



INSOL
INTERNATIONAL



PROGRAMME IN SOUTH AFRICAN BUSINESS RESCUE 2023

Commented [BB1]: TOTAL = 75/100 (mark adjusted upwards) - Well done, excellent result

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: 16 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]: 1 mark

- (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]: 1 mark

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]: 1 mark

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]: 1 mark

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]: 1 mark

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]: 0 marks

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]: 0 marks

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)

In terms of section 133(1) of the Companies Act, during business rescue proceedings, no legal proceedings or enforcement action against the company or in relation to any property belonging to or in the lawful possession of the company may be commenced or proceeded with. This is the general moratorium which is a key feature of business rescue as it gives a company some breathing room to rearrange its affairs and attempt to return to profitability.

Section 133(1) of the Companies Act sets out exceptions to the general moratorium. Based on the facts set out in the case study, legal proceedings and enforcement action could only be commenced or proceeded with, with the written consent of the business rescue practitioner or with the leave of the court in accordance with terms the court considers suitable.

None of the creditors would be entitled to commence or proceed with legal proceedings or enforcement action against Khusela without reliance on one of the two exceptions listed above apply.

Question 3

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

Commented [M23]: 2 out of 2 marks.
Excellent answer.

Commented [M24]: 3 out of 3 marks.
Excellent answer.

In terms of section 152(2) of the Companies Act, the requisite support to preliminarily approve a proposed business rescue plan is 75% of creditors' voting interests voted and at least 50% of independent creditors' voting interests voted.

In terms of section 152(3)(b) of the Companies Act, if the proposed business rescue plan does not alter the rights of the holders of any class of securities of the company, then the preliminary approval under section 152(2) will be the final approval.

In terms of section 152(3)(c) of the Companies Act, if the proposed business rescue plan does alter the rights of the holders of any class of securities of the company, then the majority of the holders of that class of affected securities must vote to approve the proposed plan in order for it to be finally approved and adopted.

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)

The approved business rescue plan is binding on Opera Sound Engineering despite it voting against the plan.

In terms of section 151(4) of the Companies Act, an adopted business rescue plan is binding on the company, each of its creditors and every holder of the company's securities whether or not they were present and the meeting at which the plan was voted on, voted in favour of adoption of the plan or, in respect of creditors, have proven their claims against the company. This is known as the "cram-down" principle.

In *African Banking Corporation of Botswana Ltd v Kariba Furniture Manufacturers (Pty) and Others* (2013 (6) SA v471 (GNP)), the court held that the "cram-down" principle was important for the successful implementation of an approved business rescue plan as it prevents any continued dispute and frustration in the implementation of the plan, particularly for selfish or nefarious reasons.

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)

Section 128(1)(f) of the Companies Act defines "financially distressed" in relation to a company at a particular time, that:

Commented [M25]: 3 out of 3 marks. Correct section reference is section 152(4) - mark awarded because content was correct.

Commented [M26]: 3 marks out of 5. Needed to discuss the principles in *Gormley v West City Precinct Properties (Pty) Ltd* and *FirstRand Bank v Lodhi 5 Properties Investment*.

- (i) it appears 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 (i.e. commercially insolvent); or
- (ii) it appears to be reasonably likely that the company will become insolvent within the immediately ensuing six months (i.e. factually insolvent).

This is a forward looking test, to project the solvency or expected insolvency of the company in six months' time and give directors and affected persons time to take action before the financial position of the company is dire. In early 2023, before Khusela was placed into business rescue, Khusela was failing to pay its debt obligations and overhead costs and Khusela's and the Khusela board of directors were of the view that (i) it was reasonably unlikely that Khusela would be able to pay its debts as they became due in the ordinary course and (ii) at that point in time, its liabilities exceeded its assets. Khusela was insolvent when it was placed into business rescue and was not financially distressed as defined in section 128(1)(f) of the Companies Act.

However, financial distress is not the only requirement for placing a company in business rescue. In terms of section 131(1) of the Companies Act, an affected person may apply to a court at any time for an order placing a company under supervision and business rescue, which was the case with Khusela. Section 131(4)(a) of the Companies Act provides that a court may grant such an order if it is satisfied that (i) the company is financially distressed; (ii) the company has failed to pay over any amount in terms of an obligation under or in terms of a public regulation, or contract, with respect to employment related matters; or (iii) it is otherwise just and equitable to do so for financial reasons, and there is a reasonable prospect for rescuing the company. Section 131(4)(a)(ii) and (iii) provide alternative grounds for financial distress, which a court can rely on in considering whether to grant an order placing a company in business rescue.

The courts have confirmed these alternative grounds. In *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd* (2013 (4) SA 539 (SCA)), the court held that a commercially insolvent company would still meet the test for financial distress and the determination of whether business rescue or liquidation was the appropriate step for the company would depend on the circumstances of the case. In *Tyre Corporation Cape Town (Pty) Ltd v GT Logistics (Pty) Ltd (Esterhuizen Intervening)* (2017 (3) SA 74 (WCC)), the court held that if it was incorrect that an insolvent company can also be classified as financially distressed and that test fail as a result, a court could rely on the test of whether it would be just and equitable to place a company in business rescue for financial reasons.

Therefore, even though Khusela was insolvent, and not financially distressed as defined in section 128(1)(f) of the Companies Act, it was not too late for the court to grant the business rescue order as it was able to rely on section 131(4)(a)(ii) of the Companies Act (i.e. Khusela not paying employee salaries) to grant the order placing Khusela in business rescue. It is assumed that the court also determined that there was a reasonable prospect of rescuing the company.

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)

The application to place Khusela in business rescue was commenced in terms of section 131(1) of the Companies Act, i.e. by an application to court. In terms of section 131(6) of the Companies Act, if liquidation proceedings have already been commenced by or against the company at the time an application is made in terms of subsection (1), the application for business rescue would suspend the liquidation proceedings until (a) the court has adjudicated the application or (b) the business rescue proceedings end, if the court makes the order applied for.

The Companies Act is not clear on what "commenced" liquidation proceedings means and at what stage the liquidation proceedings should be at before they can be suspended by an application to court to place a company in business rescue. This has been considered in case law.

In *Van Staden v Angel Ozone Products (in liquidation) CC (2013 (4) SA 630 (GNP))* the court held that conversion from liquidation to business rescue could be done at any time, particularly where business rescue may be a better option for stakeholders and would result in a better balancing and protection of rights than a liquidation would, which instead attempts to maintain the ranking of stakeholders, without preferring one of the other. A conversion to business rescue should be considered where it would result in a better outcome for stakeholders.

In *Richter v Absa Bank Limited (2015 (5) SA 57 (SCA))*, the Supreme Court of Appeal held that liquidation proceedings can be converted to business rescue at any time, including after a final order of liquidation has been made. Section 136(4) of the Companies Act supports this view by providing that a liquidator will become a creditor of the company in business rescue after the conversion, in relation to any outstanding claims for remuneration and expenses by the liquidator against the company in business rescue. While this process may be open to abuse by parties attempting to delay or frustrate the liquidation of company, as the process is run through a court application, the court would have to determine whether the application for business rescue was *bona fide* and that business rescue would be the most appropriate approach for the company.

Section 132(1)(c) of the Companies Act also supports this view by providing that business rescue proceedings begin when a court makes an order placing a company under supervision during the course of liquidation proceedings. The court in *Van der Merwe and Others v Zonnekus Mansion (Pty) Limited (in liquidation) and Another (Commissioner for the South African Revenue Service and Another as Intervening Parties) ([2017] JOL 39477 (WCC))* held that the Supreme Court of Appeal's decision in the *Richter* case was supported by section 132(1)(c).

Commented [M27]: 3 marks out of 5.
Needed to discuss relevant case law ie. ABSA Bank Limited v Summer Lodge, Standard Bank of South Africa Limited v Gas2Liquids (Pty) Ltd and Standard Bank of South Africa v A-Team Trading CC.

The courts have also considered the effect of the conversion of the liquidation to business rescue and held that the liquidator retains its powers as the liquidation is only suspended and not terminated (*GCC Engineering (Pty) Ltd and Others v Maroos and Others (2019 (2) SA 379 (SCA)*). Further, the Supreme Court of Appeal in *Lutchman NO v African Global Holdings (Pty) Ltd (2022 (4) SA 529 (SCA))* held that the applicant had to comply with section 131(2) of the Companies Act which require that an affected person applying to court for a company to be placed in business rescue (whether or not liquidation proceedings have commenced) serve a copy of the application on the CIPC and notify each affected person of the application in the prescribed manner. The court held that this was a key part of the section 131 process to be followed before section 131(6) could be relied on.

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.

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

Commented [M28]: 2 marks.

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)

A general notarial bond only confers a title interest and not a security interest on the holder thereof, unless and until (i) the general notarial bond is perfected in court with the consent of the business rescue practitioner (as this constitutes enforcement action), (ii) possession is taken of the assets, or (iii) the company is in liquidation, in which case the general notarial bond confers a preference over concurrent creditors. Crypto Bank does not have a security interest in the assets over which the general notarial bond is registered, therefore, Crypto Bank is not protected by section 134(3) of the Companies Act and its consent to the sale of the assets is not required. Ms van Zyl is entitled to sell the assets without Crypto Bank's consent.

Question 7.2

Commented [M29]: 4 marks.

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

In terms of section 134(1)(a) of the Companies Act, during the business rescue proceedings, a company may dispose or agree to dispose of property only (i) in the ordinary course of its business, (ii) in a *bona fide* transaction at arm's length for fair value approved in advance and in writing by the practitioner or (iii) in a transaction contemplated within and undertaken as part of an approved business rescue plan.

The sales are not in the ordinary course of business as Khusela's primary business is not the sale of assets and vehicles, so the requirements of section 134(1)(a)(i) are not met.

Sarah would have to prove that the sales are *bona fide*, at arm's length and for fair value, and not urgent fire sales to recover any money possible to fund the company's operations. The sales must be genuine market standard and value sales to meet the requirement of section 134(1)(a)(ii).

If the Sarah cannot meet the requirements of section 134(1)(a)(i) and (ii), she can as a last resort, include the plan for disposal of the assets in the business rescue plan to be voted on. This does not help the current requirement for the need for cash, but it is in compliance with the requirements of section 134(1)(a)(iii).

Question 8

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)**

In terms of section 135(2)(a) of the Companies Act, a during business rescue proceedings, a company in business rescue may obtain financing and such financing may be secured to the lender using an asset of the company to the extent that it is not otherwise encumbered.

Easy Access is requesting security over Khusela's existing material distribution agreements and proceeds. These assets are already encumbered in favour of Crypto Bank, and in accordance with section 135(2)(a) of the Companies Act cannot be provided as security in favour of post-commencement finance from Easy Access PCF.

Commented [M30]: 4.5 marks. Needed to state with reference to the facts that "security to the reasonable satisfaction of Crypto Bank could be provided by Ms van Zyl for the amount of the proceeds".

Ms van Zyl could look to rely on section 134(3) of the Companies Act. Section 134(3) of the Companies Act provides that if during a company's business rescue proceedings, if a company wishes to dispose of any property over which another person has any security or title interest, the company must (a) obtain the prior written consent of that person unless the proceeds of disposal of the asset would be sufficient to fully discharge the indebtedness owed to that person, and (b) promptly pay the proceeds to that person or security for the proceeds are provided, to the satisfaction of that person. Section 134(3) provides protection to secured creditors and does not allow the company in business rescue or the business rescue practitioner to alter or cancel their security interests in a company's assets.

"Disposal" is not defined in the Companies Act, however the ordinary meaning includes the transfer of ownership of an asset. Easy Access is requesting a sale of Khusela's existing material distribution agreements and proceeds. This security would be an out-and-out cession and constitute a disposal. Ms van Zyl would require the prior written consent of Crypto Bank to dispose of Khusela's existing material distribution agreements and proceeds in favour of Easy Access, and the amount received for such disposal (R1million) would have to be sufficient to fully discharge the amount Khusela owes to Crypto Bank (R100million) and be promptly paid to Crypto Bank. The amount offered by Easy Access is not sufficient to discharge the Crypto Bank debt, and unless a PCF is offered by Easy Access of at least R100million, Ms van Zyl cannot agree to Easy Access's requirements.

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.

Commented [M31]: 3 marks out of 7. Needed to state that the status and rights of employees in a business rescue process are entrenched in chapter 6 of the Companies Act, subject to the provisions of applicable labour laws. Needed to discuss the fact that the BRP may commence with a section 189 process, in the absence of a collective agreement that allows for a reduction in salaries and benefits. Needed to describe what the section 189 process entails. Needed to state that the BRP could issue voluntary severance offers to all affected employees, subject to any collective agreements.

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)

The business rescue practitioner did not follow the correct process. In terms of section 136(1)(a) of the Companies Act, during business rescue proceedings, employees continue to be employed on the same terms and conditions except to the extent that (i) changes occur in the ordinary course of attrition or (ii) employees and the company agree different terms and conditions in accordance with applicable labour laws. This section provides a general protection for employees' continued employment and the terms thereof.

Section 136(1)(b) further provides that any retrenchment of employees contemplated in the business rescue plan is subject to section 189 and 189A of the Labour Relations Act (66 of 1995) and other applicable employment related legislation. This section makes it clear that any contemplated retrenchment of employees must (i) be set out in the business rescue plan to be voted on and (ii) must be in accordance with applicable legislation. Ms van Zyl did comply with the Labour Relations Act, however, the retrenchment process was not set out in a business rescue plan, was done before the plan was published and was not voted on as part of the vote on the plan, and accordingly, she did not act in accordance with section 136(1)(b) of the Companies Act.

The requirement for the process in section 136(1)(b) was confirmed by the court in *South African Airways SOC Ltd and Others v National Union of Metalworkers of South Africa obo members and Others* ([2021] 6 BLLR 627 (LC)), where the business rescue practitioners attempted to retrench employees before a business rescue plan was published. The court held that section 136(1)(b) is clear on the requirement for retrenchments to be dealt with in the business rescue plan, and that such requirement was aligned with the right of access to information under the Companies Act. The Labour Court hearing the matter held the same.

Ms van Zyl must set out the retrenchment plan in the business rescue plan and once the plan is adopted, then undertake the section 189 and 189A processes (including the consultative process) to retrench employees in the manner set out in the approved plan. While this may not be practical given the cost saving achieved by Ms van Zyl or an efficient use of the often long time between the time of commencement of business rescue and publication of the plan, the legislation and case law are currently clear on the position that

retrenchment processes cannot be undertaken until set out in an adopted business rescue plan.

Question 10

Commented [M32]: 3 marks.

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

Employees are affected persons as defined in section 128(1)(a) of the Companies Act. They are entitled to apply to court at any time for an order placing a company in business rescue, in accordance with section 131 of the Companies Act.

Section 135(1) and 144(2) provides employees the right to receive from the company any remuneration, reimbursement for expenses and any other amount due, payable and unpaid post and pre business rescue, respectively, in the preference as post commencement finance and preferred unsecured creditors, respectively.

Section 136(1) gives employees the right to preserve their employment and terms thereof until otherwise provided for in an approved business rescue plan.

In terms of section 144(3) of the Companies Act, employees of a company in business rescue have the right to (i) receive notice of each court proceeding, decision, meeting or other relevant event concerning the business rescue proceedings; (ii) participate in court proceedings related to the business rescue proceedings; (iii) form a committee of employees' representatives; (iv) be consulted by the practitioner in development of the business rescue plan, review and make submissions in relation to its consideration; (v) be present at and make submissions at the section 151 meeting at which the proposed business rescue plan will be considered; (vi) where an employee is a creditor, vote on the proposed business rescue plan; and (vii) if a proposed business rescue plan is rejected, in its capacity as an affected person, propose the development of an alternative plan or present an offer to acquire the voting interests of one or more affected persons.

Question 11

Commented [M33]: 1 mark. Needed to discuss the fact that directors are relieved of certain of their fiduciary duties to the extent that they act according to the BRP's instructions and subject to his/her instructions. Needed to apply legal principles to the facts.

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)**

The CEO, CFO and board of directors must continue to fulfil their roles as directors and management of the company, under the direction of the business rescue practitioner and in compliance with section 76 of the Companies Act. The directors cannot undertake any acts for or on behalf of the company without the authority of the business rescue practitioner. Such acts would be void.

In terms of section 142 of the Companies Act, the directors of a company have a duty to co-operate and comply with the directions of the business rescue practitioner and assist the practitioner in its role. This includes a duty to deliver all books and records relating to the company's affairs to the practitioner which are in the director's possession or inform the practitioner of their whereabouts. Further, section 142(3) requires that, within 5 business days of commencement of business rescue proceedings or such longer period as permitted by the practitioner, the board must provide the practitioner with a statement of affairs of the company, containing at a minimum, (i) material transactions within the 12 months before business rescue commenced; (ii) any court, arbitration or administrative proceedings including pending enforcement proceedings involving the company; (iii) assets and liabilities of the company, its income and disbursements within the immediately preceding 12 months; (iv) the number of employees and any collective agreements or agreements relating to employees' rights; (v) any debtors and their obligations to the company; and (vi) any creditors and their rights or claims against the company.

Question 12

Commented [M34]: 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)

Section 150(1) requires that the practitioner prepare the business rescue plan for consideration and possible adoption at a meeting called for that purpose, after consulting with creditors, other affected persons and the management of the company.

The meaning of "consulting" was considered in the case *Hlumisa Investments Goldings (RF Limited and Another) v Van der Merwe NO and Others* ([2016] JOL 34326 (GP)), where the court distinguished between "informing" and "consulting". The court quoted the findings in *Scalabrini Center Cape Town and Others v Minister of Home Affairs and Others* (2013 (3) SA 531 (WCC)) where it was held that consulting was (i) substantively, a "genuine invitation to give advice and a genuine receipt of that advice". Further, it was more than a formality and not to be done once the decision maker had reached a decision, and required substantive consultation in an appropriate manner as determined by the decision-maker. Relying on the *Scalabrini* interpretation of "consulting", the court in *Hlumisa* informing creditors and shareholders of the progress of business rescue by way of SENS announcements and at meetings of shareholders did not constitute consulting.

Consultation under the Companies Act requires a meaningful engagement and sharing of ideas between the business rescue practitioner and affected persons such that the business rescue plan prepared by the practitioner reflects a due consideration and recognition of the views, sentiments, concerns, advice and guidance expressed by the affected persons.

Question 13

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)**

In terms of section 143(2) of the Companies Act, a business rescue practitioner may propose an agreement with the company for further remuneration, in addition to the tariff based fee, which would be calculated on a contingency basis and based on adoption of the plan, or within a time period or inclusion of a specific matter in the plan, or based on the achievement of a certain result or combination of results related to the business rescue proceedings. This is typically referred to as a success fee, payable over and above the tariff fee.

In terms of section 143(3), such an agreement must be approved by the holders of the majority of creditors' voting interests and the holders of the majority of the voting rights attached to shares of the company which entitle the shareholder to a portion of residual value of the company on winding-up, both of which were present and voting at a meeting called for the purpose of considering the proposed agreement.

It may also be possible to have the agreement or terms of the success fee included in the proposed business rescue plan to be voted on for approval in terms of section 152(2) of the Companies Act.

Commented [M35]: 2 marks. Great answer.

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)**

Regulations 26(2) and 127(2)(b) of the Companies Regulations 2011 set out the classifications of a company based on a public interest score determined with reference to the number of employees, the amount of liabilities, the turnover during the financial year and the number of individuals who have a beneficial interest in the company's issued securities. One point is allocated for every employee, R1million or part thereof and individual, as applicable to each category.

Regulation 127(2)(b) provides that a small company has a score below 100 points, a medium company has a score between 100 and 500 points and a large company has a score above 500 points.

Khusela had 2000 employees at the end of 2021, that equates to 2000 points. That alone would make Khusela a large company. Looking at the debt of R75million, that would give

Commented [M36]: 3 marks.

Khusela 75 points, based on 1 point per R1million or portion thereof. The annual turnover and number of shareholders is not stated in the case study.

As Khusela is a large company, in terms of Regulation 128 of the Companies Regulations 2011, Ms van Zyl could charge R2 000 per hour, limited to a maximum of R25 000 per day (including VAT).

Question 15

Commented [M37]: 3 marks.

The case study includes the following statements:

"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)**

Section 141 of the Companies Act requires that "as soon as practicable after being appointed", a business rescue practitioner must investigate the affairs of the company, its business, property and financial situation and thereafter consider whether there is any reasonable prospect of rescuing the company. A time frame has not explicitly been stated for "as soon practicable after being appointed" but a practitioner is required to make an assessment of the prospects of the company being rescued (i) before accepting appointment as a practitioner; (ii) before the first meeting of creditors in terms of section 147 of the Companies Act, as the practitioner must (in terms of section 147(1)(a)(i)) inform the meeting whether there is a reasonable prospect of rescuing the company; and (iii) continuously during the business rescue proceedings (section 141(2)).

This means that at least an initial assessment of whether Khusela was capable of being rescued must have been made before Sarah's appointment was ratified at the first meeting of creditors. Sarah would be required to make a statement of whether Khusela could be rescued at the first meeting of creditors and she could not reasonably do so if her investigations into the business and affairs of Khusela only started after the first meeting of creditors.

Sarah breached her duties as a practitioner and an affected person would apply to court for her removal in terms of section 139(2)(a) and (b) of the Companies Act on the grounds

that she failed to perform the duties of a business rescue practitioner and failed to exercise the proper degree of care in the performance of the functions of a practitioner.

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)**

In terms of section 132(3) of the Companies Act, if the business rescue proceedings have not ended within 3 months of the start of the proceedings, or such longer period of time provided for by a court on application by the practitioner, the business rescue practitioner must:

- (i) prepare a report on the progress of the proceedings and provide monthly updates to the report until the end of the business rescue proceedings (section 132(3)(a)); and
- (ii) deliver the report and each update in the prescribed manner to each affected person and the court if proceedings commenced by court order, or to the CIPC in other instances (section 132(3)(b)(i) and (ii)).

Practically, business rescue proceedings do not end within 3 months of commencement. This is often due to the time it takes for the practitioner to investigate the affairs of the company, engage with affected persons and formulate a business rescue plan in consultation with affected persons, and depends on the complexity of the rescue. Accordingly, business rescue practitioners often have to comply with section 132(3) of the Companies Act.

Question 17

Mr Sandiso Siwisa, who is the cousin of the 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)**

Section 128(1)(g) of the Companies Act defines an "independent creditor" as a person who (i) is a creditor of the company, including an employee of the company who is a creditor in terms of section 144(2); and (ii) is not related to the company, a director or the practitioner (noting that an employee of the company is not related to the company solely by being a member of a trade union that holds securities in the company).

Commented [M38]: 2 marks. Needed to mention section 150(5) - securing an extension of time to publish the BR plan.

Commented [M39]: 2 marks. Needed to discuss the definition of "related" as set out in the Companies Act. Needed to discuss Mr Siwisa's relationship with Mrs Phillips and how their combined shareholding gives them control over Khusela. See section 2(1)(a) to (c) of the Companies Act.

In terms of section 2(a) of the Companies Act, an individual is related to another individual if they (i) are married or live together in a relationship similar to a marriage; or (ii) are separated by no more than two degrees of natural or adopted consanguinity or affinity.

Mr Siwisa is related to Mrs Lungi Phillips by virtue of sharing a parent. However, section 128(1)(g) of the Companies Act does not refer to shareholders in determining whether a creditor is independent.

Mr Siwisa passes the test at section 128(1)(g)(i) of being a creditor of Khusela by virtue of the R500,000 loan. However, Mr Siwisa fails the test at section 128(1)(g)(ii) because he is related to a director of Khusela by virtue of being a cousin of a director of Khusela and thus falling within the two degrees of natural or adopted consanguinity, in terms of section 2(a) of the Companies Act. Therefore, Mr Siwisa is not an independent creditor.

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

A business rescue practitioner is not permitted to unilaterally amend a business rescue plan once it has been approved. Ms van Zyl's actions are not valid.

In *Booyesen v Jonkheer Boerewynmavery (Pty) Ltd (in business rescue) and Another* ([2014] 1 All SA 862 (WCC) (10999/16) [2016] ZAWCHC 192 (15 December 2016)), the court held that a practitioner could not unilaterally amend an approved business rescue plan. To do so would go against the procedures set out in the Companies Act and the practitioner did have the powers to impose a plan on creditors which they did not consider and vote on in accordance with section 152 of the Companies Act.

An amendment to a business rescue plan can be implemented in a number of ways. Firstly, amendments to a plan can be implemented at the section 151 meeting at which the plan is to be considered as permitted by section 152(1)(d)(i). These would typically be minor or non-material amendments.

Secondly, where a plan has been rejected at the section 151 meeting, section 153(1)(a)(i) of the Companies Act provides that a practitioner may call a vote for it to prepare and publish a revised plan. Lastly, where the practitioner does not do so, section 152(1)(b)(i)(aa) provides that an affected person may call for a vote to approve the practitioner preparing and publishing a revised plan. If the proposal for the practitioner to prepare and publish a revised plan is approved following one of the votes referenced above, the practitioner must convene the meeting and prepare and publish a new or revised plan within 10 business

Commented [M40]: 4 marks. Need to distinguish between the process of amending a BR plan prior to its adoption and after its adoption.

days and the process for consideration, voting on and revising the plan in terms of the Companies Act will apply to the revised or amended plan.

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)

I would expect to see the following key items in the financial projections:

(i) a projected balance sheet of the company, a statement of income and expenses and a cash flow statement (though not required by the Companies Act) for the following three years, on the basis that the proposed business rescue plan is adopted (section 150(2)(c)(iv)). These would assist Opera Sound Engineering in assessing the potential solvency, profitability and liquidity (respectively) of the company if the proposed business rescue plan was approved and implemented. This will also give some indication whether the company will no longer be financially distressed (as defined in section 128(1)(f) of the Companies Act);

(ii) a notice of any material assumptions on which the projections are based and at the business rescue practitioner's discretion, alternative projections based on varying assumptions and contingencies (section 150(3)(a) and (b)). These would give Opera Sound Engineering some context as to how the projections were developed (e.g. on the assumption that employee costs could be reduced and the cost of that process); and

(iii) a certificate by the business rescue practitioner stating that the actual information provided appears to be accurate, complete and up-to-date and that the projections provided are estimates made in good faith based on the factual information and assumptions included in the statement (section 150(4)). This would provide comfort that the business rescue practitioner has exercised care and diligence in preparing the financial projections.

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)

I would advise Ms Sarah van Zyl to include a cash flow statement for a three year period, with monthly projections in the first year and annual over the remaining two years, in her business rescue plan. While not required under section 150(2)(c) of the Companies Act (which only requires a balance sheet and statement of income and expenses for the ensuing three years) the benefit of a cash flow statement is that creditors who are voting on approval

Commented [M41]: 0 marks. The question required you to list items that you would expect to see as part of the financial projections of the BR plan and not what must be included in the BR plan.

Commented [M42]: 2 marks.

or rejection of the plan will be able to see the expected movement (inflows and outflows) of cash in the company and thus the liquidity of the company if the business rescue plan is implemented. Cash is an important factor in the success of a company. The cashflow statement will give affected persons voting on the plan, an indication of the likelihood of the successful rescue of the company and whether the company is likely to be able to operate on a solvent basis on implementation of the business rescue plan.

Question 21

Commented [M43]: 3 marks.

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

Business rescue provides better protection for employees than liquidation does.

Business rescue protects the rights of employees, whereas liquidation has limited protections.

In terms of section 136 of the Companies Act, employees of a company in business rescue continue to be employed on the same terms as conditions as prior to business rescue. In liquidation, employee contracts and their rights thereunder are suspended or terminated.

In business rescue, in respect of any remuneration, reimbursement for expenses or other amounts relating to employment which became due and payable to an employee before business rescue proceedings commenced, an employee will be a preferred unsecured creditor of the company in business rescue (section 144(2) of the Companies Act). Any of the aforementioned amounts which become due and payable but are unpaid during business rescue will be treated as post-commencement finance and have priority of ranking (section 135(1) and (3)(a) of the Companies Act). In liquidation, employees' claims which became due prior to business rescue would have a statutory preferent claim in terms of section 98A of the Insolvency Act. However, and employee claims during business rescue would have a concurrent claim recoverable from the proceeds of the sale of any unencumbered assets of the company.

Employees have a right to participate in business rescue in accordance with section 144(3) of the Companies Act. This includes a right to receive notice of and participate in meetings, court proceedings and decisions; a right to form a committee of employee representatives; a right to be consulted by the business rescue practitioner during development of the business rescue plan, to review the plan and address the meeting at which the plan is being considered; a right to be present at, and make a submission to, the meeting where a proposed business rescue plan will be voted on; and a right to propose the development of an alternative plan and acquire the voting interests of affected persons where a proposed business rescue plan is rejected. Liquidation proceedings do not provide employees the right to participate in the process. A liquidator will be winding down the company and will not require the participation of employees in the process.

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

TOTAL MARKS: [100]