PROGRAMME IN SOUTH AFRICAN BUSINESS RESCUE 2023

Commented [BB1]: TOTAL = 84/100 - 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

Commented [M2]: Total for Q1: 19 marks.

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.

Question 1.1

Commented [M3]: 1 mark

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?

(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

Commented [M4]: 1 mark

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?

(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]: 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]: 1 mark

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 appoint 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]: 1 mark

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 voted 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

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

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)**

[Answer

As a starting point, Section 133 (1) of Companies Act provides that no legal proceedings, including enforcement action, may be commenced or proceeded with against company in business rescue. This is inclusive of property in the lawful possession of the company unless you the writing consent of the business rescue practitioner or the court.

The aforesaid section includes existing legal proceedings as well as new legal proceedings.

In view of the aforesaid, the legal proceedings instituted by the creditors "to recover amounts owing to them" would be suspended or would not be able to be commenced with by virtue of Khusela being placed into business rescue. As such, in the absence of written consent from the business rescue practitioner or the leave of the court, such creditors would not be able to continue or institute legal proceedings. For example, Opera Sound Engineering's money judgment application would be suspended subject to the exceptions in Section 133(1). The moratorium would last for the period of business rescue.

However the moratorium described above would not extend to juristic acts such as cancelation of agreements or sending letters of demand.]

Question 3

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

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

[Answer

In accordance with Section 152(2) of the Companies Act of 2008, a business rescue plan must obtain 75% of the creditors' voting interest that were voted on and at least 50% of the independent creditors' voting interests that were voted. This would constitute final adoption of the business rescue plan only if the plan would not have the effect of altering the rights of the shareholders of the company in business rescue.

To the extent that the business rescue plan does alter the rights of shareholders of the company in business rescue, then in addition to aforesaid requirement of Section 152(2), Section 152(3) provides that the business rescue practitioner must also have a separate meeting with the shareholders to vote on the plan after the creditors have voted on it. A simple majority vote of these shareholders is sufficient. If the majority vote of these shareholders is obtained, the proposed plan would then be adopted.]

Question 4

Commented [M25]: 3 out of 3 marks.

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)**

[Answer

In terms of Section 152(4) of Companies Act,2008, a business rescue plan, once adopted, becomes binding on the company in business rescue, all its creditors (both secured and unsecured) and shareholders whether or not they were present at meeting and voted for or against the plan or whether as a creditor they had proved their claims against the company.

The aforesaid position is often referred to as the cram-down principle, which principle is essential in a business rescue plan as it prevents certain creditors from holding out (with respect to their vote) in an attempt to get better treatment (over the other creditors). The principle further prevents the business rescue process being held up by such creditors. The court in African Banking Corporation of Botswana Ltd v Kariba Furniture Manufacturers (Pty) Ltd and Others held the aforesaid position.

In addition to the above, the court in DH Brothers Industries (Pty) Ltd v Gribnitz NO and Others stated that where the business rescue plan is "crammed down", the voting interests of the creditors who voted no to the plan or who were absent should not exceed more than 25% of the voting interests.

With regards to the present set of facts, Opera Sound Engineering has been said to be only a "minority" creditor. Thus, when contrasted with the extent of Khusela's total creditors (from the facts), it can be inferred that Opera Sound Engineering (together with any other dissenting creditors) would not have exceed the 25% voting interest threshold set in the DH Brothers case.

In view of the aforesaid, the approved business rescue plan would be binding on Opera Sound Engineering.]

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)**

[Answer

The inability of a company to pay its debts as and when they fall due for payment would rendered that company by definition "commercially insolvent". From the fact set presented, it is common cause that Khusela was not able to pay its debts as and when they fell due for payment prior to (and at the time) of being placed in business recue. Thus, Khusela was commercially insolvent at the time of the application to place it in business rescue.

Notwithstanding the above, if regard is had to the definition of financial distress in Section 128(1)(f) of the Companies Act, 2008 it will be noted that "financial distress" comprises two elements.

To this end, Section 128(1)(f)(i) provides that "*it appears to be reasonably unlikely that the company will be able to pay all of its debts as they fall due and payable within the immediately ensuing six months*".

And Section 128(1)(f)(ii) provides that "*It appears to be reasonably likely that the company will become insolvent within the immediately ensuing six months*".

From an analysis of the wording contained in Section 128(1)(f), it can be said that financial distress envisages a forward looking test that essentially requires an assessment/answer as to whether (i) the company will be commercially insolvent or (ii) factually insolvent in the ensuing 6 months. The rational for the aforesaid position is to allow a board to pre-empt the financial troubles of a company.

If regard is had purely to the wording of Section 128(f), it could be argued that Khusela ought to have been considered too late for a business rescue order to have been issued as it was already commercially insolvent at the time when the order was granted whilst section 128(f) seemingly envisaged future insolvency.

Commented [M26]: 2 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*. Needed to discuss the 'just and equitable' ground for a BR order. See *Tyre Corporation Cape Town v GT Logistics*.

The Supreme Court of Appeal, however, in Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd held that even if a company is already commercially insolvent, it would still meet the financial distress requirement of Section 128(1)(f) and could thereby be placed in business rescue.

In view of the case law on the topic, Khusela business rescue order cannot be said to be too late as present commercially insolvency would still satisfy the requirements of Section 128(1)(f) of the Companies Act, 2008.]

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)**

[Answer

In order to deal with the above issue, one must consider Section 131 (6) of the Companies Act 2008 as well as the case law on the topic.

In this regard, Section 131(6) provides that if liquidation proceedings have already commenced against a company at the time of a court application to commence business rescue (a) those liquidation proceedings will be suspended until the court has adjudicated upon the business rescue application or (b) the business rescue proceedings end, if the court makes the order applied for.

Further guidance on this issue can be found in the case of FirstRand Bank Ltd v Imperial Crown Trading 143 (Pty) Ltd which held that "commenced" means the same as commencement date in terms of the Companies Act of 1973 i.e the date the application was presented to the court for issuing.

The court in Tjeka Training Matters v KPPM Construction (Pty) Ltd & Others held that were a liquidation application had been issued and filed in court by a creditor **but** not had not yet been served on the company, it cannot be regarded that liquidation proceedings have been initiated if the company does not even know that liquidation proceedings have commenced. This position was favoured in the SCA in Lutchman v African Global Holdings. Thus, the mere issuing on a liquidation application is not sufficient to regard liquidation proceedings as having commenced but rather only when the application is served on the company, at least within the context of Section 131(6).

The aforesaid considerations would have great timing implications should the board of director of Khusela have wanted to adopt a resolution in terms of Section 129(1) of the Companies Act to commence voluntary business rescue. Thus, if the liquidation application envisaged above had been issued and served on Khusela prior to such a resolution having

Commented [M27]: 2 marks out of 5. Needed to discuss relevant principles set out in 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.

been adopted, the board would have then been precluded from adopting a Section 129(1) resolution.

Given that the present business rescue was however brought by way of a court application, the aforesaid considerations pertaining to timing would not have had any effect or impact to the institution of the business rescue application.

Accordingly, in view of the fact the question merely says the liquidation was filed at court without having been served as yet, it cannot be said be said that World of Music's liquidation proceedings against Khusela had commenced. In any event, even if the World of Music's liquidation application had been served on Khusela and liquidation proceedings had commenced, same would have been suspended in terms of Section 131(6) subject to Section 131(6)(a) & (b).

World of Music could however simply have opposed the business rescue application. Subject to them satisfy the relevant requirements, a court would be empowered in terms of Section 131(4)(b) to grant a liquidation order.]

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

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)**

[Answer

I would advise Sarah that the threatened urgent application by Crypto Bank would be ill-advised on their part due to the misunderstanding that Crypto Bank has pertaining to the

Commented [M28]: 2 marks. Excellent answer.

security that a general notarial bond ("GNB") provides within the current set of facts. I say so for *inter alia* the following reasons:

1. From the fact set and question, it merely says that Crypto Bank registered a GNB. The facts do not indicate that Crypto Bank had either perfected their GNB (by application in High Court and thereafter acquired possession of the assets) prior to business rescue or during business rescue (with the business rescue practitioners consent or the leave of the court).

2. A holder of a GNB and the preference afforded to such holder (being Crypto Bank) is only exercised/ trigger in the event of the insolvency of the company. As such, in the absence of the GNB having been perfected, no such preference exists.

3. In view of the aforesaid, it is submitted that Crypto Bank's GNB confers neither security or title interest over the movable assets of Khusela and thus such assets do not constitute security for Crypto Bank over Khusela's property in view that no perfection seems to have taken place. As such, Sarah would not require Crypto Bank's consent in terms of Section 134(3)(a) to sell such assets nor would the proceeds from such sale need to discharge Crypto Bank's indebtedness in full.

In view of the above considerations Sarah would have strong prospects of success in opposing the threated application.]

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)**

[Answer

In order for Sarah to ensure compliance with the statutory requirements for such sale/disposal of the assets, compliance with Section 134(1)(a) of the Companies Act, 2008 is required. In this regard, the requirements for the sale/disposal of the assets would be that the disposal of the assets by Khusela would have to be:

1. Either in the ordinary course of business, or

2. In a bona fide transaction at arm's length, for fair value, approved in advance and in writing by the business rescue practitioner, or

3. In a transaction contemplated within and undertaken as part of the business rescue plan that has been approved.

Given the nature of Khusela's business it might be difficult to argue that the disposal of equipment would be in the ordinary course of its business.

However, given that Sarah requires funds urgently, it would be sensible for Sarah to ensure that the disposal is a bona fide transaction at arm's length, for fair value, approved in advance and in writing by herself in order to comply with Section 134(1)(a)(ii) of the Companies Act, 2008. Sarah would be able to satisfy the aforesaid requirement easily as she is selling redundant equipment and vehicles. These assets can be regarded as non-core assets and can be used to raise funds and reduce operational expenses.

As a further consideration to the above, certain academic commentary suggests that in terms of S134(1)(a) it is still the company represented by its board of directors who is responsible for concluding the transaction to sell/dispose of the property. As such, Sarah could potentially delegate the conclusion of the aforesaid sale transaction to the board who could, with Sarah's oversight, conclude the transaction as contemplated above.]

Question 8

Commented [M30]: 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)**

[**Answer**

As a starting point, the cession of the rights of Khusela's material distribution agreements to Crypto Bank would mean that Crypto Bank holds a security interest in the property of Khusela as envisaged in terms of Section 134(3) of the Companies Act, 71 of 2008 . The court in *Van den Heever vs Van Tonder* confirmed the position that a holder of a cession of rights has a "security interest" as contemplated in Section 134 and is thus a secured creditor.

In view of the provisions of Section 134(3) of the 2008 Act, as well as the case law on the topic, Sarah, as business rescue practitioner, is precluded from disposing of and/or utilising such encumbered property (in this case the rights to the material distribution agreement) without obtaining the consent of the secured creditor (Crypto Bank) unless the business rescue practitioner is first able to discharge such creditor's indebtedness. Alternatively the business rescue practitioner would have to furnish security for the amount of these proceeds to the reasonable satisfaction of Crypto Bank.

As such, the only way in which Sarah could potentially utilise the rights to material distribution agreement as security would be if Crypto Bank consented to same or if the proceeds from the sale of the rights to the material distribution agreement could settle Crypto Bank in full.

From the fact set, neither of the above options seem plausible. Considering the large extent of Khusela's indebtedness to Crypto Bank it is hard to imagine that they would simply consent to relinquish their security in this manner. Furthermore, it would not seem likely that the sale of the rights to the material distribution agreement could raise sufficient funds to settle Crypto Bank in full as there claim seems to be in excess of R100,000,000.

As such, Sarah would not be able to sell the rights to the material distribution agreement to Easy Access in the absence of satisfying the above provisions. As an alternative solution, Sarah could assess what unencumbered assets exist and these assets could be used as security for Easy Access in terms of Section 135(2)(a). Considering that only R1,000,000.00 of funding is being provided by Easy Access, this seems the most appropriate option.]

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

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.

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)**

[Answer

As a point of departure, it is important to note that retrenchments pursuant to a Section 189 process in terms of Labour Relations Act may be one of the most critical ways in which a business rescue practitioner may reduce the overheads of a financially distressed company in business rescue. From the facts, Khusela had 2000 employees in 2021 which increased from 500 in 2015. The consequence of a such a drastic increase of the numbers of employees was that Khuslea's employment costs quadrupled. As such, the need to reduce the work force (and the costs associated therewith) would evidently be a key aspect of Khusela's business rescue.

The rights of employees with regards to their employment contracts can be found in Section 136 of the Companies Act 2008. Section 136(1)(a) provides that during business rescue proceedings an employee will remain employed of the same terms as conditions subject to the exceptions of Section 136(1)(a)(i) and (ii). Furthermore, Section 136(1)(b) of the Companies Act, 2008 provides that any retrenchment of employees contemplated in the business rescue plan is subject to Section 189 and 189(A) of the Labour Relations Act.

Guidance on the above sections as well as the conduct of Sarah can be found in the case of SA Airways (SOC) Ltd (In Business Rescue) and Others v National Union of Metalworkers of SA. The court held that the if a business rescue practitioner envisages a change of the employees working circumstances and contract terms, then section 189 of the Labour Relations Act contemplates a consultative process. However, the court further held In this case, that section 136(1)(b) of the Companies Act requires that retrenchments

contemplated during business rescue must be dealt with in the business rescue plan and that a business rescue practitioner is not empowered to retrench employees in the absence of an adopted business rescue plan.

If view of the above, it is apparent that Sarah's conduct in retrenching more than 1500 employees of Khusela did not comply with the legislative requirements as well as the case law on the topic as Sarah embarked on the Section 189 process upon her immediate appointment and subsequently retrenched 1500 employees of Khusela before the business rescue plan was published and adopted. Sarah's conduct was patently irregular and the correct procedure was evidently not followed.

Sarah was required to have first dealt with the contemplated retrenchments in the business rescue plan and then only once the business rescue plan was published and adopted, should Sarah have then embarked on the Section 189 process and made the subsequent retrenchments. In view of her failure to do so, it can be said that it was procedurally unfair to retrench the 1500 employees before a business rescue plan contemplating such retrenchments was published and adopted notwithstanding that the fact that the employees were paid their severance packages. The retrenched employees would in my view still have recourse against Khusela (and by virtue Sarah) on the basis that retrenchments were procedurally unfair.

As an aside, the consequences of the SA Airways (SOC) Ltd (In Business Rescue) and Others v National Union of Metalworkers of SA judgment now means that in circumstances where a business rescue plan may take 6 months (or in this case a year) to publish and adopt, a business recue practitioner would not be able to embark on the Section 189 process or retrenchment process as contemplated in a business rescue plan until the plan is adopted. This means that the salaries incurred during this period still remain payable when they could have potentially been drastically if the Section 189 process and retrenchments could have been implemented immediately. This may make many business rescues such as those with work forces of the size of Khusela unworkable.]

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)**

[Answer

It is clear from Chapter 6 of the Companies Act, 2008 that the legislature has tried to elevate and safeguard the rights of employees during business rescue. In this regard, employees are affected persons in terms of Section 128 (1)(a)(iii) and are thus afforded the same rights in general that affected persons have. As such, an employee would have the right to be notified of and participate in (and object to) the business rescue proceedings of Khusela including court proceedings. This would also mean that employees have the rights to bring an application for business rescue as an affected person.

Furthermore, in terms of Section 144(3)(d) employees have the right to participate in the development of the proposed business rescue plan and to consult with the business rescue practitioner in this regard.

To the extent that the employee is a creditor of the company, such employees also have the right to vote with creditors on any motion to approve the proposed business rescue plan of Khusela and have the right to be notified of such meeting.]

Question 11

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)**

[Answer

As a starting point, upon company being placed into business rescue, Sarah, as business rescue practitioner, would assume full management control of the Khusela in substitution for its board and pre-existing management. Sarah may then delegate any power or function to a director or pre-existing management of the company.

As such, the Chief Executive Officer and the Chief Financial Officer, whilst not board members, would still nevertheless be required to assist Sarah as they would both have intimate knowledge of Khusela's financial affairs. Thus their input in the preparation and implementation of the business rescue plan and throughout the business rescue process will be vital. Furthermore, and to the extent that Sarah requires, certain tasks and powers could be delegated back to Chief Executive Officer and Chief Financial Officer as they may have the more suited skillset to deal with particular issues.

With regard to the board of directors of Khusela, these directors remain directors of the company and as such must continue to exercise their functions as directors, subject to the authority of the business rescue practitioner. The board would thereby have to attend to the reasonable requests of the business rescue practitioner. Furthermore, the board of directors of Khulesa would likewise have intimate knowledge and the dealings and affairs of the company and will be able to offer input when the business rescue plan is being prepared. The board of directors may also have contacts with key suppliers etc within the industry and may thus be able to assist the business rescue practitioner in this regard. As

Commented [M33]: 2 marks. 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.

such, the business rescue can delegate certain powers back to the board of directors of Khusela such as the power to sign certain contracts.

The board of directors would have a further role during business rescue as they would be required to provide information about the company's affairs, and would have deliver to the business rescue practitioner all of the company's books and records that may be in their possession as well as a statement of affairs.]

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)**

[Answer

In terms of Section 150(1) of the Companies Act 2008, a business rescue practitioner has a statutory obligation to consult with creditors, other affected persons and the management of the company before preparing a business rescue plan for consideration and possible adoption.

Guidance pertaining to what "consultation" as required by Section 150(1) would entail can be found in the case of Hlumisa Investments Holdings (RF Limited and Another) v Van der Merwe NO and Others. The facts, briefly summarized pertained to minority shareholders who brought an urgent interdict to prevent a meeting from going ahead to vote on a transaction in the business rescue plan. The interdict was based on fact that the minority shareholders were not consulted with. As the company in rescue was a public company it had many shareholders and the business rescue practitioner purported to consult by sending notices to shareholders by way a Stock Exchange News Service.

The court in Hlumisa found that there was a clear distinction between merely informing and consulting. To this end, the court in Hlumisa cited the case of Scalabrini Center Cape Town and Others v Minister of Home Affairs and Others which case in turn held that consultation entails a genuine invitation to give advice and a genuine receipt of that advice and should thus not be treated as a mere formality. As matter of logic consultation could not take place after the decision had already been reached.

In view of the position in Scalabrini, the court in Hlumisa found that merely that notifying creditors and shareholders by way of Stock Exchange New Service announcements, having meetings with individual shareholders or only a body of preferent shareholders, did not amount to "consultation" as required in terms of Section 150(1).

In view of case law on the topic "consultation" within the context of business rescue and particularly Section 150(1) should thus be meaningful in that a business rescue practitioner

should actively engage with creditors, other affected persons and the management of the company to identify concerns and to receive suggestions and solutions pertaining to issues surrounding the rescue. Consultation within this context and in view of the case law would then require the business rescue practitioner to consider and incorporate these considerations and suggestions when developing the business rescue plan. Lastly, it is imperative that consultation as envisaged in this paragraph be done with all creditors, other affected person and management of the company and not just specific classes and/or groups so as to exclude others.

Sarah must ensure that she consults in the above manner to avoid any affected persons potentially interdict any meetings on the basis that they were not consulted with.]

Question 13

Commented [M35]: 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)**

[Answer]

Sarah would indeed be able to propose an agreement for further remuneration in addition to that provided for in a tariff. Such an agreement is often referred to as a contingency fee/success fee agreement.

Section 143(2) of the Companies Act 2008 makes provision for this and provides that such additional fee must be negotiated between the business rescue practitioner and the company.

In terms of Section 143(3) of the Companies Act 2008, such contingency/success fee agreement becomes binding and enforceable by the business rescue practitioner against the company if it is approved by the majority creditors' voting interests and those shareholders entitled to receive a residual value of the company on winding-up.

Sarah, as business rescue practitioner, would have to convene a meeting specifically to approve this success fee by way of the vote contemplated above.]

Question 14

Commented [M36]: 3 marks.

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)**

[**Answer**

In order to determine the tariff that Sarah can charge for her service as business rescue practitioner, it must first be established if Khusela is a small, medium or large company. In order to determine if Khusela is a small, medium or large company, its public interest ("PI") score must be calculated and in this regard, regulation 127(2)(a) to the Companies Act 2008 provides guidance.

In view thereof, a company is:

1. Small if it has a PI score of less than 100;
2. Medium if it has a PI score of between 100 - 500; and
3. Large if it has a PI score of 500 or more.

A company's PI score is calculated as follows: 1 point for every shareholder, 1 for every employee, 1 point for every R1 million of turnover and 1 point for every R1 million of creditors.

In view of the fact that Khusela had 2000 employees at commencement of business rescue, this fact alone would give Khusela a PI score of at least 2000 without even considering the other requirements. As such, Khusela is evidently a large company based on its PI score. Thus, Sarah, as business rescue practitioner of Khusela, would be able to charge R2,000 per hour (up to a maximum of R25,000 per day inclusive of VAT) for her services.]

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)**

[Answer

In terms of Section 147(1)(a)(i), Sarah as business rescue practitioner of Khusela, was required to inform the creditors of Khusela as to whether she believed that there was a reasonable prospect of rescuing Khusela at the first meeting of creditors.

In view of the facts stating that Sarah first investigated the affairs of Khusela (after her appointment was ratified at the first meeting of creditors) and then only expressed her view that a reasonable prospect existed to rescue Khusela, it is apparent that she could not have expressed as such at the first meeting of creditors. As such, Sarah did not comply with the requirement of Section 147 (1)(a)(i) of the Companies Act 2008 in that she did not express her view on whether Khusela had a reasonable prospect of rescue at the first meeting.

A business rescue practitioner must express their view on as to whether there is a reasonable prospect of rescuing the company at the first meeting. This is, however, difficult as the first meeting happens within 10 days of a business rescue practitioner being appointed.

In view of the above, Sarah should have done the following differently: In terms of Section 141(1) of the Companies Act 2008, Sarah as business rescue practitioner had an obligation to commence with her investigations into the affairs of Khusela upon her appointment as business rescue practitioner. Thus, upon the grant of the court order placing Khusela under business rescue, Sarah should have at that stage begun to investigate the affairs of Khusela. She could have done so by considering the business rescue application and through holding discussions with the directors and affected persons of Khusela, such as its major creditors. At a minimum, this would have provided her with sufficient information pertaining to the background of the company as well as what the stance of the various creditors would be to the business rescue. Utilizing the aforesaid information that she could have obtained within the first 10 days of her appointment, Sarah should have then expressed her view at the first meeting as to whether a reasonable prospect of rescuing Khusela existed.

The rationale for this is that if a business rescue practitioner already at the first meeting of creditors is of the view that there no reasonable prospect of rescue, they must inform creditors this at the first meeting and then take steps to convert it into a liquidation.]

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)**

[Answer

In terms of Section 150(5) of the Companies Act 2008, a business rescue practitioner has 25 business days from the date of their appointment to publish the business rescue plan.

Commented [M38]: 2 marks. Needed to refer to section 132(3) - publish monthly progress reports after month 3 as the BR proceedings did not end within 3 months.

From the facts of this matter, it is evident the business rescue of Khusela has number of complexities ranging from the large number of employees to the varying interests of its creditors. As such, it would not be uncommon for the business rescue plan of Khusela to take a number of months to develop considering it is a large company, however, this would have had to have been conveyed to the creditors to obtain their consent.

However, given that Sarah took almost one year to publish to the business rescue plan of Khusela, she would have triggered Section 150(5) of the Companies Act which states that to the extent that a business rescue practitioner does not publish the business rescue plan within 25 days of their appointment as business rescue practitioner, such longer time can be permitted by (a) the court on application, (b) or the holders of the of a majority of the creditors' voting interests - i.e the simple majority consent of the creditors of Khusela.

The easiest manner that Sarah could have requested the extension was to simply request it from the creditors and if such consent was refused then an application to court may have been necessary.

The facts do not indicate if Sarah followed the available avenues and requested such extensions to publish the business rescue plan. One would assume that as a senior business rescue practitioner she would have been mindful of this requirement to avoid the potential legal consequences of non-compliance with Section 150(5) of the Companies Act.]

Question 17

Commented [M39]: 5 marks.

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)**

[Answer]

There are a few ways to determine if Mr Siwisa is an independent creditor of Khusela.

Firstly: Guidance pertaining to the definition of "independent creditor" can be found at Section 128(1)(g) which defines an "independent creditor" as:

(i) a creditor of the company, including an employee of the company who is a creditor in terms of section 144(2); and

(ii) not related to the company, a director, or the business rescue practitioner, subject to section 128(2).

It is clear that Mr Siwisa is a creditor in terms of Section 128(1)(g)(i), however, the fact that Mr Siwisa is a cousin of a director of Khusela requires further consideration. In this regard, Section 2(1)(a)(ii) provides that an individual is "related" to another if they are separated by no more than two degrees of natural or adopted consanguinity or affinity.

In view of the fact that Mr Siwisa is only a cousin to a director, that would not render him related to a director for the purposes of Section 128(1)(g)(ii) as more than two degrees of consanguinity exist. As such, and insofar as it concerns the fact that Mr Siwisa is a cousin to a director of Khusela, that in itself would disqualify Mr Siwisa from being an independent creditor of Khusela.

However:

Secondly: By virtue of his shareholder loan to Khuslea, Mr Siwisa is clearly a creditor. The same provisions concerning Section 128(1)(g) apply, however, one ought to now further consider Section 2(1)(b) as read with Section 2(2)(a)(ii) of the Companies Act, 2008 which provides that an individual is related to a juristic person (Khusela) if the individual directly or indirectly controls the juristic person and such person together with another related person is directly or indirectly able to exercise or control the exercise of the majority of the voting rights associated with the shares of the company.

Given that Mrs Lungi Phillips, a 26% shareholder in Khusela, is the half-sister of Mr Siwisa, they would be related to each other in terms of Section 2(1)(ii) and thus would in turn also be related for the purposes of Section 2(2)(ii)(aa).

Furthermore, Mr Siwisa and Mr Lungi Philips cumulatively own 51% of the issued shares in Khusela. They would thus, cumulatively, have the majority of the voting interests as contemplated in Section 2(2)(ii)(aa) and would therefore be able to exercise control over the voting rights contemplated in the section.
As such, it cannot be said that Mr Siswa is an independent creditor due to the provisions of Section 2 of the Companies. This must be so as if he was regarded as an independent creditor, he would be entitled to vote at the creditors meeting adopting the business rescue plan.

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)**

[Answer

Commented [M40]: 7 marks out of 8. Needed to state that the amended BR plan must be published.

As a general guideline a business rescue plan should always be structed in a way to allow it to be flexible and amended. A business rescue practitioner may even include a section in the plan that can allow amendments to the plan (to correct minor errors or clerical errors etc) subject to it not prejudicing the rights of the creditors. If the proposed amendment would have the effect of prejudicing or altering the rights of creditors, then the business rescue practitioner ought to first consult with the affected persons as provided for in terms of Section 150. The business rescue practitioner should then propose the amendments for consideration and voting at a meeting held in accordance with section 151. The proposed amendments will then only be effective should it be adopted in the same manner as provided for in section 152 of the Companies Act.

The facts state that the business rescue plan was not capable of being implemented in its initial form. This alone indicates that the heart or main thrust of the plan would need to change and such amendments cannot be done unilaterally. Furthermore, it is clear that Sarah could not validly amend the adopted business rescue plan on a unilateral basis particularly in view of the fact that the amendments were prejudicial to the interests of Crypto Bank Limited and Old Money Investment Corporation - so much so that both entities attempted to remove Sarah as business rescue practitioner.
A similar issue was dealt with by the court in Booysen v Jonkheer Boerewynmakery (Pty) Ltd (in business rescue) and Another. The court held that a business rescue practitioner did not have the right to unilaterally amend a business rescue plan and thereby circumvent the provisions of the Companies Act 2008 and furthermore that the business rescue practitioner did not have the power to impose on the creditors a plan which they had not voted on and discussed in the manner contemplated by Section 152.

In view of the legislative provisions cited above as well as the case law on the topic, it is clear that if the amended business rescue plan changes the heart of the initial plan or alters the rights of creditors then you need same threshold of support as adoption of the initial plan to support your amended plan.

As such, to the extent that an amendment to the plan requires implementation as envisaged aforesaid, the following requirements are needed and ought to have been followed by Sarah:

1. The business rescue practitioner should first consult with the affected persons as provided for in terms of Section 150 with regards to the proposed amendment to the plan;

2. The business rescue practitioner should then propose the amendments for consideration and voting at a meeting held in accordance with section 151;

3. The proposed amendment will then only be effective should it be adopted in the same manner as provided for in section 152 of the Companies Act. In this regard, the amended business rescue plan must get 75% of the creditors voting interest that was voted and at least 50% of the independent creditors' voting interests that were voted as envisaged in Section 152(2)

and to the extent that shareholders rights may be altered, then the majority vote of such shareholders.]

Sarah ought to have followed the above procedure. This would have ensured that her conduct was not susceptible to an application to remove her as business rescue practitioner.]

Question 19

Commented [M41]: 2 marks out of 3.

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)**

[Answer]

Opera Sound Engineering, as a creditor, should expect to the following the three key items in the financial projections:

1. A notice of material assumptions- i.e. what are the business rescue practitioners assumptions about working capital etc and what is driving the financial forecast of the company;

2. Alternative projections taking into account varying assumptions and contingencies - i.e what are the key sensitivities of the plan that might impact its successful implantation. This should include factors like exchange rate changes.

3. An illustration as to the cash flow of the company as this would inform the basis as to how dividends will be paid to the creditors]

Question 20

Commented [M42]: 2 marks.

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)**

[Answer

A cash flow statement shows cash flows from operations, investment activities and financing activities and provides clarity on future cash flow of the business. It may also assist creditors on seeing the basis on which dividends are calculated.

As such, I would advise Sarah that whilst a cash flow statement is not required in terms of Section 150(2)(c)(iv) in the same way as balance sheet and income statement, it would still nevertheless be considered as a best practice standard to include a cash flow statement in the business rescue plan. To further ensure best practice standards, I would further advise

Sarah to provide a full set of financial forecasts for three years (balance sheet, income & expense and cash flow statement).]

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)**

[Answer

1. Business rescue as opposed to liquidation would mean that Khusela can continue to operate (at least for the foreseeable future from commencement of business rescue). As such, the most apparent advantage would be that the jobs of the employees could be preserved. Thus whilst retrenchments were needed, complete job loss for all 2000 employees was avoided - this would not be the case on a liquidation.

2. Employee rights, ranking and preferences of in respect of their claims both pre & post commencement of business rescue are elevated above other affected persons. In this regard, payment of employee post commencement claims for remuneration & other employment related claims in terms of S135(1) of the Companies Act 2008 as read with Section 135(5)(3)(a) receive a preference for such payments in that they are paid after the business rescue practitioner is, who is paid first in business rescue.

   In terms of Section 144(2), pre-business rescue debts of employees still receive a preference under this section. These employees are preferred unsecured creditors and thus rank after post-commencement claims but before unsecured creditors. The South African Pilots Association and South African Airways (2021 LC) case said that preferences afforded to employees in terms of S144(2) could not be compromised or negated in a business rescue plan. Thus when the above position is contrasted to a liquidation where employees would have limit on their preference claim but only up to a limited monetary amount, the rest being a concurrent claim in the liquidation. The position for employees is thus far more beneficial in business rescue.

3. On a liquidation, employee contracts are suspended and with the effluxion of time they will terminate. However, on a business rescue, Section 136(1)(a) provides that during business rescue proceedings an employee will remain employed of the same terms as conditions subject to the exceptions of Section 136(1)(a)(i) and (ii). Furthermore, any retrenchments must be done in terms of a business rescue plan and pursuant to a Section 189 process as contemplated in the Labour Relations Act. In view of the aforesaid, the employment rights of employees with regards to procedural fairness are safeguarded in a business rescue whereas such considerations would not apply in a liquidation.]

*** END OF ASSESSMENT ***

TOTAL MARKS: [100]