arrangement and not the amount of their liability that existed prior to the compromise or the arrangement.[610] The same principle should apply to a section 155 compromises.

Self-Assessment Questions for Chapter 15

Question 1

Can a company achieve a scheme of arrangement between its shareholders utilising the provisions of section 155 of the Companies Act 2008?

Question 2

Are the provisions of section 155 available to an affected party in business rescue, or to a business rescue practitioner?

Question 3

If a company has a number of different creditors with different rankings, can the company's directors or liquidator compromise only one such category of creditors to the exclusion of all others (that is, can preferent creditors be compromised under section 155 without compromising the rights and claims of the secured and concurrent creditors)?

Question 4

How does one determine the various classes of creditors for the purposes of voting on a section 155 offer?

Question 5

Would an offeror or a receiver be acting in contempt of court if, after an offer of compromise has been sanctioned by court order, they are unable to pay creditors in accordance with the terms and conditions of the sanctioned compromise?

Question 6

If a creditor voted in favour of a scheme of arrangement, is it thereafter necessary to serve upon such creditor the application to the court to sanction the compromise?

[610] *Friedman v Bond Clothing Manufacturers (Pty) Ltd* 1965(1) SA 673 (T) 680; *Dick v Olver* 1979 (4) SA 880 (C) 882.

Question 7

What role (if any) does the Master of the High Court play in a section 155 compromise?

Question 8

If all creditors vote in favour of a compromise, can a court in a subsequent application refuse to sanction it? If it can, kindly motivate your answer.

For feedback on this self-assessment exercise, see the document "Comment and Feedback on Self-Assessment Questions", which is made available to you as a separate document.

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