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202122-686.SummativeAssessment

PROGRAMME IN SOUTH AFRICAN BUSINESS RESCUE 2023

Commented [BB1]: TOTAL = 58/100

Summative Assessment (Examination)

Date: 16 - 17 November 2023

Time limit: 24 hours (from 13:00 SAST on 16 November 2023 to 13:00 SAST on 17 November 2023)

Mr M Mpolokeng Dr E Levenstein Professor A Loubser Mr T Jordaan Ms R Webster
Mr B Duma Mr D van der Merwe Mr C Rey Ms L Kahn Mr J Evans Ms J de Hutton
Ms N Mabaso Mr P van den Steen Ms A Cohen Mr D Lake Ms J Mitchell-Marais
Ms A Timme Mr S Smyth Mr C Strime

MODERATORS

Ms R Bekker Ms B Bennett Dr D Burdette Mr Z Cassim

It is imperative that all candidates read and take cognisance of the examination instructions on the next page.

All candidates are expected to comply with ALL the instructions.

INSTRUCTIONS

1. This assessment paper will be made available at **13:00 (1 pm) SAST on Thursday 16 November 2023** and must be returned / submitted by **13:00 (1 pm) SAST on Friday 17 November 2023**. Please note that assessments returned late will not be accepted.
2. All assessments must be submitted electronically in Microsoft Word format, using a standard A4 size page and an 11-point Avenir Next font (if the Avenir Next font is not available on your PC, please select the 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. 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). Candidates who include very long answers in the hope it will cover the answer the examiners are looking for, will be appropriately penalised.
4. You must save this document using the following format: **studentID.SummativeAssessment**. An example would be something along the following lines: 202223-336.SummativeAssessment. **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 “studentID” 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. The assessment can be downloaded from your student portal on the INSOL International website. The assessment must likewise be returned via your student portal as per the instructions in the Course Handbook for this course. **If for any reason candidates are unable to access their student portal, the answer script must be returned by e-mail to david.burdette@insol.org.**
6. Due to the high incidence of load shedding currently taking place across South Africa, candidates are required to determine whether any load shedding is scheduled during the examination period and, if so, to make alternative arrangements to write elsewhere if at all possible.
7. Enquiries during the time that the assessment is written must be directed to David Burdette at **david.burdette@insol.org** or by WhatsApp on +44 7545 773890 or to Brenda Bennett at **brenda.bennett@insol.org** or by WhatsApp on +27 66 228 2010. Please note that enquiries will only be responded to during UK office hours (which are 9 am to 5 pm GMT, or 11 am to 7 pm SAST).

8. While the assessments are open-book assessments, it is important to note that candidates **may not receive any assistance from any person** during the 24 hours that the assessment is written. **Answers must be written in the candidate's own words; answers that are copied and pasted from the text of the course notes (or any other source) will be treated as plagiarism and persons who make themselves guilty of this will forfeit the assessment and disciplinary charges will follow.** When submitting their answers, candidates will be asked to confirm that the work is their own, that they have worked independently and that all external sources used have been properly cited. If you submit your assessment by e-mail, a statement to this effect should be included in the e-mail.
9. Once a candidate's assessment has been uploaded to their student portal (in line with the instructions in the Course Handbook), a confirmatory e-mail will be auto-generated confirming that the assessment has been uploaded. If the confirmatory e-mail is not received within five minutes after uploading the assessment, candidates are requested to first check their junk / spam folders before e-mailing the Course Leader to inform him that the auto-generated e-mail was not received.
10. If a candidate is unable to complete this summative assessment (examination), please note that a re-sit assessment will only be given if there are exceptional circumstances that prevent the candidate from completing or submitting it (such as illness). Feedback on the final assessment will be provided within four weeks of the paper having been written - please do not enquire about your marks before four weeks have elapsed. Please note that the model answers to this assessment will NOT be provided to candidates on the course after the assessment has been written.
11. You are required to answer this paper by typing the answers directly into the spaces provided (indicated by text that states [Type your answer here]). For multiple-choice questions, please highlight your answer in yellow, as per the instructions included under the first question.
12. Since you have 24 hours within which to answer the assessment, it is suggested that you take the time to read through the assessment in its entirety before attempting to answer the questions.

ANSWER ALL THE QUESTIONS

QUESTION 1

Questions 1.1 - 1.20 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. Each of the 20 questions count 1 mark.

Commented [M2]: Total for Q1: 13 marks.

Question 1.1

Choose the **correct** statement:

Sensational Cycles Proprietary Limited rents bicycles to tourists at the Cape Town promenade. Due to a decrease in tourism and cold, wet winter months, business is slow and the loans taken out by the Sensation Cycles from its bankers are now to falling due. You have been approached for advice to determine whether the company is a candidate for business rescue. Which of the following statements correctly describes the test for financial distress?

Commented [M3]: 0 marks

- (a) It appears to be reasonably unlikely that the company will be able to pay all of its debts as they become due within the immediately ensuing six months.
- (b) It appears to be reasonably unlikely that the company will be able to pay the overwhelming majority of its debts as they become due within the immediately ensuing six months.
- (c) It appears to be reasonably likely that the company will become insolvent within the immediately ensuing six months.
- (d) Both (a) and (c) are correct.

Question 1.2

Choose the **correct** statement:

Unlike in some other jurisdictions which have debtor-in-possession regimes, in South Africa an independent person is appointed as the business rescue practitioner who supervises the company during its business rescue proceedings. Which of the following statements is correct?

Commented [M4]: 1 mark

- (a) During a company's business rescue proceedings, the business rescue practitioner consults with the board of directors and external advisors in preparing and implementing a business rescue plan to return the company to profitability.
- (b) During a company's business rescue proceedings, the business rescue practitioner has full management control of the company in substitution for its board and pre-existing management.
- (c) During a company's business rescue proceedings, the business rescue practitioner is statutorily obliged to supervise the company together with the pre-existing management and the board of directors.
- (d) During a company's business rescue proceedings, the business rescue practitioner is not empowered to remove any of the company's pre-existing management.

Question 1.3

Commented [M5]: 1 mark

Choose the **correct** statement:

An application to court for the commencement of business rescue in respect of a company that is already in liquidation:

- (a) is not allowed by the Companies Act 2008.
- (b) may only be made before a final liquidation order has been issued.
- (c) may only be made before a provisional liquidation order has been issued.
- (d) may be made before the company is dissolved.

Question 1.4

Commented [M6]: 0 marks

Choose the **correct** statement:

The general moratorium is one of the critical components of business rescue because:

- (a) it affords the company in business rescue sufficient time to avoid paying its creditors for the benefit of its shareholders who own the company in business rescue as provided for in section 133 of the Companies Act of 2008.
- (b) it gives the company in business rescue sufficient breathing space to restructure its affairs by staying or prohibiting all legal proceedings against the company in business rescue in terms of section 130 of the Companies Act of 2008.
- (c) it gives the company in business rescue a period of respite to allow the company in business rescue to restructure its affairs by staying or prohibiting legal proceedings

against the company in question in terms of section 133(1) of the Companies Act of 1973.

- (d) it gives the company in financial distress a period of respite to restructure its affairs by suspending or precluding legal proceedings against the company while in business rescue as stipulated in section 133(1) of the Companies Act of 2008.
- (e) All of the above.

Question 1.5

Commented [M7]: 0 marks

Choose the **correct** statement:

Company X files for business rescue. Its only source of revenue is the proceeds of sales to its clients on credit. These debtors are ceded to X Bank as security for its loan to the company.

The company simply cannot survive if it does not have access to the proceeds of the payments by these clients from time to time. Under these circumstances, the business rescue practitioner may:

- (a) continue to utilise the proceeds of the debtors to operate the company as these debtors are not "property" as defined in the Companies Act.
- (b) approach the Court for an order to compel X Bank to consent to the company utilising the proceeds of these debtors in order to save the Company.
- (c) ensure that the total debtors' book does not decrease, by replacing every debtor receipt with at least an equal new sale to ensure that X Bank is not prejudiced by the continued use of the proceeds of the debtors to fund the ongoing operations of the company in business rescue.
- (d) approach X Bank for their consent to utilise the proceeds of these debtors for the ongoing operations of the company.

Question 1.6

Commented [M8]: 0 marks

Choose the **correct** statement:

As at the commencement of the business rescue process, X Bank holds security by way of a registered general notarial bond over of all of the assets of a company in business rescue.

X Bank may:

- (a) take possession of the assets subject to its security and sell it in order to reduce the company's indebtedness to X Bank.

(b) insist that the business rescue practitioner obtain their consent before selling any of the assets subject to the general notarial bond, as provided for in section 134 of the Companies Act.

(c) not prevent the business rescue practitioner from disposing of the assets subject to the general notarial bond in the normal course of business by the company during business rescue proceedings

(d) seek an order of Court to perfect their security, without the consent of the business rescue practitioner, in order to protect their rights.

Question 1.7

Commented [M9]: 0 marks

Choose the **correct** statement:

A company is leasing the property from which it is conducting its business. The company is placed in business rescue and continues to conduct its business from the property. The landlord has a claim for arrear rentals that have been incurred whilst the Company is in business rescue. This claim ought to be classified as:

(a) a business rescue cost.

(b) post-commencement finance.

(c) a preferent claim.

(d) a secured claim.

(e) an unsecured claim.

(f) a damages claim.

Question 1.8

Commented [M10]: 1 mark

Choose the **correct** statement:

You are appointed as business rescue practitioner in a large manufacturing business and within the first few weeks of your appointment an employee approaches you and advises you that they have been unsuccessful in obtaining authorisation for certain medical costs from the group medical scheme of the company since the filing for business rescue has taken place. The employee informs you that the medical scheme has indicated that due to non-payment of the deductions relating to the medical scheme by the company, that all of the benefits to employees under the scheme have been suspended. What would your advice to the employee be in relation to this issue?

- (a) Unfortunately, the employee would need to make payment of the outstanding amounts due to the medical scheme in order for the employee to enjoy further benefits from the group medical scheme.
- (b) As the benefits under the group medical scheme have been suspended, an alternative medical scheme would need to be sought by each employee, for the period of business rescue.
- (c) The group medical scheme, which exists for the benefit of both past or present employees of the company, would have an unsecured claim in the business rescue proceedings for the amounts that were not paid to the group medical scheme immediately prior to the commencement of business rescue proceedings and as such the medical scheme would not be entitled to suspend the benefits to such employees as the group medical scheme, as it is a creditor of the company in business rescue.
- (d) The group medical scheme would have a secured claim in the business rescue proceedings.
- (e) None of the above.

Question 1.9

Commented [M11]: 0 marks

Choose the **correct** statement:

The business rescue practitioner has an obligation to consult with creditors, other affected persons and the management of the company:

- (a) during the process of preparing a business rescue plan for consideration and adoption.
- (b) after preparing a business rescue plan for consideration and adoption.
- (c) before preparing a business rescue plan for consideration and adoption.
- (d) Both (a) and (c) are correct.

Question 1.10

Commented [M12]: 1 mark

Choose the **correct** statement:

You are a member of SARIPA and were certified by CIPC for the first-time last year to practice as a junior business rescue practitioner after you completed the INSOL SARIPA Programme in South African Business Rescue. Since then, you have accepted appointment as the business rescue practitioner of one small company and are busy implementing the business rescue plan that was adopted by creditors in that matter. You have been

approached by your brother-in-law to accept appointment as the business rescue practitioner of a large company that he is a director and shareholder of. Which of the below are appropriate?

- (i) You should not accept appointment as you have a conflict of interest.
- (ii) You can accept appointment.
- (iii) You should not accept the appointment as the company's business rescue practitioner as you are not independent.
- (iv) You should not accept appointment as you lack the necessary skills and do not meet the legislated criteria.

Your answer is:

- (a) (i).
- (b) (ii).
- (c) (iii).
- (d) Both (i) and (iii).
- (e) Both (iii) and (iv).

Question 1.11

Commented [M13]: 1 mark

Choose the **incorrect** statement:

- (a) The board of directors of the company can commence business rescue voluntarily by passing a board resolution, provided that it has reasonable grounds to believe that the company is financially distressed and there is a reasonable prospect of rescuing the company.
- (b) A creditor of a company can approach the High Court to place the company in business rescue, as long as the board of the company has not already adopted a resolution to begin business rescue proceedings.
- (c) As an affected person, an employee, an employee representative, a registered trade union, a shareholder or a director of a company can approach the High Court to place the company in business rescue, as long as the board of the company has not already adopted a resolution to begin business rescue proceedings.
- (d) Notwithstanding any financial distress, an affected person of a company may approach the High Court to place the company into business rescue provided that it is just and equitable to do so for financial reasons and there remains a reasonable prospect of rescuing the company.

Question 1.12**Commented [M14]: 1 mark**

Choose the **correct** statement:

A foreign-domiciled unsecured creditor is owed money by a company in business rescue for services that it supplied to the company outside of South Africa before the company entered business rescue. The creditor is refusing to recognise the approved business rescue plan, refused to vote on the plan when called to do so, and is arguing that their claim is not compromised by the moratorium because their debt was established and is owed outside of South Africa. How should the business rescue practitioner treat this creditor and their claim?

- (a) Because the creditor is a foreign business, it is not bound by the approved business rescue plan and its claim is not affected by the moratorium. The business rescue practitioner must settle the creditor's claim in full in the normal course.
- (b) The creditor's claim is preferent to the claims of other South African unsecured creditors and will rank ahead of them in terms of the payment waterfall.
- (c) The creditor's claim is treated the same as all other unsecured creditors, whether the creditor is foreign or South African, and whether it chose to vote on the business rescue plan or not.
- (d) Business rescue is a South African legal process aimed at trying to save financially distressed South African businesses and, as such, the claims of any foreign creditors are automatically fully expunged upon the commencement of business rescue proceedings.
- (e) If there are foreign-domiciled creditors, the business rescue practitioner must produce two business rescue plans - one to deal with local South African creditors and the other to deal with foreign creditors.

Question 1.13**Commented [M15]: 0 marks**

Choose the **correct** statement:

The company in business rescue's body of creditors includes the following claims (which have been accepted):

- Bank A: owed R60m and a fully secured creditor;
- 20 separate trade creditors: collectively owed R5m and unsecured;
- SARS: owed R5m in relation to income tax owing pre-business rescue and unsecured;
- Related / Inter-company X: owed R15m and unsecured;
- Party Y: owed R15m and which claim is subordinated in favour of all other creditors (an independent liquidation calculation valued this claim at R0);

All the above creditors attend the section 151 meeting to vote on the business rescue plan. However, only Bank A and Party Y vote in favour of the plan, with all other creditors (trade creditors, SARS and company X) voting against the plan. Has the plan been validly voted in / approved?

- (a) No: SARS's claim should be considered to be preferent and hence any vote is incorrect because of this obvious classification error.
- (b) Yes: The plan is voted in by virtue of 75% of all creditors voting in favour thereof (of which at least 50% of the independent creditors' voting interests were voted).
- (c) No: The plan is not voted in due to less than 75% of all creditors voting in favour thereof (despite the fact that more than 50% of the independent creditors' voting interests were voted).
- (d) No: 24 individual creditors in number (not value) voted and there were only 2 parties who voted in favour, therefore those voting against the plan far outweigh those voting in favour.

Question 1.14

Commented [M16]: 1 mark

Choose the **correct** statement:

Whilst section 150(c)(iv) does not require a cash flow statement or cash flow projections, best practice suggests that a cash flow should be presented. If presented, such a cash flow statement could explain to the reader:

- (a) The expected revenue (income) and expenses of the company, including depreciation and amortisation.
- (b) How expected cash receipts and payments are forecast to be received and paid respectively, that is, the liquidity of the company.
- (c) The financial position of the company as at the date of publication of the rescue plan.
- (d) All of the above.
- (e) Both (a) and (b) are correct.

Question 1.15

Commented [M17]: 1 mark

Choose the **correct** statement:

Per the Companies Act 2008, for what duration should the projections (statement of income and expenses and balance sheet) be prepared for in the business rescue plan?

- (a) Three years from the commencement of business rescue proceedings.
- (b) One year from around the date of publication of the business rescue plan.
- (c) Three years from around the date of publication of the business rescue plan.
- (d) Any amount of time - this is at the discretion of the business rescue practitioner.
- (e) Only for the duration of the proceedings until substantial implementation has been achieved.

Question 1.16

Commented [M18]: 1 mark

Choose the **correct** statement:

The business rescue plan can, once adopted, be "crammed down" on:

- (a) The secured and unsecured creditors.
- (b) Only those creditors and shareholders who voted in favour of its adoption.
- (c) The creditors and shareholders who were present at the meeting in which the plan was adopted.
- (d) The creditors and shareholders who were not present at the meeting in which the plan was adopted.
- (e) The company, its shareholders, and the secured and unsecured creditors, regardless of whether or not they were present, or voted in favour of adopting the plan.

Question 1.17

Commented [M19]: 1 mark

Choose the **correct** statement:

A motor-vehicle of a company in business rescue is valued at R100,000.00. The same vehicle is the subject of the security of X Bank, who are still owed R50,000.00 for financing the vehicle.

The business rescue practitioner wishes to sell the vehicle in the normal course of business as it is no longer required for the operation of the business. What is the correct course of action for the business rescue practitioner?

- (a) Always obtain the consent of X bank before selling any asset.

(b) If the business rescue practitioner is sure that the proceeds of the sale will be sufficient to settle the claim of X Bank, then he can sell the vehicle without their consent and simply pay what is owed to X Bank when he receives the sale proceeds for the vehicle.

(c) Simply sell the vehicle at the best possible price to his brother.

(d) All of the above.

Question 1.18

Commented [M20]: 1 mark

Choose the **correct** statement:

During the business rescue proceedings of any company the business rescue practitioner has to consider a vast number of statutory obligations that the company must comply with. With regard to employees' statutory rights as contained in the Labour Relations Act, which of the following statements is correct:

(a) The Companies Act 2008 supersedes the Labour Relations Act and therefore the only rights of employees during business rescue proceedings are contained in the Companies Act 2008.

(b) The business rescue practitioner must have regard to section 5 of the Companies Act 2008 in the general interpretation of the Companies Act 2008. The provisions of the Companies Act 2008 and the Labour Relations Act apply concurrently, to the extent that it is possible to apply and comply with one of the inconsistent provisions of the two Acts, without contravening the second. However, to the extent that it is impossible to apply or comply with one of the inconsistent provisions of the two Acts, without contravening the second, then the Labour Relations Act will prevail in the case of any inconsistencies.

(c) The business rescue practitioner must discount the provisions of the Companies Act 2008 and only rely on the provisions of the Labour Relations Act.

(d) The business rescue practitioner may elect to consider either the Labour Relations Act or the Companies Act 2008, however both cannot be interpreted concurrently.

(e) none of the above.

Question 1.19

Commented [M21]: 1 mark

Choose the **correct** statement:

If determined necessary, commencing a section 189 retrenchment process (in accordance with the provisions set forth in the Labour Relations Act), would be of significant benefit to most companies that have commenced business rescue, as this process is one of the

primary ways in which a financially distressed company can reduce overhead costs and operating expenditure. In this regard, when should a business rescue practitioner commence a section 189 process?

- (a) As soon as possible after the commencement of business rescue and the business rescue practitioner's appointment as practitioner. It is often a vital process in business rescue and should thus be prioritised as a critical procedure to be undertaken as soon after the commencement of business rescue as possible.
- (b) The business rescue practitioner is required to call for a vote on their intention to commence a section 189 process and this vote should be called at the first meeting of creditors convened in terms of section 147 of the Companies Act 2008. If the vote is passed by the requisite majority of creditors of the company, the business rescue practitioner should commence a section 189 process immediately after the vote has been passed in the section 147 first meeting of creditors.
- (c) The business rescue practitioner is required to include provisions regarding their intention to commence a section 189 process in the business rescue plan that they publish. The business rescue practitioner can only commence a section 189 retrenchment process if the business rescue plan contemplates the company commencing the process and only if it is duly approved and adopted by the requisite majority of creditors. Thus, the business rescue practitioner should only commence a section 189 process after publication of the plan and subsequent to the business rescue plan being voted on, approved and adopted by creditors.
- (d) The business rescue practitioner is legally permitted to commence a section 189 process at any time from the date of commencement of business rescue, but it must be initiated, and the requisite section 189 consulting period must be concluded, prior to the substantial implementation of the business rescue plan.

Question 1.20

Commented [M22]: 1 mark

Choose the **incorrect** statement:

If a business rescue practitioner is not appointed within five (5) business days after commencement of a company's voluntary business rescue:

- (a) The business rescue proceedings immediately end.
- (b) The business rescue resolution lapses and is a nullity.
- (c) The business rescue proceedings are not affected unless a court sets aside the resolution.
- (d) Approval of the business rescue plan will automatically cure this procedural error.

Where appropriate, refer to the case study below when answering the questions that follow.

CASE STUDY

Khusela Entertainment Proprietary Limited

Khusela Entertainment Proprietary Limited (**Khusela**) is a private company duly incorporated and registered as such under the applicable company laws of the Republic of South Africa (**South Africa**). Khusela has been operating as one of the largest record companies in South Africa for almost 30 years and has enjoyed great success and profitability through innovative branding, creative marketing and its management's ability to identify the latest trends in South African music and sign the greatest local talent. Leveraging off the influence and popularity of distinctively South African genres such as "Kwaito", "Gqom" and "Amapiano", Khusela has amassed a valuable catalogue comprising a multitude of well-known hits. Whilst Khusela's head office is located in Johannesburg, it operates recording studios in all major South African cities, including Polokwane, Durban, Pretoria, Mbombela, Bloemfontein, Gqeberha and Cape Town. For this purpose, Khusela has entered into various commercial lease agreements with Universal Properties Limited (**Universal Properties**), in terms of which studio space and recording equipment are leased from Universal Properties on a long-term basis. In order to facilitate artists' travel between the various recording studios, Khusela acquired a fleet of brand-new luxury mini-buses from Fast Cars Proprietary Limited under instalment sale agreements.

Over the past five years, Khusela has expanded rapidly in order to provide a complete service offering to its artists, music producers and promoters and consequently established a publishing division, an events management division as well as a record label called Soweto Music. As a result of this rapid expansion, Khusela incurred large amounts of high-interest debt by way of various financing arrangements with local banks and private equity firms. In addition to this, Khusela hired large amounts of employees in anticipation of increased demand resulting from its new service offerings. From having approximately 500 employees in 2015, Khusela's workforce (and its associated wage bill) quadrupled and comprised approximately 2,000 employees by the end of 2021. Khusela's employees are represented by the South African Entertainers Union (**SAEU**), a South African registered trade union that aims to safeguard the interests of musicians and entertainers, by advocating for fair labour practices and favourable working conditions for artists.

During the 2022 financial year, Khusela began to experience a substantial decrease in its operating revenue as a result of the following factors: (i) increased competition from new players in the South African music industry, (ii) the introduction of online platforms that allow artists to publish and distribute their music without the need to sign with a record label, and (iii) the increased tendency for up and coming artists to promote their music via social media platforms, as opposed to traditional means of marketing and promotion.

Due to the poor financial performance of Khusela during the 2022 financial year, Khusela's management went into panic mode and their immediate reaction was to pump additional capital into the business, in order to expand its service offering even further. As part of this capital-raising strategy, Khusela (i) entered into a revolving credit facility agreement with Crypto Bank Limited, in terms of which Khusela acquired a revolving credit facility in an aggregate amount equal to R100,000,000 against security in the form of a cession of book debts and a cession of all of Khusela's rights under its material distribution agreements, (ii) refinanced its existing debt (on more onerous and somewhat prejudicial terms) with Old Money Investment Corporation, a South African private equity firm, against the provision of additional security in the form of a mortgage bond registered over Khusela's head office and a deed of hypothecation over Khusela's registered trademarks, and (iii) initiated a rights offer in terms of which Khusela's existing shareholders acquired additional shares in the ordinary share capital of Khusela, and pursuant to which approximately R30,000,000 in additional equity was raised.

After acquiring additional capital to fund its business, Khusela's outlook in the short term seemed positive. However, it quickly became apparent to Khusela's Chief Financial Officer, Mr Kabelo Mogale and its Chief Executive Officer, Mr Themba Sithole, that whilst there was a noticeable increase in profits (as reflected in the latest management accounts), the likelihood of Khusela becoming overindebted in the long-term remained. For this reason, Kabelo and Themba set out to obtain legal advice from Best Law Inc on the options available to companies experiencing financial distress, as a precautionary measure. In particular, they wished to understand the entry routes into the South African business rescue process and the prescribed statutory requirements for each route.

In the midst of their financial uncertainty, and just as Khusela began to recover from its financial decline, a group of Khusela's biggest artists (and largest contributors of revenue), announced that they wished to leave Khusela's record label, reclaim their master rights, and go independent. This decision resulted in significant cash shortfalls given that Khusela experienced a substantial and unexpected reduction in its revenue streams. This "liquidity crisis" culminated in Khusela being unable to service its debt obligations and pay its overheads at the beginning of the year 2023. It then became clear to Khusela's board of directors that it appeared to be reasonably unlikely that the company would be able to pay its debts as they became due and payable in the ordinary course, and at this point, Khusela's draft financial statements indicated that the company's liabilities exceeded its assets.

Whilst Khusela's board of directors were contemplating the options available to them, the company was not able to pay its critical suppliers, landlords and its employees' salaries. As a result, certain creditors began taking legal action to recover the amounts owing to them, and in this regard:

- (i) Opera Sound Engineering Services Proprietary Limited (**Opera Sound Engineering**) issued a money judgment application in the High Court of South Africa KwaZulu-Natal Division, Durban against Khusela, in terms of which it claimed certain amounts owing by Khusela pursuant to repairs carried out by it at one of Khusela's studios;
- (ii) World of Music Proprietary Limited had begun preparing a liquidation application, on the basis that Khusela ought to be deemed to be unable to pay its debts;
- (iii) Fast Cars Proprietary Limited threatened to cancel the instalment sale agreements entered into with Khusela, as a result of Khusela's failure to pay instalments under the relevant instalment sale agreements; and
- (iv) In addition to the abovementioned legal steps, Universal Properties, one of Khusela's landlords and a creditor that was owed in excess of R20,000,000 in arrear rentals, sought legal advice and subsequently brought an application in the High Court of South Africa Gauteng Local Division, Johannesburg as an "affected person" to place the company under supervision and commence business rescue proceedings. In its business rescue application, Universal Properties nominated Ms Sarah van Zyl (a senior practitioner) for appointment as the business rescue practitioner of Khusela. After considering the business rescue application brought by Universal Properties, the High Court granted an order placing Khusela into business rescue and made a further order appointing Ms Sarah van Zyl as interim business rescue practitioner.

In light of the fact that salaries remained unpaid for a substantial period of time, and given that Khusela was subsequently placed into business rescue, the employees of Khusela were uncertain about what they could expect and wished to obtain the following legal advice:

- (i) whether their position in business rescue was more advantageous than if Khusela was put into liquidation;
- (ii) whether they (as employees) have any statutory rights to participate in the business rescue proceedings;
- (iii) a breakdown of the status of their claims in respect of unpaid salaries (both pre-business rescue and post-business rescue), in terms of the provisions of the Companies Act 2008 (**Companies Act 2008**);
- (iv) whether the business rescue practitioner may unilaterally amend and vary their employment terms and conditions; and
- (v) whether they may be validly retrenched in terms of the applicable labour laws of South Africa read with the Companies Act 2008.

The employees of Khusela obtained a detailed legal opinion from insolvency and restructuring law experts on the aforementioned issues.

Following her appointment, Ms Sarah van Zyl immediately assumed full management control of Khusela and scheduled a first meeting of creditors. At the first meeting of creditors, Ms Sarah van Zyl's appointment was ratified in the manner prescribed by the Companies Act 2008 and thereafter she began to investigate the affairs of Khusela, with the view of developing a business rescue plan.

During the course of Sarah's investigations, she was approached by Themba Sithole (the CEO of Khusela) who informed her that he had previously bound himself as surety for the debts of Khusela under the initial funding transaction entered into with Old Money Investment Corporation in the year 2019. Themba was curious to know whether his obligations under the deed of suretyship had been extinguished by virtue of the fact that Khusela was placed into business rescue proceedings. Sarah addressed a letter to Themba setting out the status of Themba's obligations under the deed of suretyship in light of relevant case law.

In relation to the various contracts concluded by Khusela with its various suppliers and landlords (prior to the commencement of business rescue proceedings), Sarah was uncertain as to whether she was able to suspend and / or cancel prejudicial contracts. She recalls from legal advice that she obtained previously that the Companies Act 2008 gives business rescue practitioners the ability to suspend or cancel prejudicial contracts, but she is uncertain as to how this may be done practically. Consequently, Sarah reached out to Best Law Inc and requested them to prepare a brief legal opinion dealing with the suspension or cancellation of prejudicial contracts in the business rescue context.

Following her investigations into the business and affairs of Khusela, Sarah was of the view that Khusela was capable of being rescued, particularly in view of Khusela's established brand and goodwill that it has in the South African music industry. She immediately sets out to secure post-commencement financing to keep the company afloat, whilst Khusela's business rescue plan was being prepared and drafted for consideration by creditors.

The business rescue plan of Khusela was eventually published a year after Sarah was appointed as the business rescue practitioner. The business rescue plan was subsequently put to a vote at a meeting of creditors held in terms of section 151 of the Companies Act. The business rescue plan of Khusela was supported by the requisite majority of creditors and was finally adopted.

Opera Sound Engineering, a minority creditor, voted against the adoption of the business rescue plan, as its board of directors was of the view that there were no reasonable prospects of Khusela being rescued. The board of Opera Sound Engineering was further of the view that the approved business rescue plan was not binding on Opera Sound Engineering at all, given that it had voted against the adoption of the business rescue plan.

Sarah proceeded to implement Khusela's approved business rescue plan. The business rescue proceedings of Khusela continued over a prolonged period of time and eventually it became clear that the business rescue plan was not capable of being implemented in its initial form. Sarah consequently amended Khusela's business rescue plan unilaterally and circulated a notice to creditors informing them of such amendments. The provisions of the amended business rescue plan were prejudicial to the interests of Crypto Bank Limited and Old Money Investment Corporation. Accordingly, both Crypto Bank Limited and Old Money Investment Corporation initiated joint legal proceedings to have Sarah removed as the business rescue practitioner. The application to remove Sarah as the business rescue practitioner was unsuccessful.

Ultimately, despite the best efforts of Ms Sarah van Zyl and Khusela's board of directors, it was determined that Khusela was not capable of being rescued. Accordingly, Ms Sarah van Zyl proceeded to take the necessary steps to place Khusela into liquidation.

Question 2

It is recorded in the case study that "certain creditors began taking legal action to recover the amounts owing to them". Briefly discuss the enforceability of legal proceedings in light of Khusela's ongoing business rescue proceedings. (2)

[Type your answer here]

By virtue of being in business rescue, Khusela does enjoy protection against legal proceedings instituted against it as a result of the moratorium provided for in section 133(1) of the Companies Act. This means the creditors who have served it legal proceedings would be entitled to institute and continue with those legal proceedings only with the consent of the business rescue practitioner or the leave of the court. Thus, those creditors are not entitled to institute and continue with those legal proceedings as if Khusela was not in business rescue.

Question 3

What is the requisite majority of creditors' support that is required for a business rescue plan to be adopted? (3)

[Type your answer here]

Section 152(2) of the Companies Act 2008 - explain the meaning of the requisite majority (forexample that in a vote called in terms of subsection (1)(e), the proposed business rescue plan will be approved on a preliminary basis if it was supported by the holders of more than 75% of the creditors' voting interests that voted; and the votes in support of the proposed plan included at least 50% of the independent creditors' voting interests, if any, that voted

Commented [M23]: 2 marks out of 2.

Commented [M24]: 2 marks out of 3. Need to refer to the approval by holders of security in the event that their interests are affected.

Question 4

It is mentioned that Opera Sound Engineering voted against the business rescue plan. Is the approved business rescue plan binding on Opera Sound Engineering? Substantiate your answer with authority. (3)

[Type your answer here]

Section 152(4) of the Companies Act 2008 provides that once a business rescue 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 business rescue 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.

Binding nature of this business rescue plan:

The attention of affected persons is drawn to the provisions of section 152(4) of the Companies Act 2008. This section provides that once a business rescue plan has been adopted, it is binding on Khusela, its creditors (including all claims, whether accepted by the business rescue practitioner as creditors, whether foreign or local creditors, whether disputed creditors, conditional claims and / or prospective claims) and every holder of the Khuselas' securities, whether or not such a person:

- was present at the meeting to determine the future of Khusela;
- voted in favour of the adoption of the business rescue plan; or
- in the case of creditors, had proven a claim against Khusela.

Question 5

Considering the fact that Khusela was already unable to pay its debts at the time of the application to place it in business rescue, explain whether the requirement of financial distress as defined in the Companies Act 2008 was met, or whether it was too late for a business rescue order to be issued. (5)

[Type your answer here]

Financially Distressed in reference to a particular company at any particular time, means that –

- 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

Commented [M25]: 3 marks out of 3.

Commented [M26]: 1 mark out of 5. Needed to discuss the requirement of financial distress specifically with reference to applicable case law.

- it appears to be reasonably likely that the company will become insolvent within the immediately ensuing six months.
- The test for financial distress is forward-looking
- It 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.

Yes, the directors did correctly assess the situation with supporting legal advice. Financial distress as defined in section 128 of Companies Act 2008 was met as both commercial or factual (balance-sheet) insolvency, current and the next 6 months was diagnosed. 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.

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:

- factually insolvent (that its liabilities will exceed its assets);
- or commercially insolvent (unable to pay its debts as they become due and payable) in the next six-month period.

The BRP will need to use all their skills (EQ, negotiation, persuasion - counter-arguments, etcetera) as conveners, arbitrators and agitators to reset 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).

There are methods of cost reduction and strategic re-alignment of business activities to create successful business rescue. The Business Rescue Practitioner, Ms Sarah van Zyl, acted promptly and cut costs by reducing staff counts and regress the business to a previously sustainable level. The commencing a section 189 retrenchment process (in accordance with the provisions set forth in the Labour Relations Act), would be of significant benefit to most companies that have commenced business rescue, as this process is one of the primary ways in which a financially distressed company can reduce overhead costs and operating expenditure.

The sale of unencumbered assets to pay of liabilities or finance working capital are mechanisms to improve short term cash flow.

The loss of a major client has created a dent in earning potential and restructuring is necessary to meet liquidity demands. An analysis of all existing contracts to immediately reduce expenditure is required.

The model of the business has been impacted severely by the technology and social advances but time was required to test the markets. The Business Rescue Practitioner, Ms Sarah van Zyl exhausted avenues to recreate success and then came to a conclusion that the business model was no longer sustainable.

Question 6

What effect - if any - would the application for Khusela to be placed in business rescue have on the application by World of Music for the company to be placed in liquidation had this application (for liquidation) already been filed at the High Court at the time? (5)

[Type your answer here]

Effect of Business Rescue application on liquidation proceedings (section 131(6))
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, or the business rescue proceedings end, if the court makes the order applied for.

Section 131(6) of the Companies Act 208 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.

When application "is made" for business rescue it suspends current liquidation proceedings until court has adjudicated upon the Business Rescue application

Meaning of "liquidation proceedings"?

An application for BR can be made "at any time" (s 131(1))

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

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;

Question 7

In addition to the cession of books debts in favour of Crypto Bank, it also insisted and thereafter registered a general notarial bond over the movable assets of Khusela.

Commented [M27]: 1 mark out of 5. Needed to discuss relevant case law ie. *Lutchman NO v African Global Holdings, ABSA Bank Limited v Summer Lodge and Standard Bank of South Africa v A-Team Trading CC*. Also needed to mention that the issue for consideration is whether a pending liquidation application should be regarded as part of liquidation proceedings prior to the application being heard in court.

Commented [M28]: Total for Q7: 3 marks.

Ms Sarah van Zyl identified a large amount of redundant equipment and even a few unroadworthy old vehicles that could be sold urgently in order to fund the ongoing operation cost of Khusela during business rescue.

Crypto Bank came to hear of Sarah van Zyl's intention to sell these assets and addressed a letter to her via their attorneys threatening to launch an urgent Court application to interdict her from selling the assets subject to their security, without their consent.

Question 7.1

Sarah Van Zyl approaches her lawyers at Best Law Inc for advice on what the legal position of Crypto Bank with regard to the general notarial bond, and her prospects of success in opposing the threatened urgent application. As an experienced lawyer at Best Law Inc advise Sarah van Zyl on whether or not she is entitled to sell the assets in question without Crypto Bank's consent. (2)

[Type your answer here]

A general notarial bond only confers a preference to its holder, upon liquidation, and then only after the statutory preferences and before other concurrent creditors. This "preference" is only triggered in terms of the laws of insolvency. Crypto Bank would further be unable to apply to court for the perfection of their general notarial bond, without the consent of the business rescue practitioner.

As Crypto Bank general notarial bond only confers preference in the event of a liquidation, the assets subject to the general notarial bond remain unsecured and the business rescue practitioner will be able to utilise the assets in the normal course without their consent.

That is, in order to dispose of the security, the business rescue practitioner would have to obtain the prior consent of the financiers, unless the proceeds of the disposal would be sufficient to fully discharge the indebtedness owed to the financiers.

Question 7.2

If Sarah van Zyl is in a position to sell the assets, what would the requirements for such disposal be? (4)

[Type your answer here]

That is, in order to dispose of the security, the business rescue practitioner would have to obtain the prior consent of the financiers, unless the proceeds of the disposal would be sufficient to fully discharge the indebtedness owed to the financiers.

However, if the business rescue practitioner does not dispose of the security and the secured creditor's claim is either compromised in terms of section 154(1) or becomes unenforceable under section 154(2), the security may have to be released unless the business rescue plan provides otherwise.

Commented [M29]: 0 marks out of 2. See page 75 of the Course Notes.

Commented [M30]: 3 marks out of 4. Requirements of section 134(1)(a) had to be discussed. See Chapter 4 of the Course Notes.

Also, Section 112 of the Companies Act provides that a company may not dispose of all or a greater part of its assets unless the disposal has been approved by a special resolution of shareholders.

A transaction such as this cannot be in the ordinary course of business for Kusela - section 134(1)(a)(i).

The business rescue practitioner would have to consider whether such a transaction would be considered as bona fide, at arm's length and for value. Assuming the need for cash is urgent and the sale can continue as long as the transaction meets the requirements of section 134(1)(a)(ii).

Considering the unusual nature of the proposed transaction it would be more prudent to consider such a transaction only pursuant to an adopted business rescue plan authorising such disposal. Section 134(1)(a)(iii), but urgency may make this safer option unrealistic.

Question 8

Commented [M31]: 5 marks.

Sarah Van Zyl approaches Easy Access PCF, a well-known provider of funding to distressed businesses, for a loan to fund the expected operational losses during business rescue. After a short due diligence, Easy Access PCF indicate that they are willing to provide post commencement funding of R1,000,000 subject to Sarah agreeing to sell to them the proceeds of Khusela's existing material distribution agreements and the proceeds being paid to them directly until such time as the post commencement finance is repaid in full.

Advise Sarah van Zyl under which circumstances she can agree to Easy Access's requirements considering that the rights to these agreements have already been ceded to Crypto Bank. (5)

[Type your answer here]

Even if the business rescue practitioner considers the disposal as bona fide, the shares and loan account are subject to a cession in favour of Crypto Bank,. Where there was initial debate as to whether a holder of a cession of rights held a "security interest", as defined in the Act, and further whether a business rescue practitioner could suspend such obligation. Our Courts have now brought finality to the debate with the unambiguous judgment of Van den Heever vs Van Tonder, confirming that a holder of a cession of rights, in securitatem debiti, has a "security interest" and is a secured creditor as envisaged in section 134.

If the proceeds of the intended sale are insufficient to settle the indebtedness of the secured creditors, then the business rescue practitioner cannot dispose of these assets without obtaining the secured creditors prior consent. If however the proposed sale will realise sufficient proceeds to settle the secured creditor in full, then the business rescue

practitioner would not need the creditors written consent, or settling the secured creditor in full from the proceeds of the secured asset as required in section 134(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-

- 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

promptly-

- 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
- provide security for the amount of those proceeds to the reasonable satisfaction of that other person."

Question 9

The business rescue practitioner of Khusela Entertainment (Pty) Ltd was faced with a work force of over 2,000 employees at the commencement of the business rescue proceedings. Within the first week of business rescue proceedings having commenced, the business rescue practitioner identified the need to embark on a retrenchment process with more than fifty percent (50%) of the employees of Khusela Entertainment (Pty) Ltd, for operational considerations. The business rescue practitioner, being a prudent and careful business rescue practitioner, immediately embarked on a section 189 consultative process with the affected employees of Khusela Entertainment (Pty) Ltd, in terms of the relevant provisions of the Labour Relations Act. The first consultation took place two weeks after the commencement of business rescue proceedings, with the various consultative meetings taking more than 60 days to complete and, eventually, more than 1,500 employees of Khusela Entertainment (Pty) Ltd were retrenched for operational considerations during the business rescue proceedings.

Despite the negative impact this had on the employees who were retrenched, the business rescue practitioner ensured that the cash flow for the business was restored to a manageable level for the business, the employees were paid their severance packages, and the business rescue practitioner felt that the correct decisions were made pursuant to the consultative process with the employees.

This retrenchment process and the resultant cash flow relief paved the way for the business rescue practitioner to draft the proposed business rescue plan, which was published after the section 189 process was finalised.

In light of the rights of employees and the current case law on this subject, discuss whether the business rescue practitioner followed the correct process and procedure in this case.

(7)

[Type your answer here]

Commented [M32]: 3 out of 7. Needed to state that the status and rights of employees in a BR process are entrenched in Chapter 6 and the provisions of Chapter 6 do not supersede the provisions of the LRA and BCEA. Need to specifically state what the section 189 process can be used for - i.e altering of rights and status, or retrenchment of employees. Need to state that the BRP could contemplate issuing voluntary severance packages, subject to any collective agreements. Needed to apply the legal principles to the facts and conclude that the section 189 process carried out by Sarah was both unlawful and unenforceable.

Yes, the business rescue practitioner did identify that due to the loss of clients that the staff number were extremely high and as a result the costs need to be reduced in a manner to support a positive cash flow and improve solvency of the business. The immediate analysis of extremely high salary costs and the beginning of the consultative process in terms of section 189 was prudent and correct action taken by Sarah Van Zyl to affect an early as possible retrenchment process that was collective agreement in place with organised labour that would allow for such actions to be validly enforced through such collective agreement. The BRP will need to use all their skills (EQ, negotiation, persuasion - counterarguments, etcetera) as conveners, arbitrators and agitators to reset the threat of the runaway costs.

The rights of employees during a business rescue are of paramount and the Companies Act 2008 has entrenched the rights of employees during business rescue proceedings. A business rescue practitioner may not unilaterally amend or vary the terms of a contract of employment. An employee would retain all his rights in terms of his contract of employment and any rights that may be conferred on that employee in terms of the Basic Conditions of Employment Act and the Labour relations Act. In order for the business rescue practitioner to retrench she would have to ascertain if there is a collective agreement in place with organised labour that would allow for such actions to be validly enforced through such collective agreement. However, in the absence of a collective agreement that provides for salary and wage costs, the only manner within which a business rescue practitioner can vary the obligations of the company to its salary and wage staff would be to do so by agreement between the parties. The business rescue practitioner may, post the publication of a business rescue plan, commence with a section 189 consultative process in terms of the Labour Relations Act and retrenchment of such staff during the business rescue. Of importance is the fact that a section 189 process may not be commenced until such time as a proposed business rescue plan has been tabled by the business rescue practitioner to all affected persons. Should a business rescue practitioner unilaterally attempt to amend terms and conditions of employment of an employee during business rescue proceedings, the employee would be entitled to approach the Labour Court for relief.

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 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.

In the matter SA Airways (SOC) Ltd (In Business Rescue) ("SAA") and Others v National Union of Metalworkers of SA ("NUMSA") on behalf of Members and Others (2020), the Labour Court upheld an urgent application by NUMSA and the SA Cabin Crew Association (the Unions) against SAA and the business rescue practitioners, and ordered that it was procedurally unfair to retrench employees before a business rescue plan contemplating such retrenchments was published and adopted. Thus, the **Fast Flight** business rescue practitioner did not commence a section 189 large-scale retrenchment process prior to the publication of the business rescue plan. This judgment set a precedent that retrenchments in business rescue cannot be contemplated or commenced, unless provided for in a company's business rescue plan that is duly approved and adopted.

Question 10

Discuss the general rights held, if any, by the employees of Khusela during the business rescue process of Khusela. (3)

[Type your answer here]

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.

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 statute.

The contractual rights of an employee subject only to the provisions of all applicable labour legislation, which may include the Labour Relations Act, Basic Conditions of Employment Act 1997²⁴⁹ and all relevant regulations to such applicable legislation.

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.

Question 11

Commented [M33]: Copy and paste?

Commented [M34]: 0 marks. The question required you to discuss the rights of employees and not their position in a business rescue. Mention rights to receive notice, participate in the BR, bring an application, form an employees committee etc.

Commented [M35]: 2 marks. Needed to state that the directors remain bound by the requirements of section 75 and to the extent that they act according to the BRP's instructions and subject to the BRP's authority, they are relieved of certain of their fiduciary duties.

Discuss whether Mr Themba Sithole (the Chief Executive Officer), (ii) Mr Kabelo Mogale (the Chief Financial Officer) and (iii) the board of directors would have had any role during the business rescue process of Khusela. (3)

[Type your answer here]

The directors must continue to exercise their functions as directors, subject to the authority of Sarah van Zyl and they owe a duty to Khusela to exercise any management function in accordance with the instructions of Sarah van Zyl. If one or more of the directors or the board purports to take any action on behalf of Fast Flight that requires the approval of Sarah van Zyl, that action is void unless approved by him.

Commented [M36]: Copy and paste?

Mr Themba Sithole and his fellow directors have mandatory statutory duties to cooperate with and assist Sarah van Zyl and must (i) attend to his reasonable requests (ii) provide information about the company's affairs, and (iii) as soon as possible after the commencement of the business rescue proceedings, deliver to him all of the company's books and records that may be in their possession. They must also, within five business days of the commencement of the business rescue, provide him 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.

Section 137(2) of the Companies Act 2008 provides that during the course of a company's Ordinary 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.

Question 12

Commented [M37]: 5 marks.

Ms Sarah Van Zyl would have had an obligation to consult with creditors, other affected persons, and the management of Khusela before preparing a business rescue plan for consideration. With reference to case law, what should the term "consultation" entail in this context? (5)

[Type your answer here]

The court in the case of *Hlumisa Investments Holdings (RF Limited and Another) v Van der Merwe NO and Others*, 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*, 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 means 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 announcements and in meetings with individual shareholders and a body of preferent shareholders, did not amount to "consultation".

Ms Sarah Van Zyl is therefore obliged to engage properly with the shareholders, to hear their views and to take them into account before finalising the business rescue plan. If Ms Sarah Van Zyl publishes a plan and schedules a meeting to vote on that plan without proper consultation with the shareholders, they can go to court on an urgent basis to interdict the meeting pending proper consultation with them.

Question 13

Commented [M38]: 2 marks.

Discuss whether Ms Sarah Van Zyl could propose an agreement with Khusela providing for further remuneration in addition to what is permitted by the government-regulated tariff, and who would have to approve such proposal? (2)

[Type your answer here]

As Ms Sarah Van Zyl is earning remuneration in excess of the tariff rates, she would be obliged to enter into a remuneration agreement with Khusela. Shareholders would have a right to vote in favour or against her remuneration agreement, if they would be entitled to claim a portion of the residual value of the company on a winding up.

As far as the tariff rates were set in 2011 and appraisal with prime rates may be acceptable to compensate for inflation.

Where a business rescue practitioners' remuneration exceeds the rates outlined in the tariff, such arrangement requires a remuneration agreement to be entered into between the company and the business rescue practitioner. Such an agreement should furthermore be voted on and approved by creditors and shareholders ahead

of the publication of the business rescue plan. Finally, a copy of the written agreement concerning the business rescue practitioners' remuneration should be disclosed in the business rescue plan.

Question 14

Is Khusela Entertainment a small, medium or large company, and what is the tariff rate per hour that Ms Sarah van Zyl can charge for her services as business rescue practitioner? Base your answer on the information provided and assume no significant changes between the dates set out in the case study and the date of commencement of business rescue. (3)

[Type your answer here]

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);

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.

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.

On employee count basis Khusela Entertainment is a large company. So Ms Sarah van Zyl tariff rate will be R2000 per hour and a maximum of R25 000 per day.

Question 15

The case study includes the following statements:

Commented [M39]: 2 marks out of 3. Needed to state that the public interest score of Khusela is greater than 500 points as it has more than 2000 employees.

Commented [M40]: 0 marks. Needed to discuss the fact that at the first meeting of creditors, a business rescue practitioner must inform the creditors whether the practitioner believes that there is a reasonable prospect of rescuing the company. Sarah ought to have commenced an investigation into the affairs of the company immediately on being appointed to comply with this duty.

“At the first meeting of creditors, Ms Sarah van Zyl’s appointment was ratified in the manner prescribed by the Companies Act and thereafter she began to investigate the affairs of Khusela.”

and

“Following her investigations into the business and affairs of Khusela, Sarah was of the view that Khusela was capable of being rescued.”

Read together these statements indicate that Sarah may not have complied with the Companies Act 2008 in performing her duties as the business rescue practitioner of Khusela Entertainment. Identify the section of the Act that may not have been complied with and explain why and what should have been done differently. **(3)**

[Type your answer here]

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 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

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.

Question 16

The business rescue plan was published almost a year after the commencement of business rescue proceedings. The delay would have triggered a number of duties or obligations on the business rescue practitioner. List these and identify the relevant section of the Act that creates the obligation or duty. **(4)**

[Type your answer here]

Some of the duties and obligations are discussed include the duty to:

publish monthly progress reports on the business rescue proceedings if the proceedings last for more than three months; Companies Act 2008, s 132(3).

Commented [M41]: 2 marks. Needed to mention section 150(5) - securing an extension of time to publish the BR plan.

ensure that the company protects the interests of creditors that hold a security or title interest over any property; s 134(3).

notify regulatory authorities of the commencement of business rescue proceedings and that they have been appointed; s 140(1A).

the duties and liabilities of a director as set out in sections 75 to 77 of the Act; s 140(3).

investigate the affairs of the company; s 141.

notify affected persons of each court proceeding, decision, meeting or other relevant event concerning the business rescue proceedings; ss 144(3), 145(1)(a) and 146(a).

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; s 145.

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; s 147(1).

give notice of the first meeting to every creditor of the company whose name and address is known or can reasonably be obtained; s 147(2).

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; s 148(1).

give notice of the first meeting to every employee and registered trade union representing employees of the company; s 148(2).

consult with affected persons prior to publishing a proposed business rescue plan; s 150, read with ss 144, 145 and 146.

ensure that the proposed business rescue plan contains the minimum prescribed information; s 150(2).

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; s 151

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 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; s 152(1).

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; s 152(5).

entertain motions requiring the practitioner to prepare and publish a revised plan where the proposed plan was rejected; s 140(1)(a), and leave 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; s 137(2), (3).

Question 17

Mr Sandiso Siwisa, who is the cousin of one of the directors of Khusela, owns 25% of the issued share capital of Khusela. Mr Siwisa's half-sister, Mrs Lungi Phillips, owns 26% of the issued share capital of Khusela. There is only one class of shares and each share affords a shareholder one vote.

Mr Siwisa is also a creditor of Khusela by virtue of a R500,000 loan made to Khusela when it urgently needed cash during 2022.

Is Mr Siwisa an independent creditor of Khusela? Provide full reasons for your answer. (5)

[Type your answer here]

Mr Sandiso Siwisa is not an independent creditor of Khusela.
Mr Siwisa's half-sister owns 25% of the issued share capital of Khusela.
Mr Siwisa is also a creditor of Khusela by virtue of a R500,000 loan made to Khusela.

In terms of the Companies Act 2008, an independent creditor is defined as:

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) of the Companies Act 2008.

Question 18

Comment on the validity of the business rescue practitioner, Sarah van Zyl, having the "ability" to unilaterally amend the business rescue plan. Also discuss the requirements of

Commented [M42]: 2 marks. Needed to discuss the definition of "related" and the provisions of section 2(1)(a) to (c) of the Companies Act. Needed to demonstrate why Mr Siwisa is not an independent creditor.

Commented [M43]: 3 marks. Marks awarded for the case law discussion.

implementing an amendment to the business rescue plan with reference to the Companies Act 2008 and appropriate case law. (8)

[Type your answer here]

The status and rights of employees in a business rescue process are entrenched in chapter 6 of the Companies Act 2008, and the provisions of chapter 6 of the Companies Act 2008 does not supersede the provisions of the Labour Relations Act nor the Basic Conditions of Employment Act. Accordingly, a business rescue practitioner does not have the statutory power to unilaterally amend or cancel any contract of employment or any aspect of a contract of employment, without the express consent of the employees concerned.

The unilateral amendment of the salaries and benefits of such employees by the business rescue practitioner would be seen as an unfair labour practice and his attempt to do so is accordingly unlawful.

The financial distress of the company would affect employees and in the absence of a collective agreement that allows for a reduction in salaries and benefits of such employees in terms of such collective agreement, the business rescue practitioner would be required to commence with a section 189 consultative process in terms of the Labour Relations Act, if it is perceived that rescue proceedings would have an effect on the rights of employees during a business rescue process.

As part and parcel of the section 189 consultative process in terms of the Labour Relations Act, and as an alternative to a proposed retrenchment, the business rescue practitioner could propose a reduction in salaries and benefits of employees in order to assist and alleviate in the cash flow pressures of the business during proceedings. Accordingly, section 189 can be utilised to create consensus and agreement between employees and the company in rescue regarding the altering of the rights and status during proceedings, as an alternative to a potential retrenchment.

One must however be cognisant of the Labour Appeal Court decision that requires other business rescue practitioners who envisages the need for a section 189 process in terms of the Labour Relations Act to include this in his proposed business rescue plan prior to the commencement of the section 189 process.

Should the business rescue practitioner continue to implement the unilateral amendment of the contractual rights between the company and its employees, the employees would have the right to approach the Labour Court for urgent relief as the business rescue practitioner 's actions are unlawful.

Booyesen 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.

Question 19

Placing yourself in the shoes of Opera Sound Engineering, explain three key items you would expect to see in the financial projections of the business rescue plan to assist you to vote in the business rescue of Khusela. (3)

[Type your answer here]

- Balance sheet for the ensuing three year period required.
- Income statement on a monthly basis for the first year and annualised thereafter ,
- Detailed cash flow statement for the three years with the first year monthly and annualised thereafter.
- The financial projections are the basis upon which the affected persons are able to assess the overall proposal and likely success of the business rescue. The financial projections guides the vote on the plan. The more granularity that is provided, the better, as this assists affected persons in understanding the reasonableness, to a greater degree, of the projections. Cash flow is vital to the success of a business rescue and it demonstrates how the business rescue dividend / distribution will be paid, future lifeblood of the business and highlights any potential liquidity challenges in the forecast period.

Section 150(3) of the Companies Act

Question 20

Ms Sarah van Zyl has asked you whether she should include a cash flow statement in her business rescue plan, as technically it is not required. What would your response be? (2)

[Type your answer here]

- Cash flow is vital to the success of a business rescue and it demonstrates how the business rescue dividend / distribution will be paid, future lifeblood of the business and highlights any potential liquidity challenges in the forecast period.

Question 21

From the perspective of the employees, what are three advantages of Khusela being placed in business rescue rather than being liquidated? (3)

[Type your answer here]

The rationale 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 - Focus is on "saving companies not destroying them"

Commented [M44]: 0 marks. The question requires to list three items you would expect to see in the financial projections of the BR plan.

Commented [M45]: 1 mark.

Commented [M46]: 3 marks.

Statutory protection contained in Chapter 6:
Employment contracts do not terminate
Retrenchments subject to Labour Relations Act 66 of 1995
Priority as post-commencement creditors.

***** END OF ASSESSMENT *****

TOTAL MARKS: [100]