



SUMMATIVE (FORMAL) ASSESSMENT: MODULE 7D

SOUTH AFRICA

Commented [SL1]: TOTAL = 45/50

90%

This is the **summative (formal) assessment** for **Module 7D** of this course and must be submitted by all candidates who **selected this module as one of their elective modules**.

The mark awarded for this assessment will determine your final mark for Module 7D. In order to pass this module, you need to obtain a mark of 50% or more for this assessment.

INSTRUCTIONS FOR COMPLETION AND SUBMISSION OF ASSESSMENT

Please read the following instructions very carefully before submitting / uploading your assessment on the Foundation Certificate web pages.

1. You must use this document for the answering of the assessment for this module. The answers to each question must be completed using this document with the answers populated under each question.
2. All assessments must be submitted electronically in **Microsoft Word format**, using a standard A4 size page and an 11-point Arial font. This document has been set up with these parameters – **please do not change the document settings in any way. DO NOT** submit your assessment in PDF format as it will be returned to you unmarked.
3. No limit has been set for the length of your answers to the questions. However, please be guided by the mark allocation for each question. More often than not, one fact / statement will earn one mark (unless it is obvious from the question that this is not the case).
4. You must save this document using the following format: **[studentnumber.assessment7D]**. An example would be something along the following lines: 202021IFU-314.assessment7D. **Please also include the filename as a footer to each page of the assessment** (this has been pre-populated for you, merely replace the words “studentnumber” with the student number allocated to you). Do not include your name or any other identifying words in your file name. **Assessments that do not comply with this instruction will be returned to candidates unmarked.**
5. Before you will be allowed to upload / submit your assessment via the portal on the Foundation Certificate web pages, you will be required to confirm / certify that you are the person who completed the assessment and that the work submitted is your own, original work. Please see the part of the Course Handbook that deals with plagiarism and dishonesty in the submission of assessments. **Please note that copying and pasting from the Guidance Text into your answer is prohibited and constitutes plagiarism. You must write the answers to the questions in your own words.**
6. The final submission date for this assessment is **31 July 2021**. The assessment submission portal will close at **23:00 (11 pm) GMT on 31 July 2021**. No submissions can be made after the portal has closed and no further uploading of documents will be allowed, no matter the circumstances.
7. Prior to being populated with your answers, this assessment consists of **8 pages**.

ANSWER ALL THE QUESTIONS

QUESTION 1 (multiple-choice questions) [10 marks in total]

Questions 1.1. – 1.10. are multiple-choice questions designed to assess your ability to think critically about the subject. Please read each question carefully before reading the answer options. Be aware that some questions may seem to have more than one right answer, but you are to look for the one that makes the most sense and is the most correct. When you have a clear idea of the question, find your answer and **mark your selection on the answer sheet by highlighting the relevant paragraph in yellow**. Select only **ONE** answer. Candidates who select more than one answer will receive no mark for that specific question.

Commented [SL2]: SUB-TOTAL = 8

Question 1.1

Commented [SL3]: 1

Choose the **correct statement**:

- (a) A creditor in whose favour a mortgage bond over immovable property has been registered, may not dispose of the immovable property upon the sequestration of the debtor's estate.
- (b) A creditor in whose favour a general notarial bond over immovable property has been registered, may not dispose of the immovable property upon the sequestration of the debtor's estate.
- (c) A creditor in whose favour a special notarial bond over immovable property has been registered, may not dispose of the immovable property upon the sequestration of the debtor's estate.
- (d) A creditor in whose favour a mortgage bond over movable property has been registered, may not dispose of the immovable property upon the sequestration of the debtor's estate.

Question 1.2

Commented [SL4]: 1

Choose the **correct statement** in relation to impeachable dispositions and the powers of the business rescue practitioner to have dispositions set aside –

- (a) A disposition not for value made by the company prior to being placed under business rescue may be set aside in terms of the provisions of section 26 of the Insolvency Act 24 of 1936.
- (b) A disposition preferring one creditor above another made by the company prior to being placed under business rescue may be set aside in terms of the provisions of section 29 of the Insolvency Act 24 of 1936.
- (c) A disposition with the intention to prefer one creditor above another made by the company prior to being placed under business rescue may be set aside in terms of section 30 of the Insolvency Act 24 of 1936.
- (d) None of the above are correct.

Question 1.3

Commented [SL5]: 1

A liquidator of a company may exercise the following power **without** the consent of the Master of the High Court:

- (a) Terminating a lease agreement prior to the general meeting.
- (b) Instituting legal proceedings.
- (c) Selling any movable property of the company prior to the general meeting.
- (d) Selling any immovable property of the company prior to the general meeting.

Question 1.4

Commented [SL6]: 1

Read the following statements in (i) to (iv) below.

- (i) In terms of the Insolvency Act 24 of 1936, a debtor whose estate has been sequestrated may enter into any type of agreement, as long as prior consent of the trustee is obtained.
- (ii) In terms of the Insolvency Act 24 of 1936, a debtor whose estate has been sequestrated may enter into an agreement to alienate property, as long as prior consent of the trustee is obtained.
- (iii) In terms of the Insolvency Act 24 of 1936, a debtor whose estate has been sequestrated requires the assistance of the trustee in order to institute legal proceedings relating to an injury sustained in a motor vehicle accident.
- (iv) In terms of the Insolvency Act 24 of 1936, a debtor whose estate has been sequestrated may be employed as an electrician without the trustee's permission in this regard.

Of the above statements, indicate which statement(s) is / are **correct**:

- (a) Option (i) is correct.
- (b) Options (ii) and (iii) are correct.
- (c) Option (iii) is correct.
- (d) Options (ii) and (iv) are correct.

Question 1.5

Commented [SL7]: 0

In January 2020 Company A was placed in liquidation. The liquidator of Company A became aware of the fact that Company A disposed of property worth ZAR 10,000 to Company B for an amount of ZAR 5,000 during September 2019. Directly after the disposition, Company A's liabilities exceeded its assets by ZAR 6,000. **If the disposition is set aside –**

- (a) Company B will be required to return ZAR 10,000 to the liquidator of Company A.
- (b) Company B will be required to return ZAR 6,000 to the liquidator of Company A.
- (c) Company B will be required to return ZAR 5,000 to the liquidator of Company A.
- (d) Company B will be required to return ZAR 4,000 to the liquidator of Company A.

Question 1.6

With reference to question 1.5 above, what does Company B have to prove in order to ensure that the disposition **is not set aside**?

- (a) That a disposition was made by the Company A within six months prior to liquidation.
- (b) That the effect of the disposition is that one creditor was preferred above another.
- (c) That the disposition was made by the Company A with the intention of preferring one creditor above another.
- (d) That immediately after the disposition the liabilities of Company A exceeded its assets.**

Commented [SL8]: 1

Question 1.7

Indicate **the correct order of preference** of the following costs / claims in the free residue account:

- (a) Costs of sequestration; funeral expenses; income tax; claims secured by a general bond; and, lastly, employee claims.
- (b) Funeral expenses; costs of sequestration; employee's claims; income tax; and, lastly, claims secured by a general bond.**
- (c) Funeral expenses; employee's claims; costs of sequestration; income tax; and, lastly, claims secured by a general bond.
- (d) Employee claims; funeral expenses; costs of sequestration; income tax; and, lastly, claims secured by a general bond.

Commented [SL9]: 1

Question 1.8

Company A wishes to obtain funding in order to expand its cinema and other related businesses. As part of the security package negotiated with the lender, the lender requires Company A to provide its IMAX 3D cinema screens to it as security. Company A makes use of these screens at the cine-complexes at various shopping malls. This form of security is known as a –

- (a) Pledge.
- (b) Hypothec.
- (c) Cession in security of a debt (*in securitatem debiti*).
- (d) Special notarial bond.**

Commented [SL10]: 1

Question 1.9

Read the following statements:

- (i) The Companies and Intellectual Properties Commission plays an active role throughout the business rescue process.

Commented [SL11]: 0

- (ii) Business rescue requires a reasonable possibility of restoring the company in question to a solvent basis.
- (iii) Immediate inability to pay debts is a prerequisite for placing a company under business rescue.
- (iv) A company may be placed under voluntary business rescue by the shareholders of the company in terms of a resolution if the company is in financial distress.

Of the above, which of the following is **correct in relation to business rescue**:

- (a) Options (i) and (ii) are correct.
- (b) Options (ii) and (iii) are correct.
- (c) Options (i) and (iii) are correct.
- (d) None of the above options are correct.

Question 1.10

Which of the following is **incorrect in relation to the recognition of foreign judgments**:

- (a) All foreign judgments are enforced in terms of the Enforcement of Foreign Civil Judgments Act 32 of 1988.
- (b) All foreign judgments are enforced in terms of the common law.
- (c) Foreign judgments are directly enforceable in South Africa.
- (d) All of the above.

QUESTION 2 (direct questions) [10 marks in total]

Question 2.1 [maximum 4 marks]

In accordance with the South African common law dealing with cross-border insolvency, how are the **assets of an insolvent governed**? (Briefly refer to the position applicable to both movable and immovable property.)

[Cross-border insolvency law in South Africa¹ is governed by common law principles². Further to this, the type of assets and the classification of persons involved in a cross-border insolvency are important factors when dealing with the assets of an insolvent in South Africa.

According to the common law principles in South Africa, movable property is governed by the law of the natural person's domicile (lex domicilii)³. Once foreign insolvency proceedings have commenced, a debtor is automatically divested of his movable assets and the same principle applies to the debtor's assets located in South Africa. Immovable property on the other hand,

¹ The SA legislation dealing with cross-border insolvency is the Cross-Border Insolvency Act 42 of 2000.

² The principles are a hybrid of territorialism and universalism concepts.

³ Merriam-Webster Dictionary: "the law of the domicile by which the rights of persons are sometimes governed (as where a person dies leaving personal property)".

Commented [SL12]: 1

Commented [SL13]: SUB-TOTAL = 10

Commented [SL14]: 4

is governed by the law of the place where the immovable property is situated (lex situs)⁴. In this case, once foreign proceedings have commenced, immovable assets (located in South Africa) of a debtor are not automatically divested.

A foreign representative⁵ dealing with assets (movable or immovable) located in South Africa is required to apply for recognition to the High Court of South Africa before dealing with those assets.]

Question 2.2 [maximum 6 marks]

Commented [SL15]: 6

What common law requirements need to be met in order for the cause of action established by a foreign judgment to be enforced?

[Under South African common law, foreign judgements may be enforced in the Magistrates' Court or the High Court, depending on the monetary value⁶ of the foreign judgement.

In South Africa, the enforcement of foreign judgements is governed by the Enforcement of Foreign Civil Judgements Act 32 of 1998 ("EFCJ") and the common law. At this stage, the EFCJ is only applicable to Namibia.

The enforcement of a foreign judgement in South Africa is not automatic and there are certain common law requirements that must be met before a foreign judgement is recognised. Pursuant to section 5 of the EFCJ the requirements include the following:

1. Taking into account the principles of South African private international law, the foreign court must have jurisdiction to entertain the initial insolvency proceedings. This may include proceedings involving assets such as property located in the jurisdiction of the foreign court. In like manner the South African court must have jurisdiction to hear the enforcement application- i.e. the judgement should not relate to property situated outside of South Africa (as the South African Court would not have jurisdiction over the immovable property).
2. The judgement must not constitute fraud.
3. The judgement must have been final and conclusive.
4. The judgement must not involve the enforcement of foreign penal laws or revenue laws.
5. The enforcement of the judgement must not be contrary to public policy⁷ in South Africa.
6. The enforcement of the judgement must not be contrary to the provisions set out in the Protection of Business Act 99 of 1978.]

⁴ Ibid, lex situs: the law of the place where a property is situated.

⁵ Defined in the United Nations Committee on International Trade Law, Model Law on Cross-Border Insolvency: a person or a body, authorized in a foreign proceeding to administer the reorganization or liquidation of the debtor's assets or affairs or to act as representative of the foreign proceeding. Hereinafter referred to as the "MLCBI".

⁶ Holloway Patrick, October Andre and Wentzel Webber- Enforcement of judgements in South Africa: overview, Thomson Reuters Practical Law, <https://content.next.westlaw.com/> - the financial limit on actions in the Magistrates' Court is capped at ZAR400,000 and foreign judgements in excess of ZAR400,000 is enforced in the High Court.

⁷ Article 6 of the MLCBI contains a "public policy exception" which is a safeguard to the sovereignty of an enacting State and is grounded in the domestic law of the State, thus may differ in various jurisdictions.

QUESTION 3 (essay-type question) [15 marks]

Commented [SL16]: SUB-TOTAL = 15

Question 3.1 [maximum 5 marks]

Commented [SL17]: 5

Mr L and Big Deal Limited entered into a lease agreement in terms whereof Big Deal Limited rents an office from Mr L who is the owner of the office block where the office is situated. After Big Deal Limited has rented from Mr L for over a year, it experiences financial difficulties and is placed in liquidation. Mr L is of the opinion that Big Deal Limited had been a very good tenant that paid its rent timeously up until a few months prior to the liquidation, and he is concerned about the effect of the liquidation of Big Deal Limited on their lease agreement. Advise Mr L in this regard.

[No automatic termination:

At the time of being placed into liquidation, the terms of the lease agreement between Mr. L (the "lessor") and Big Deal Limited ("lessee") was in still in effect and does not immediately terminate, simply because the lessee becomes insolvent. Further, the lease agreement is not automatically terminated in an instance where the estate of the lessee is sequestrated. It is therefore important to examine the terms of the lease agreement and identify any clauses that would govern the scenario of a liquidation.

Liquidator's authority:

Even though the lease agreement between the parties is not automatically terminated, the liquidator does have the authority to immediately cancel the lease by means of a written notice⁸. Furthermore, the liquidator has up to three months to decide whether to cancel or continue with the lease arrangement but must do so by issuing a written notice of his/her intention to the lessor. If the liquidator fails to notify the lessor before the end of the aforementioned period, the lease will be considered automatically cancelled.

Payment of rent:

Until the liquidator makes a decision, the lease agreement remains in force and any rental amounts which became due after the liquidation to the date of the cancellation of the lease agreement will be treated as preferent claims⁹ and must be settled by the liquidator. Any other claims, such as rental amounts owed prior to the commencement of the liquidation will be treated as a concurrent claim.

Lessor's right to cancel:

However, the onus is not entirely in the hands of the liquidator. The lessee was already in breach of the lease agreement prior to being placed into liquidation and therefore, the lessor has a common law contractual right to cancel the lease after the liquidation of the company and also obtain a "hypothec over immovable property in lieu of rental arrears"¹⁰ due prior to the liquidation.]

Question 3.2 [maximum 10 marks]

Commented [SL18]: 10

Ms A is a schoolteacher by profession. She earns a gross income of ZAR 20,000 per month. In 2018 she borrowed ZAR 1,200,000 from ABC Bank (Pty) Ltd (the bank) in order to purchase

⁸ Companies Act 1973 section 396(2) subsection (1)(d).

⁹ Lawrenson, Sanrie, INSOL Guidance Text, Module Seven, Section 6.2.13 (Statutory preferent creditors) – "Preferent creditors are creditors whose claims are statutorily preferent in terms of the Insolvency Act.

¹⁰ Insolvency Act section 37(1) and (5), and guidance text section 6.2.9, p. 21

an apartment in Cape Town. In order to secure the repayment of the debt, the bank registered a mortgage bond over the apartment. In 2019 the local municipality failed to service the sewerage facilities in the suburb where the apartment is located, which resulted in severe damage to the entire plumbing and drainage system of the apartment complex. Subsequently the apartment decreased in value to ZAR 750,000.

During 2019 Ms A bought a Toyota Yaris motor vehicle from Harry's Cars and Motorbikes for a purchase price of ZAR 120,000. In terms of the instalment sale agreement entered into between the parties, Ms A's monthly repayment for the vehicle is ZAR 5,000 per month. While Ms A's motor vehicle was parked in the parking lot of the school where she teaches, a hail storm hit the area and her vehicle was severely damaged. As a result, the value of her motor vehicle decreased to ZAR 60,000.

At present, Ms A is experiencing difficulties in repaying her debts. She has to make the following monthly payments:

Municipal rates and taxes	ZAR 1,500
Cell phone	ZAR 1,000
Insurance	ZAR 750
Groceries	ZAR 4,000
Harry's Cars and Motorbikes	ZAR 5,000
Home loan	ZAR 8,500
TOTAL	ZAR 20,750

Ms A still owes the bank ZAR 800,000 in terms of her home loan agreement and she still owes ZAR 70,000 to Harry's Cars and Motorbikes in respect of the Toyota Yaris. At present Ms A owes her creditors approximately ZAR 900,000 in total. Ms A cannot afford to pay her creditors the amounts that she owes them. Mr B, the manager of the bank, has also contacted Ms A on a few occasions to enquire as to the outstanding payments in relation to her home loan.

Identify Ms A's financial status and explain to her what measures she can consider taking in order to manage or resolve her financial problems, as well as what legal requirements will be required of her to succeed in this regard. Further, also explain what measures are available to the bank in an attempt to secure payment of the amount due to them by Ms A, given her financial circumstances.

[Ms A's financial status:

Ms A is cashflow insolvent because she is unable to pay her debts as they fall due. Ms A has income of ZAR 20,000 per month and her outgoing is ZAR 20,750, therefore she has a deficit of ZAR 750.00- Ms A is unable to meet all of her monthly payments. Further, Ms A is balance sheet insolvent because her debts exceed her assets.

What measures can Ms A consider taking in order to manage or resolve her financial problems:

Before delving into the various statutory options available, Ms A should consider performing her own personal review of her current financial circumstance to determine whether she can either decrease her cash outflow or increase her income. In other words, Ms A will need to determine whether some of her monthly commitments are essential or non-essential. For example, the question of whether Ms A's monthly cell phone charge of ZAR 1,000 could be reduced to a fraction of the monthly cost should be considered. Furthermore, Ms A has leverage to significantly reduce her monthly grocery cost by considering a practical and

manageable monthly grocery budget. Essentially, if Ms A is able to reduce her outflow by a quarter, she may be able to comfortably meet her monthly debts.

Ms A is eligible to apply for a debt review as provided for in terms of the National Credit Act 34 of 2005 ("NCA"). Ms A's gross income is ZAR 20,000 per month and her monthly obligations exceed this amount (her debt ratio is more than 100%). Section 79 of the NCA states that "a consumer is over-indebted if the...the consumer is or will be unable to satisfy in a timely manner all the obligations under all the credit agreements to which the consumer is a party". The debt review as provided for under the NCA offers options of a debt rearrangement¹¹ or debt restructuring¹² and although a debt review/relief will not discharge Ms. A of her debts, it will offer some relief from the pressure of her state of insolvency.

Personal bankruptcy (sequestration) is provided for in the Insolvency Act and Ms A can approach the court for a voluntary sequestration of her estate for the benefit of her creditors. Should Ms. A decide to pursue this route there are several legal requirements of the court which must be met¹³:

- (a) Proof that Ms A, as the "debtor" is insolvent;
- (b) Proof that Ms. A has sufficient free residue to defray the costs of sequestration;
- (c) Proof that the sequestration of her estate will be to the advantage of creditors; and
- (d) Proof that the formalities in Section 4 of the Insolvency Act¹⁴ have been complied with.

Ultimately, it is the responsibility of Ms A to satisfy the aforementioned requirements. Furthermore, should a sequestration order be issued by the Court, an automatic stay (*consensus creditorum*)¹⁵ of civil proceedings against the estate of Ms A, by the bank or Harry's will be stayed.

Although section 3 of the Insolvency Act states that a debtor 'may' petition the court for acceptance of surrender of the debtor's estate and therefore there is no obligation on the part of the debtor to enter a voluntary bankruptcy proceeding. Further to this, voluntary sequestration is only at the discretion of the court and there is no monetary threshold for entering sequestration court proceedings. Since Ms A's estate consists only of liabilities (does not own sufficient property to meet the costs of the sequestration) this may not be a sensible option and therefore cancels the notion of a common law compromise. Sequestration of Ms A's estate is not the only option for her debt relief as there are 'alternatives to formal sequestration'.

Explain what measures are available to the bank in an attempt to secure payment of the amount due to them by Ms A, given her financial circumstances.

Section 9 of the Insolvency Act states that creditors "may" petition the court for sequestration of a debtor's estate. The bank is a secured creditor and may apply to the court for compulsory sequestration of Ms A's estate (for disposition purposes) to recover the debt owed to them.

¹¹ National Credit Act 34 of 2005, Section 86(7)(b) - "the consumer is not over-indebted, but is nevertheless experiencing, or likely to experience, difficulty satisfying all the consumer's obligations under credit agreements in a timely manner, the debt counsellor may recommend that the consumer and the respective credit providers voluntarily consider and agree on a plan of debt re-arrangement".

¹² Ibid, Section 86(7)(c)(ii) - "...the debt counsellor may issue a proposal...that one or more of the consumer's obligations be re-arranged..."

¹³ Insolvency Act Section 3 – 7

¹⁴ Insolvency Act, Section 4: Notice of surrender and lodging at Master's Office of Statement of debtor's affairs.

¹⁵ Guidance Text 6.2.3, p.14

However, there are several legal conditions which must be met by the bank should an application for the sequestration of the Ms A's estate be granted by the court. These are:

- a. The bank must have a liquidated claim against Ms A for not less than ZAR100.
- b. Proof that Ms. A has committed an act of insolvency or is insolvent.
- c. Proof that the sequestration of Ms A's estate will be advantageous to the bank recovering the debt due to them.
- d. Confirmation that the formalities (such as a petition to court) provided for in section 9 of the Insolvency Act have been complied with.

Ms A is insolvent, and she is currently not able to provide sufficient disposable property which would satisfy the amount owed to the bank of ZAR 800,000. Added to this, the security (the house) has been devalued to ZAR 750,000 because of a severe plumbing issue.

If the bank petitions the court for compulsory sequestration of Ms A's estate, they must be able to prove that sequestration will be to the advantage of the bank¹⁶. This may influence the court in its decision to accept an application for the sequestration of Ms. A's estate. The bank must be able to prove that sequestration of Ms A's estate will not 'yield a negligible dividend'.

Whether the bank has been accommodating to Ms. A's circumstance by offering alternatives of time for repayment, a monthly plan or restructuring of the loan agreement was not mentioned in the case study. However, the fact that the bank has already 'pressed' Ms. A for payment is a factor that may influence the court toward refusing the bank's application for the sequestration of Ms. A's estate. The court will look more favourably on applications by the bank where they can evidence that they offered alternative solutions to the debtor.

Ultimately, the court may also consider that Ms. A's financial circumstance would be more appropriately dealt with in a debt review as provided under the NCA.]

QUESTION 4 (fact-based application-type question) [15 marks]

The directors of i-Orchard (Pty) Ltd (the company) foresee the reasonable likelihood that the company will, within the next six (6) months, be unable to pay its debts as they become due in the ordinary course of business, and will most likely reach a situation where its liabilities exceed its assets. The directors therefore elect to initiate business rescue proceedings and adopt the relevant board resolution, which is subsequently filed with the Companies and Intellectual Property Commission (CIPC). Mr X is appointed as the company's business rescue practitioner. Various parties are affected by the company's decision. The following parties approach you as a collective seeking legal advice:

- (i) Mr A, a successful businessman, lent the company ZAR 700,000 which the company failed to repay. He initiated proceedings against the company in the High Court to reclaim his money and at the time that the company was placed under business rescue proceedings, the court proceedings were almost finalised. Mr A is unsure as to the effect of business rescue on the money owed to him.
- (ii) Ms B has worked for the company for the last five (5) years and she is concerned about the effect that business rescue will have on her employment contract.
- (iii) Mr M leases office space to the company and he is concerned about the effect of the business rescue proceedings on the lease agreement with the company.

¹⁶ Ibid, Section (6)(1).

Commented [SL19]: 12

Discussion could have included approval of plan, purchasing of voting rights, cram-down. Also see comments below in text

(iv) Ms T is a shareholder of the company and is unsure whether she will lose her shareholding now that the company has been placed under business rescue.

(v) Mr H is a director of the company and is unsure as to his position and role now that business rescue proceedings have commenced.

Write a single legal memorandum to all the above-mentioned persons wherein you explain their legal rights, and / or the potential outcome of their respective situations, taking into consideration the business rescue process. The memorandum should further make mention of any potential remedies at their disposal; any practical implications of their respective situations; and also include any considerations in respect of the business rescue plan that the practitioner needs to take cognisance of.

INSOLVENCY AND BANKRUPTCY
i-Orchard (Pty) Ltd

LEGAL MEMORANDUM

STATEMENT OF FACTS

1. i-Orchard (Pty) Ltd (the company) is in financial distress. Factors indicating this include:
 - a. The company appears to be commercially insolvent and reasonably unlikely to be able to settle its debts, as they fall due, within the ensuing six-month period.
 - b. The company has failed to repay the ZAR 700,000 owed to Mr. A.
2. There are two ways in which a business rescue can be initiated:
 - a. By way of a resolution of the company's board of directors; or
 - b. By application to the High Court by an affected person. (Mr. A is an affected person because he is a creditor of the company) Mr. A has already progressed legal proceedings in the High Court against the company, however, it is not clearly stated whether the legal proceedings are in favor of a business rescue or winding up of the company and the legal proceedings have not been finalized.
3. Acting under the provisions as set out in Section 129(1) of the New Companies Act, the board of directors had adopted a resolution to initiate business rescue proceedings. The fact that the directors have elected a business rescue proceeding over a winding up of the company indicates that there is a likelihood that the company has some viability and an appropriate business rescue plan could yield a positive return to the company's creditors. Despite the powers of the directors and their view with respect to the viability of the company, section 129 (2)(a) of the New Companies Act indicates that the directors may not adopt a resolution to initiate business rescue proceedings if there has been a petition before the court to commence liquidation or winding up proceedings. As stated in the preceding point, Mr. A has in fact initiated legal proceedings against the company.
4. The company has at least one employee.
5. The company has a contractual lease agreement obligation for office space.

ISSUES RAISED

- (i) **Mr A, a successful businessman, lent the company ZAR 700,000 which the company failed to repay. He initiated proceedings against the company in the High Court to reclaim his money and at the time that the company was placed under business rescue proceedings, the court proceedings were almost finalised. Mr A is unsure as to the effect of business rescue on the money owed to him.**

- a. **Legal right** – Each creditor is entitled to formally participate in legal proceedings relating to the business rescue proceedings, to form a creditors' committee, to be consulted by the business rescue practitioner during the development of a business rescue plan, and to vote on the business rescue plan. As a creditor, Mr. A is also entitled to participate in the development of a business rescue plan on a more informal level by making proposals for a business rescue plan to the practitioner.
- b. **The potential outcome of this situation** – Business rescue proceedings result in a moratorium on legal proceedings against the company. Further, once the business rescue plan is approved or adopted, all affected persons are bound whether they voted in favour of the adoption of the plan or whether their claims against the company was admitted. A 'cramdown' of creditors may occur- creditors are forced to accept a business rescue plan, even against their wishes – thus enabling the business rescue to proceed despite any objections.
- c. **Potential remedy at disposal** – The bank is an affected person and may approach the court in certain circumstances to request an order setting aside the business rescue resolution adopted by the board, setting aside the appointment of the appointment of the business rescue practitioner or requiring the appointed business rescue practitioner to provide security¹⁷. However, according to section 129(2) of the Companies Act, the board may not adopt a resolution to commence business rescue proceedings if the court has been petitioned for the winding up of the business.
- d. **Practical implications** – If the business rescue process succeeds, Mr. A's claim would be treated as a pre-commencement claim. Although the details of the lending agreement between Mr. A and the company were not specified in the case study, the business rescue plan could include a proposal that the debt owed to Mr. A could be converted to equity in the company.

(ii) Ms B has worked for the company for the last five (5) years and she is concerned about the effect that business rescue will have on her employment contract.

- a. **Legal right** – As an employee of the company, Ms B is considered an 'affected person' and has a legal right to be notified of the business rescue arrangement and participate in legal proceedings relating to the business rescue proceedings, by forming a committee of employees' representatives. Additionally, Ms B may continue to be employed throughout the business rescue proceedings without any change to the terms and conditions of her employment (unless otherwise agreed by both parties).
- b. **The potential outcome of this situation** – In the event the business rescue plan fails, there is a possibility of retrenchment but this scenario is subject to the provisions of South African employment-related legislations and more specifically, sections 189 and 189A of the Labour relations Act 66 of 1995.
- c. **Potential remedy at disposal** – Should the company's business rescue plan fail, Ms B has the legal recourse to submit a claim for compensation (considering the terms of her employment contract) as a preferential creditor.
- d. **Practical implications** – In reality, if the business rescue plan is approved and executed, the prospects of retaining Ms B as an employee of the company would be favourable. However, in a contrary circumstance, it is likely that Ms B's employment status would be made redundant.

(iii) Mr M leases office space to the company and he is concerned about the effect of the business rescue proceedings on the lease agreement with the company.

- a. **Legal right** – Currently, there is no legal recourse for Mr. M as it relates to the lease agreement of the office space which the company occupies.

Commented [SL20]: Ranking of claims for salary

Commented [SL21]: Discussion on treatment of executory contracts; relevant case law

¹⁷ Ref. Section 130 of the Companies Act.

- b. **The potential outcome of this situation** – As it relates to any contractual obligation of the company, the business rescue practitioner may apply to the court to cancel (entirely, partially or conditionally) the terms of the agreement.
- c. **Potential remedy at disposal** – In this circumstance, the only remedy of an aggrieved contracting party is to claim damages from the company.
- d. **Practical implications** – The reality is, at current the treatment of lease agreement is not provided for the Companies Act and therefore Mr. M does not have a favourable case as a preferred creditor. There is a proposed amendment to address circumstances of a landlord's claim for rent due outside of the commencement of a business rescue procedure but until such time, Mr. M's claim cannot be treated as a preferential claim.

(iv) Ms T is a shareholder of the company and is unsure whether she will lose her shareholding now that the company has been placed under business rescue.

- a. **Legal right** – As a shareholder, Ms. T is considered an affected person and has the right to be notified of the business rescue proceedings and entitled to formally participate in legal proceedings. Furthermore, in accordance with the provisions set out in section 152(3)(c), Ms T may vote on the business rescue plan only if the adoption and implementation of the plan would alter the rights associated with the class of securities she holds.
- b. **Practical implications** – The business rescue plan forms the foundation of the business rescue proceedings to which all the affected persons are bound. The plan is binding on the company, on each creditor and on every holder of securities of the company, whether or not that person was present at the meeting, voted in favour of adoption of the plan or in the case of creditors were forced to accept the plan even against their wishes.

(v) Mr H is a director of the company and is unsure as to his position and role now that business rescue proceedings have commenced.

- a. **Legal right** – While the company is under a state of business rescue, Mr. H and every other director must continue to exercise his function as a director (and maintain obligations of duty and care as a director) but under the authority of the business rescue practitioner. Furthermore, Mr. H has a legal responsibility to cooperate with the business rescue practitioner and comply with requests for all books and records and any pertinent information relative to the company's state of affairs.
- b. **The potential outcome of this situation** – If Mr. H fails to comply with his duties and obligations, Mr. X has the legal right to apply to court for an order removing Mr. H in his capacity as director from office.
- c. **Practical implications** – Should the business rescue practitioner become aware of any acts where Mr. H or any director of the company authorized, directed or procured a wrongful act that may have led to the losses sustained by the company they are liable. A director that breaches an act outlined in Section 77¹⁸ of the Companies Act 2008, the court may impose personal liability for the debts of the company which was incurred as a result of reckless or fraudulent acts.]

*** End of Assessment ***

¹⁸ Ibid, Section 77 – Proceeds of issue of shares of no par value to be stated capital.