Is Business Rescue really the so-called “lifejacket” alternative to our “sinking” liquidation proceedings:

A critical analysis of the Business Rescue and Liquidation proceedings compared.

by

SHANI DU PLOOY

201047968

A dissertation submitted in partial fulfilment for the degree

of

Master in Law (LL.M)

in

Mercantile Law

Faculty of Law

UNIVERSITY OF JOHANNESBURG

Supervisor: Prof Juanitta Calitz

2014

DECLARATION

I confirm that this is the final corrected version of my minor dissertation. I declare that no unethical research practices were used or material gained through dishonesty. I herewith declare that my academic work is in line with the Plagiarism Policy of the University of Johannesburg with which I am familiar.

SHANI DU PLOOY **02 February 2015**

FULL NAMES **DATE**

ACKNOWLEDGEMENTS

First and foremost I would like to take this opportunity to thank Professor Juanitta Calitz from the University of Johannesburg for the endless guidance, advice, time, patience and motivation she has shown me throughout this dissertation. Her sheer dedication as a supervisor has contributed greatly towards making the completion of this dissertation a reality.

Furthermore, none of this would have been possible without the continuous love and support from my family, friends and my partner, Chris Morgan. Their constant encouragement, patience and enthusiasm during this dissertation has motivated and inspired me beyond words.

Nelson Mandela said, “Education is the most powerful weapon which you can use to change the world.” I could not agree more. In light of this, I would like to thank the University of Johannesburg for giving me the opportunity to empower myself with one of the greatest weapons known to man, knowledge. With this knowledge, I will strive to change the world and empower those around me.

SUMMARY

The introduction of Chapter 6 of the Companies Act No 71 of 2008 into the South African corporate insolvency setting had a noteworthy impact on procedures as we knew it and replaced its predecessor, judicial management in terms of the Companies Act no 61 of 1973. Chapter 6 provides for business rescue proceeding, its main function being to assist and rehabilitate financially distressed companies. The significance of this chapter is that it promotes proactive action to be taken by companies in initiating business rescue proceedings when possible financial distress becomes apparent. Business rescue proceedings can commence by making use of S 129 of the Companies Act No 71 of 2008 or of S 130 of the Companies Act No 71 of 2008. S 129 allows for the board of directors of the company to pass a resolution permitting business rescue proceedings to apply to the relevant company. S 130, on the other hand, makes provision for an affected person to apply to the High Court with a query regarding a company and business rescue proceedings.

A remarkable number of new provisions were introduced relating to business rescue procedures and with their introduction came the responsibility of our Courts to interpret its rightful place within our law. As a result, the valuable question of when our courts should aim to rescue a company and when to liquidate the company's assets in order to settle its debts, must be asked. Both proceedings have the same aim; that is helping the financially distressed company pay its debts. However, both also employ vastly different methods to achieve their aims and with different consequences. Business rescue aspires to rescue the company by restructuring its financial arrangements in order to allow for the business of the company to be sold as a going concern. Business rescue further aims to help the company settle all its claims against it in full. Liquidation, on the other hand, aspires to sell all the company's assets and divide the profit of the sale to settle the claims of the company's creditors. The company will thereafter be dissolved.

This dissertation aims to analyse the suitability of business proceedings compared to liquidation proceedings by purposefully examining the requirements for both proceedings as well as their advantages. Furthermore, this dissertation will provide for a comparative study between the Australian and South African business rescue proceedings respectively.

TABLE OF CONTENTS

CHAPTER 1

INTRODUCTION

1 *INTRODUCTION*

> In my view, business rescue proceedings are not for the terminally ill close corporations. Nor are they for the chronically ill. They are for ailing corporations, which, given time, will be rescued and become solvent.[1]

When a company approaches a point of financial distress it has two alternative methods to winding up the company available to it: the company can choose to initiate business rescue proceedings or it can elect to reach a compromise with all its creditors.[2] For purposes of this paper, only the alternative method of initiating business rescue proceedings will be applicable to the discussion underneath and all relevant procedures are explained in Chapter 6 of the Companies Act 71 of 2008.[3]

Accordingly, the main function of business rescue proceedings is to facilitate the rehabilitation of a company in financial distress.[4] Section 128 (f) of the Companies Act 2008 describes financially distressed by referring to a particular company, at any particular time were it appears to '(i) be reasonably unlikely for the particular company to pay all of its debts as they become due and payable within the immediately ensuing six months; or (ii) be reasonably likely that the company will become insolvent within the immediately ensuing six months.' The significance of this definition lies in the fact that it promotes proactive action to be taken

[1] *Welman v Marcelle Props 193 CC and Another* (33958/2011) [2012] ZAGP JHC 32 (24 February 2012) par 28.

[2] Sharrock, Smith and van der Linde *Hockly's Insolvency Law* (2012) 275.

[3] Hereinafter referred to as the Companies Act 2008. Part 5.3A of the *Corporations Act* 2001 (Cth) is the Australian equivalent to our chapter 6 business rescue proceedings. These Australian provisions are called voluntary administration. Both of these jurisdictions include its corporate insolvency provisions in its general company law statute and the Australian insolvency provisions can be located in its general Corporations Act (2001, Chapter 5). Also see Anderson "Viewing the proposed South African business rescue provisions from an Australian perspective" 2008 *PER LJ* 104.

[4] Sharrock, Smith and van der Linde (n 2). See Meskin PM *Insolvency law* Lexis Nexis Databases updated (2014) (http://www.mylexisnexis.co.za/Index.spx.) (20-10-2014) for an in-depth discussion on business rescue proceedings. Also see Smyth "Detecting 'red flags' early can help a business avoid severe financial distress" 2012 *Tax Professional* 26. The Australian voluntary administration is specifically aimed at rescuing companies experiencing financial distress and S 435A (Of the Corporations Act 2001 (Cth) lists the objects as follows; "...to provide for the business, property and affairs of an insolvent company to be administered in a way that: (a) maximises the chances of the company, or as much as possible of its business, continuing in existence; or (b) if it is not possible for the company or its business to continue in existence- results in a better return for the company's creditors and members that would result from an immediate winding up of the company." (Hunt and Handa "A critical comparison between Australian and Canadian creditor protection regimes: Voluntary administration and CCAA" 2005 Available at SSRN 6-7) These provisions are almost identical to the objectives listed in S 128(1) (f) of the South African Companies Act 2008.

by companies in initiating business rescue proceedings when possible financial trouble becomes apparent.[5]

Business rescue commences when the board of directors of the company passes a resolution in favour of initiating business rescue proceedings in terms of section 129 of the Companies Act 2008 or the High Court is approached with a business rescue application request in terms of section 130 of the Companies Act 2008.[6]

Section 7(k) of the Companies Act 2008 provides for the 'efficient rescue and recovery of a financially distressed company, in a manner that balances the rights and interests of all the relevant stakeholders' of the particular company.[7] This section can be seen as one of the most important purposes of business rescue. As a result, our courts will use section 131(6) of the Companies Act 2008 to award a high level of preference to business rescue proceedings over that of liquidation proceedings, given that there is an authentic endeavour to rescue the business.[8] Section 131(6) provides that in the event where liquidation proceedings have already been initiated by or against a company at the time a business rescue application is made, the business rescue application will suspend those liquidation proceedings until the court has either adjudicated upon the application, or when the business rescue proceedings terminate, should the court grant the order applied for.[9] This specific section has the effect of bringing any pending liquidation proceedings against the particular company to a complete halt. This places any creditor and/or liquidating practitioner to a pending liquidation proceeding against a

[5]Wassman"Business rescue-getting it right" 2014 De Rebus 36 37.

[6]Wassman (n 5) 36. See Rushworth "A critical analysis of business rescue regime in the Companies Act 71 of 2008' 2010 *Acta Juridica* 375.

[7] Loubser (n 21) 16 below. In *Swart v Beagles Run Investments 25 (Pty) Ltd and Others* Makgoba, J stated at par 29 that '[w]here an application for business rescue...entails the weighing-up of the interests of the creditors and the company the interests of the creditors should carry the day.'

[8]S 131(6) of the Companies Act 2008. In A*bsa Bank Ltd v Summer Lodge (Pty)* Ltd 2013 (5) SA 444 (GNP) concluded in par 12 that all legal proceedings instituted by the liquidator in the liquidation proceedings which are pending as at the date an application for business rescue proceedings is made against a company under liquidation are automatically suspended when such an application is made.

[9]In *Van Niekerk v Seriso 321 CC & another* [2012] ZAWCHC 63 (20 March 2012) at par 23 the court found that an application for business rescue may be made even if proceedings for the liquidation of the company have already commenced in terms of s 131(6). In *Cardinet (Proprietary) Limited v Wedgewood Golf and Country Estates (Pty) Ltd (in liquidation)* WCC Case no 19599/2012 at par a business rescue order was issued almost a year after the final liquidation order was granted. In *Van Zyl v Engelbrecht* 2014 (5) SA 312 (FB) at par 14 The phrase 'liquidation proceedings' in s 131(6) of the Companies Act 2008 have been held to —'refer to a process that consists of the collection of the assets, realising and reducing them to money, dealing with proof of creditors by admitting or rejecting them, and distributing the net proceeds after providing for costs and expenses by the liquidator to the persons entitled thereto. Thus, the words liquidation proceedings have to do with the process that is overseen by the liquidator and the Master of the High Court in winding-up and not the legal proceedings before a court of law in order to obtain such order.' Also see Braatvedt "Unscrambling the liquidation egg" 2013 *Without Prejudice* 36.

company, who now wishes to pursue the business rescue application route in an undesirable situation. Section 131(7) of the Companies Act 2008 further provides a court with additional powers to make an order in terms of section 131 (4) or (5) of the Companies Act 2008 *at any time* during the course of any liquidation proceedings, or to alternatively allow the courts to enforce any security against the company.[10] The literal meaning of 'at any time' and when might it be too late to institute business rescue proceedings by or against a company when the same company is already involved in pending liquidation proceedings still needs to be determined.[11] This query however, was addressed in the case of *Van Staden v Angel Ozone Products CC*[12] where the court held that 'winding-up proceedings are part and parcel of the liquidation proceedings' meaning a business rescue application can be initiated even in the dying stages of the winding up of a company. This affirmation is both problematic and unpractical because how do you undo all the work done by the liquidators. There almost is no answer. In fact, a handful of provisions in Chapter 6 of the Companies Act 2008 dealing with business rescue proceedings are extremely vague and perplexing, resulting in numerous questions being asked but no concrete answers provided. Consequently, it must be determined if business rescue really is a sensible solution in all matters where liquidation proceedings are already well underway and have a greater possibility of securing better returns for the creditors. Due to the nature and space limitation of this paper, only a few of the problematic provisions, as mentioned above, will be discussed in support of my problem statement and arguments.

In recent case law, *Oakdene Square Properties (Pty) Ltd & others v Farm Bothasfontein (Kyalami) (Pty) Ltd & others* [13] the court considered the relevant business rescue provisions in the Companies Act 2008 and came to the conclusion that proceeding with liquidation procedures will be more beneficial and appropriate in the specific circumstances of this matter

[10] S 131 (4 and (5) of the act states the following; " (4) After considering an application in terms of subsection (1), the court may- (a) make an order placing the company under supervision and commencing business rescue proceedings, if the court is satisfied that – (i) the company is finally distressed; (ii) the company has failed to pay over any amount in terms of a public regulation or contract, with respect to employment-related matters; or (iii) it is otherwise just and equitable to do so for financial reasons, and there is a reasonable prospect for rescuing the company; or (b) dismissing the application, together with any further necessary and appropriate order, including an order placing the company under liquidation. (5) If the court makes an order in terms of subsection (4) (a), the court may make a further order appointing an interim practitioner a person who satisfies the requirements of section 138, and who has been nominated by the affected person who applied in terms of subsection (1), subject to ratification by the holders of a majority of the independent creditors' voting interests at the first meeting of creditors, as contemplated in section 147."

[11] Braatvedt (n 9).

[12] 2012 JDR 1945 (GNR) at par 32 and 36.

[13] (609/2012) [2013] ZASCA 68 (27 May 2013). Hereinafter referred to as *Oakdene Square Properties* case.

than business rescue proceedings.[14] This case therefore proves that liquidation proceedings are far from 'sinking' or being rendered useless and every company in distress does not have to make use of business rescue proceedings as a lifejacket in order to stay afloat. In fact, if the right circumstances are presented, liquidation proceedings are preferred to business rescue proceedings as an alternative option to winding up the company. Due to the space limitations of this dissertation, only certain relevant sections of the relevant acts will be discussed and no detailed procedural law regarding business rescue will be provided.

2 *OVERVIEW OF JUDICIAL MANAGEMENT*

At present, Chapter 6 in the Companies Act 2008 provides for the concept of business rescue and replaced Chapter XV of the Companies Act 61 of 1973, [15] which provided for the judicial management of companies who found themselves in financial difficulty.[16] Joubert[17]explained that the introduction of chapter 6 into our current corporate environment is a necessity. It was designed to align South Africa's corporate rescue procedure with other international jurisdictions such as Australia, United States of America and the United Kingdom[18], unlike judicial management.

Judicial management placed an overly protective emphasis on creditor's interests in contrast to the aim of rescuing a debtor from financial difficulty, and its constant inclination to result in liquidation orders were the final nails in judicial management's coffin.[19] Section 427(1) of the Companies Act 1973 states that a judicial management order may be granted by a court if "any company" meets the requirements specifically mentioned in this section.[20] The section states that if a company, by reason of mismanagement or for any other cause is unable to pay its debts or is unable to meet its obligations and has not become or is prevented from becoming a successful concern, a court may place the company under judicial management.[21] Furthermore, there also needs to be a reasonable probability that if the company is placed under judicial management, it will be able to pay its debts or meet its obligations in order to become a

[14]See the *Oakdene* case (n 14) par 39 and 40.
[15] Hereinafter referred to as Companies Act 1973.
[16] Bradstreet "The leak in the Chapter 6 lifeboat: Inadequate regulation of Business Rescue Practitioners may adversely affect lenders' willingness and the growth of the economy" 2010 *SA Merc LJ* 195-196.
[17]Joubert "'Reasonable possibility' versus 'reasonable prospect': Did business rescue succeed in creating a better test than judicial management?"2013 *THRHR* 550.
[18]Joubert (n 18).
[19] Bradstreet "The new business rescue: will creditors sink or swim?" 2010 *SALJ* 352 353-354.
[20]Loubser "Some comparative aspects of corporate rescue in South Africa" (2010 LLD thesis) University of South Africa 16.
[21]Loubser (n 21) 20.

successful concern.[22]Lastly, section 427(1) requires a court to ensure that an order for judicial management will be just and equitable before it may grant such an order.

However, these very stringent requirements made it nearly impossible for companies to qualify for judicial management orders, resulting in the severe failure of this corporate rescue system. Joubert[23] lists the three main disadvantages of judicial management: Firstly, judicial management was a "cumbersome and ineffective procedure".[24] Secondly, the "high threshold of proof required" to obtain a reasonable probability before an order for judicial management will be granted was nearly unattainable.[25] To acquire this level of onus of proof became impractical and unfeasible. Lastly, there was a stigma attached to judicial management as it was labelled an "extra-ordinary remedy which infringes on the rights of creditors".[26]The court in *Le Roux Hotel Managaement(Pty) Ltd & another v E Rand (Pty) Ltd* [27] even went so far as to say that it views judicial management as "a system which has barely worked since its initiation in 1926." It was more than clear that South Africa was in dire need of new, workable corporate rescue legislation, hence the promulgation of chapter 6 in the Companies Act 2008.

3 *PROBLEM STATEMENT*

> It is not surprising that, thus far, the bulk of judicial decisions involving business rescue have involved the commencement of business rescue and the correct test to be applied to establish whether or not a business is indeed "rescuable".[28]

The new business rescue procedure has been designed to prevent the demise of viable companies by making provision for their possible rescue as an alternative method to the winding-up of the company.[29] If the company cannot be returned to a state of solvency, the secondary goal can be used in order to obtain a business rescue order. The secondary goal provides that business rescue proceedings can be used if there is an authentic possibility of securing a better return for the company's creditors and other relevant stakeholders. Business

[22]Loubser (n 21) 20.
[23]Joubert (n 18) 551.
[24]*Southern Palace Investment 265 (Pty) Ltd v Midnight Storm Investments 386 (Pty) Ltd* 2012 2 SA 423 (WCC) para 20 as used in Joubert (n 18) 551.
[25] Burdette "Unified insolvency legislation in South Africa: Obstacles in the path of the unification process" 1990 *De Jure* 57 58 and Smiths 96 as used in Joubert (n 18) 551.
[26]Loubser (n 21) 20 and Kloppers "Judicial management- A corporate rescue in need of reform?" 1999 *Stell LJ* 426.
[27] (2001) 2 SA 427 (C) para 60.
[28]Swanepoel and Gopal "An inacceptable business rescue mess" 2013 *Without Prejudice* 16.

[29] Meskin (n 4).

rescue provisions therefore hold a dual purpose. Accordingly, either one of the purposes, as set out in section 128(1) (b) of the Companies Act 2008, needs to be discharged. Once this has been fulfilled, grounds for the reasonable prospect of rescuing the company have been established. However, due to the vague nature and very similar wording to judicial management's 'reasonable probability', more clarity regarding the meaning and interpretation of the term 'reasonable prospect' is required.[30] Furthermore, the need to determine when business rescue will actually be applicable and more successful than liquidating a company has taken a front seat in many judicial matters and academic debates.

The purpose of this dissertation is to try and determine when to make use of business rescue proceedings without abusing the provision recklessly and when to realise there are no realistic merits for making use of any business rescue provisions. In the latter case, commencing with liquidation proceedings will be just as appropriate and satisfactory, if not more than business rescue proceedings. Brand JA's judgment delivered in *Oakdene Square Properties* offers a leading example in curbing any abuse of our business rescue provision by asking the right questions and applying the boundaries of our insolvency law carefully to the facts *in casu.*[31] A considerable part of this dissertation will focus on the critical analysis the judgement delivered in *Oakdene Square Properties* with the aim of it providing more clarity on the term 'reasonable prospect'. The judgement will further assist in facilitating to determine when a company is in financial distress if it should employ liquidation proceedings or business rescue proceedings as well as if both proceedings can exist concurrently without taunting one another. This dissertation will further examine business rescue and liquidation, proceedings in detail and how it fits into our South African Law.

4 *METHODOLOGY*

This dissertation comprises of four chapters. The specific outcomes of each chapter are as follows:

[30] S 131(4) (a) of the Companies Act 2008.
[31] See the Oakdene case (n 14).

Chapter 1 introduces the focal point of this dissertation by providing a general introduction of the concept of business rescue as well as liquidation proceedings. Judicial management is also discussed for purposes of providing the relevant background information. Chapter 1 further explains certain, customary concepts that will be found through the course of this dissertation.

Chapter 2 covers both the business rescue and liquidation proceedings in detail, providing for each procedure's various commencement stages as well as its legal consequences.

Chapter 3 critically analyses the advantages of the liquidation and business rescue proceedings, highlighting three main advantages of each procedure in the context of the *Oakdene* case.

Chapter 4 concludes this dissertation and briefly sets out the main contents discussed throughout the dissertation.

5 *CONCEPTS*

Concepts	**Meaning**
" The companies act 2008"	The Companies Act 71 of 2008
"The companies act 1973"	The Companies Act 61 of 1973
" The insolvency act"	The Insolvency Act 24 of 1936
"The labour relations act"	The Labour Relations Act 66 1995
"The corporations act"	Corporations Act 2001 (Cth)
"The companies act 1981"	Companies Act 1981 (Cth)
Reference to any section	Reference made to the Companies Act 71 of 2008 unless specifically stated otherwise

CHAPTER 2

BUSINESS RESCUE AND LIQUIDATION PROCEEDINGS EXPLAINED

1 *THE DEFINITIONS AND OBJECTIVES*

The ultimate purpose of business rescue is to aid in the efficient rescue and rehabilitation of a financially distressed company.[32] In *Gormley v West City Precinct Properties (Pty) Ltd, Anglo Irish Bann Corporation Ltd v West City Precinct Properties (Pty) Ltd* [33] the concept of business rescue was envisaged as the need to restructure a potentially viable company in order for it to continue to function as an economic unit arose.[34] An independent business rescue practitioner would be appointed in order to facilitate the process by proposing an efficient plan to rescue the business.[35] Section 128(b) characterises business rescue as a means to facilitate the rehabilitation of a company that is financially distressed. The rehabilitation of a company is done by providing the temporary supervision of the company, and of the management of its affairs, business and property.[36] A temporary moratorium on the rights of claimants against the company or in respect of property in its possession is also provided as a means to make the rehabilitation of the company possible.[37] The last means is the development and implementation of the business rescue plan. If the plan is approved then it would be aimed at "restructuring its affairs, business, property, debt and other liabilities, and equity in a manner that maximises the likelihood of the company continuing in existence on a solvent basis or, if it is not possible for the company to so continue in existence, results in a better return for the company's creditors or shareholders than would result from the immediate liquidation of the company".[38]

As pointed out and discussed in *Hockly's* [39]the question of whether business rescue can be used to ensure a better return for creditors or shareholders where there is no clear prospect of the

[32] Section 7(k) of the Companies Act.
[33] [2012] ZAWCHC 33 (18 April 2012) at par 6.
[34]Sharrock, Smith and van der Linde (n 2) 276.
[35] Sharrock, Smith and van der Linde (n 2) 275. Hereinafter referred to as the practitioner.
[36] S 128 (b) (i) of the Companies Act 2008.
[37] Sharrock, Smith and van der Linde (n 2) 276.
[38] S 128 (b) (iii) of the Companies Act 2008.
[39] Sharrock, Smith and van der Linde (n 2)276.

company continuing to trade or being restored to a position of solvency has puzzled our courts and for this reason we have different judgments regarding this question. As listed in *Hockly's* [40] the court in *Swart v Beagles Run Investments 25 (Pty) Ltd (Four Creditors intervening)* [41] concluded that it is indeed possible to make use of business rescue with the sole intention of securing a better return for the creditors and shareholders and that using business rescue for this goal will be regarded as an independent alternative goal. In *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 Ltd* [42] the court concurred with this conclusion, firmly stating that if this independent alternative goal were intended to be relied on, it is of vital importance that it be made clear what resources would made available and on which terms. This is to prevent the goal of securing a better return not just being a mere speculation but for it to be based on facts. In *AG Petzetakis International Holdings Ltd v Petzitakis Africa (Pty) Ltd* [43] nevertheless the court has its reservations whether the objective of ensuring a better return for creditors or shareholders can be used to enable parties to use business rescue proceedings. The court elaborated by reminding itself of section 131(4) of the Companies Act 2008 which states that before a court may grant an order to commence with business rescue, it must be satisfied that there is a reasonable prospect for rescuing the company.[44]

Section 131(4) provides information for specific circumstances in which a court may grant a business rescue application, should the applicant meet the necessary requirements.[45] While assessing if these requirements have been met, the court must further exercise its discretionary powers to decide whether there is a 'reasonable prospect' of the relevant company being rescued.[46] In order for a company to have access to business rescue it must be "financially distressed" and there must be a 'reasonable prospect' of saving it.[47] Therefore, before business

[40]Sharrock, Smith and van der Linde (n 2). See decision in *Commissioner, South African Revenue Service v Beginsel NO and Others* 2013 (1) SA 307 (WCC).
[41] 2011 (5) SA 422 (GNP) at par 25.
[42]See the *Southern Palace Investments 265* case (n 25).
[43] 2012 (5) SA 515 (GSJ) at par 13 and 14.
[44] Furthermore, like South Africa, Australian courts have also identified that the voluntary administration procedure may be used in cases where the company at hand has no real prospects of being rescued but instead, the aim of the application is to attempt to ensure a better return for its creditors. This secondary goal can be pursued and be preferred before winding-up a company. In *Dallinger v Halcha Holdings* 1996 14 ACLA 263 held at par 268 *the* court held, "where, although it is not possible for the company to continue in existence, an administration is likely to result in a better return for creditors*".*
[45] See par 2.1 below.
[46] S 131(4) (a) of the Companies Act 2008. Also see Bradstreet "Business rescue proves to be creditor-friendly: CJ Classen J's analysis of the new business rescue procure in *Oakdene Square Properties*" *SALJ* 49.
[47]Loubser A "The business rescue proceedings in the Companies Act of 2008: Concerns and questions (part 1)" 2010 *TSAR* 501 502.

rescue may be applied for, section 128(f)[48] is the first hurdle any alleged financially distressed company must jump and then it must prove that a reasonable prospect of the company being rescued exists, before being allowed to proceed with a business rescue application. The meaning of a 'reasonable prospect' will be discussed in detail below.[49]

With regards to liquidation proceedings on the other hand, sections 337-426 of the Companies Act 1973 regulate the winding-up of insolvent companies. A commercially insolvent company can be described as a company which is unable to pay its debts as they become due and payable to its relevant creditors.[50] In *ABSA Bank v Rhebokskloof (Pty) Ltd* [51] the court addressed the concept of commercial insolvency. Berman AJ held:

> Turning to the merits of the matter, Mr. Gauntlett contended that ABSA was entitled to a final winding-up order on the basis that Rhebokskloof was commercially insolvent. The concept of commercial insolvency as a ground for winding up a company is eminently practical and commercially sensible. The primary question which the Court is called upon to answer is deciding whether or not a company carrying on business should be wound up as commercially insolvent is whether or not it has liquid assets or realizable assets available to meet its liabilities as they fall due to be met in the ordinary course of business and thereafter to be in a position to carry on normal trading- in other words, can the company meet current demands on it and remain buoyant? It matters not that the company's assets, fairly valued, far exceeds its liabilities: once the Court finds that it cannot do this, it follows that it is entitled to, and should, hold that the company is unable to pay its debts within the meaning of Section 345(1)(c) as read with Section 344(f) of the Companies Act 61 of 1973 and is accordingly liable to be wound up[52]

[48] Of the Companies Act 2008 which defines what a "financially distressed" company is.

[49] See par 3 below.

[50] S 345 of the Companies Act 1973; "When company deemed unable to pay its debts. (1) A company or body corporate shall be deemed to be unable to pay its debts if- (a) a creditor, by cession or otherwise, to whom the company is indebted in a sum not less than one hundred rand then due- (i) has served on the company, by leaving the same at its registered office, a demand requiring the company to pay the sum so due; or (ii) in the case of any body corporate not incorporated under this Act, has served such demand by leaving it at its main office or delivering it to the secretary or some director, manager or principal officer of such body corporate or in such other manner as the Court may direct, and the company or body corporate has for three weeks thereafter neglected to pay the sum, or to secure or compound for it to the reasonable satisfaction of the creditor; or (b) any process issued on a judgment, decree or order of any court in favour of a creditor of the company is returned by the sheriff or the messenger with an endorsement that he has not found sufficient disposable property to satisfy the judgment, decree or order or that any disposable property found did not upon sale satisfy such process; or [Para. (b) substituted by s 26 of Act 59 of 1978.] (c) it is proved to the satisfaction of the Court that the company is unable to pay its debts. (2) In determining for the purpose of subsection (1) whether a company is unable to pay its debts, the Court shall also take into account the contingent and prospective liabilities of the company."

[51] 1993 (4) SA 436 (C).

[52] In *Standard Bank of South Africa Ltd v R-Bay Logistics CC* 2013 (2) SA 295 (KZD) at par 14 the court concluded that the word 'solvency' includes the commercial insolvency and the word 'insolvent' includes commercial insolvency, as referred to s 79-82 and item 9 Schedule 5 of the Companies Act 2008.

In addition, the court in *HBT Construction and Plant Hire CC v Uniplant Hire CC*[53] that an application for the liquidation of a company can only succeed if there was proof that the respondent was insolvent or that it was just and equitable that the respondent be liquidated.

The ultimate purpose of liquidation is to pay the creditors what is owed to them or, if full payment is not possible, to give back the biggest possible portion to them.[54] If any surplus remains after paying the respective creditors, it should be yielded to the shareholders of the company and once all the liquidation assets has been finalised as well as all the debts paid, the company will be dissolved and will cease to exist.[55] Item 9 of Schedule 5 of the Companies Act 2008 regulates the continued application of sections 337-426 (Chapter 14) of Companies Act 1973, dealing with the winding-up and liquidation of insolvent companies. Item 9(4) (a) of Schedule 5 of the Companies Act 2008 [56] further states that Chapter 14 will remain in effect up until competent and alternative legislation providing for the liquidation and winding-up of insolvent companies has been promulgated to replace it. In addition to the above mentioned applicable sections, section 339 of the Companies Act 1973 also provides that provisions relating to insolvency law must be applied *mutatis mutandis* where relevant and the "notion of insolvency law is thus of paramount importance in this regard".[57]

Finally, if a company or a close corporation is financially distressed but is able to be rehabilitated, the company can become subject to corporate business rescue proceedings. This results in not dissolving the company but rather granting the company an opportunity to recover financially, should this option be viable. In *Firstrand Bank Limited v Imperial Crown Trading 143 (Pty) Limited*[58]the court granted the application for a provisional liquidation order because there was no valid ground that existed for refusing the provisional order. The court did, however, grant an extended return date, in order to enable an application for business rescue to be brought by any 'affected person'.

[53] 2012 (5) SA 197 (FB) at par 5 and 6.
[54]Nagel *Commercial law* Lexis Nexis South Africa (2011) 574.
[55]Nagel (n 55) 574, which referred to section 82 and section 83 of the Companies Act 2008.
[56] Sharrock, Smith and van der Linde (n 2) 240.
[57]Nagel (n 55) 574.
[58] 2012 (4) SA 266 (KZD) at par 23.

2 *BUSINESS RESCUE UNDER THE COMPANIES ACT OF 2008*

2.1. The commencement of business rescue by means of section 129 of the Companies Act 2008

The first method which will commence business rescue proceedings is when the board of the directors of a company formally decide to commence with business rescue proceedings, in terms of section 129 of the Companies Act 2008, on behalf of the company.[59] The board of directors can only commence business rescue proceedings if a majority vote has been obtained. Section 129(2) (a) provide that a business rescue resolution can however not be approved if liquidation proceedings have been commenced by or against the company and vice versa. Once the resolution to commence business proceedings is valid and adopted, the company is barred from commencing liquidation proceedings[60].

A resolution for the initiation of business rescue proceedings may only be considered if there are reasonable grounds to believe the company is financially distressed[61] and if there appears to be a reasonable prospect of rescuing the company.[62] Business rescue procedure has been designed to prevent the demise of viable companies by making provision for their possible rescue as an alternative method to the winding-up of the company[63]. If the company cannot be returned to a state of solvency, the secondary goal can be used in order to obtain a business rescue order. [64]The secondary goal provides that business rescue proceedings can be used if there is an authentic possibility of securing a better return for the company's creditors and other relevant stakeholders.[65] Business rescue provisions therefore hold a dual purpose.

As seen in various cases, the court encourages an applicant to discharge one of the two purposes set out in section 128(1) (b) of the Companies Act.[66] Once this has been achieved, grounds for

[59]Davis, Cassim, Geach, Mongalo , Butler , Loubser , Coetzee and Burdette *Companies and other business structures in South Africa* Oxford University Press Southern Africa (2012) 225 229. Also see Bradstreet (n 20) 364. Also see Cassim *Contemporary Company Law* Juta South Africa (2012) 866.

[60] s 129(6) of the Companies Act 2008. Also see Kunst *Henochsberg on the Companies Act No 71 of 2008* Lexis Nexis Databasis updated (2011).

[61] See chapter 2, paragraph 1 above.

[62] s 129(1)(a) and (b) of the Companies Act 2008. Also see chapter 2, paragraph 1 above.

[63] See Meskin (n 4).

[64] s 128 (1) (a) (i)-(iii) of the Companies Act 2008.

[65] s 128 (1) (a) (i)-(iii) of the Companies Act 2008.

[66] See *Oakdene Square Properties (Pty) Ltd & Others v Farm Bothasfontein (Kyalami) (Pty) Ltd & Others*) (609/2012) [2013] ZASCA 68 (27 May 2013); *Newcity Group Limited (Pty) Ltd v Allan David Pellow N.O and Others*

the reasonable prospect of rescuing the company would have been established. Section 129(7) states that if both reasonable grounds are present, the board has to either pass the resolution or deliver a written notice to each affected person explaining on which possible grounds the company is financially distressed as well as why a business rescue resolution was not adopted. [67] More detail regarding the meaning and interpretation of the term 'reasonable prospect' will be discussed below.

2.1.1. The technicalities in commencement of a business rescue resolution

Once the resolution is filed and delivered to the Companies and Intellectual Property Commission, is the date the resolution become effective.[68] Section 129(3) states that the company must notify all affected persons within 5 business days after filing resolution by publishing a notice of the resolution to them as well as appointing a business rescue practitioner. [69] Section 129(4) states that the company must file a notice of the appointment of a business rescue practitioner within 2 business days after the appointment and must also publish a copy of such notice within 5 days after its filing. [70] Section 129(5) states that if the

(577/2013) [2014] ZASCA 162(1 October 2014) and *Propspec Investments* (*Pty*) *Ltd v Pacific Coast Investments 97 Ltd and Another*2013 (1) SA 542 (FB).

[67]The definition of an affected person is defined in S 128 (1) (a) (i)-(iii). Also see Davis, Cassim, Geach, Mongalo , Butler, Loubser , Coetzee and Burdette (n 60) 231.

[68]A filed delivery to the Companies and Intellectual Property Commission, Hereinafter referred to as the commission, is implied. See s 129(2) (b) of the Companies Act. Also see Loubser "The business rescue proceedings in the Companies Act of 2008: Concerns and questions (part 2)" 2010 *TSAR* 689 693. Voluntary administration is said to have commenced when the administrator has been appointed in terms of S 435C (1) of the Corporations Act 2001 (Cth). Unlike South Africa however, Australian courts does not have the powers to make an order to appoint an administrator (Anderson (n 3) 113)), essentially allowing the voluntary administration system to function without nearly any court intervention (Hunt and Handa (n 4) 2)).For more information regarding the functions of the Australian courts during voluntary administration see Hunt and Handa (n 4) 21-23. The main reason for this feature of the voluntary administration regime is that it is specifically designed to be moderately cheap and efficient (Hunt and Handa (n 4) 27). Also see Utz C "Voluntary administration: The Australian experience" 2008 Available on http://www.claytonutz.com/docs/VoluntaryAdministration_TheAustralianExperience.pdf 3-5.

[69] It is possible for the court to give its permission to extended the five business day period provided in the act should the court be satisfied that it is reasonable and if permission has been granted by the Companies and Intellectual Property Commission. An interesting observation made by Anderson (n 3) 117) is that "this suggests that the company may be within the business rescue regime without the control of the company being with the supervisor. It therefore provides the opportunity for something of a gap to be created of up to five business days during which the supervisor is not in place. Under proposed section 143 it is the supervisor who is responsible to supervise and advise the management whilst the business rescue is in place but the ability to retrospectively do this (where the appointment is made five days later) is unclear." This examination clearly calls for some form of clarity and it can be recommended that a possible solution could be to oblige the appointment of the practitioner to coincide with the commencement of the procedure (Anderson (n 3) 117).For information of how to end the process of voluntary administration see Hunt and Handa (n 4) 16-17.

[70] In Advanced *Technologies and Engineering Company (Pty) Ltd (in business rescue) v Aéronautique et Technologies Embaraquees SA and Others* (GNP) (unreported case no 72522/11, 6-6-2012, the court held: "it is clear... that a degree of urgency is envisaged once a company has decided to adopt the relevant resolution

company does not comply with sub-sections (3) and (4) above, the resolution lapses and is a nullity. As a consequence, the company will not be allowed to file another business rescue resolution passed by the company within three months after the date of adopting the last resolution that has lapsed.

The observation was made by some learned authors, in the textbook Companies *and other business structures in South Africa*, that this consequence seems unjustifiably harsh for something that could just be a minor oversight on the part of the company-for example, notifying an affected person one day late would give rise to this ruthless consequence. [71]

2.1.2. Terminating or setting aside the business rescue resolution or appointment of the practitioner

It is possible to set aside the business rescue resolution or the appointment of the practitioner.[72] After the board of directors of the company accept the commencement of the business rescue resolution but before it has formally been adopted, any affected person may submit an application to court to set aside the resolution.[73] The application must be submitted on the following grounds: there is no reasonable belief that the company is financially distressed; there is no reasonable prospect that the company will be rescued; or the company has failed to comply with the procedures set out in section 129.[74] It is unclear why an affected person must apply to court to have the resolution set aside since section 129(5) already stipulates that the resolution will automatically become null and will lapse if a company fails to comply with the requirements set out in section 129(4) and (5). What creates even further confusion is the fact that there is no clarification or explanation if the 'automatic lapsing and nullity' of the

beginning business process rescue proceedings. The purpose of S129 (5), is very plain and blunt. If there is non-compliance with s 129(3) and (4) the relevant resolution lapses and is a nullity. There is no other way, and no question of any condonation or argument pertaining to 'substantial compliance' ". However, it was held in *Ex parte Van den Steen NO & South Gold Exploration (Pty) Ltd* (3624/2013 GSJ) at par 12 and 15 that failure by the company applying for business rescue, to formally notify one group of creditors did not nullify the business rescue. The applied s 6(9) of the Companies Act 2008 that allows for substantial compliance with prescribed manner of delivery of notice.

[71] Davis, Cassim, Geach, Mongalo , Butler , Loubser , Coetzee and Burdette (n 60) 230.

[72]See Loubser (n 69) 689. In *Climax Concrete Products CC t/a Climax Concrete Products CC v Evening Flame Trading 449 (Pty) and Others* (ECP) (unreported case no 812/2012, 21-6-2012) at apr 16 as read in Van Staden "Cutting the lifeline. The termination of business rescue proceedings" 2013 *De Rebus* 14, the court held that in its opinion the application to have a business rescue resolution commence should be heard on an urgent basis

[73]Davis, Cassim, Geach, Mongalo , Butler , Loubser , Coetzee and Burdette (n 60) 231.

[74] S 130 (1) (a) of the Companies Act 2008 and Davis, Cassim, Geach, Mongalo , Butler , Loubser , Coetzee and Burdette (n 60)231.

resolution will have the same effect as it being void. The difference between these two concepts can have an incredible impact on the adopted resolution.

Lastly, section 130(1) (b) provides that an affected person may also apply to court to have the appointment of the practitioner set aside. This application must be based on one of the following grounds: that the practitioner does not satisfy the requirements of section 138 of the Companies Act 2008; the practitioner is not independent of the company or its management or the practitioner lacks the necessary skills when taking the specific circumstances and needs of the company into consideration. [75]

2.2. The commencement of business rescue by means of section 131 of the Companies Act 2008.

The commencement of business rescue by means of a court order is regulated by section 131 of the Companies Act 2008.[76] Section 131 (1) provides an alternative method for the commencement of business rescue proceedings by allowing an affected person to apply to court at any time for an order placing the company under supervision and commencing business rescue proceedings. In order for the court to grant and order in favour of the applicant, it must first make sure that the applicant has met various requirements.

2.2.1. The requirements that must be met in terms of section 131 of the Companies Act 2008

The first requirement is that the applicant must notify each affected person in the prescribed manner discussed above and then serve a copy of the application upon the company as well as the commission. [77] Section 131(4) provides the second requirement that must be met by the applicant, namely that the company must be financially distressed and it must have failed to pay over any amount in terms of an obligation under or in terms of a public regulation, or contract, with respect to employment-related matters.[78] Furthermore, if the court find it just and equitable to grant a business rescue order for financial reasons it may do so, in addition to there being a reasonable prospect for rescuing the company.[79] Finally section 131(4) (b) states that if the courts are not satisfied that the above mentioned requirements were met, it may dismiss the application and make any other additional but appropriate order including an order

[75] S 130(1) (b) of the Companies Act 2008.
[76] Cassim (n 60) 872. Also see Kunst *Henochsberg on the Companies Act No 71 of 2008* Lexis Nexis Databases updated (2011).
[77] S 131 (2) (a). See paragraph 2.1. and paragraph 2.1.1.
[78] S 131(4) (a) (i-ii) of the Companies Act 2008.
[79] S 131(4) (a) (iii)of the Companies act 2008.

placing the company under liquidation. It is important that a distinction is drawn between the position under section 129(1), where the board's resolution places the company under supervision and the position under section 131 where an affected person places the company under supervision by means of bringing an application. Under section 129 the board will have "full knowledge of the company's financial situation, what it is capable of achieving, and what would reasonably be required to rescue the company.''[80] In terms of section 131, however, the knowledge of the company's affairs that an affected person (an employee, creditor or shareholder) may have when an application is brought under section 131(4),would not necessarily have the information required to meet the requirements laid down by the Court in the *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 Ltd*. [81] Therefore, the court in *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 Ltd* [82] highlighted the higher threshold in order to succeed when using a rescue by means of a court order.[83]

2.2.2. The legal consequences of business rescue

When a company commences with business rescue proceedings, the company needs to be protected by temporarily placing a general moratorium on all legal proceedings that any creditors and employees may have against the company, allowing the company to try and find its feet again.[84] It is during this general moratorium that companies should channel all their available resources or attempt to obtain investors willing to bail the company out of its financial trouble instead of paying off existing debt, with money that it does not have.[85] Matters will arise where saving the business is simply not financially and practically viable. In such an instance, business rescue provisions will solely aim to keep the business alive temporarily in order to try and ensure a better return for all stakeholders of the company. As a result, business rescue has certain legal consequences for the company's activities and for its stakeholders as well.[86] The effects of the legal consequences are as follows: [87]

[80] Meskin (n 4) 18.4.3.
[81] See the *Southern Palace Investments 265* case (n 25). Also see *The Employees of Solar Spectrum Trading (Pty) Ltd v Afgri Operations Ltd and Another*; In re *Afgri Operations Ltd v Solar Spectrum Trading (Pty) Ltd* unreported Case nos. 6418/11, 18624/11, 66226/11 (GNP) at par 17.
[82]See the *Southern Palace Investments 265* case (n 25) at par 21.
[83] Wassman (n 5)37.
[84] The general moratorium will operate for duration of the business rescue. See Bradstreet (n 20)352.
[85]Bradstreet (n 20) 352.
[86]Davis, Cassim, Geach, Mongalo , Butler, Loubser , Coetzee and Burdette (n 60) 235.
[87]Davis, Cassim, Geach, Mongalo , Butler, Loubser , Coetzee and Burdette (n 60) 235.

- majority of civil legal proceedings are paused until business rescue proceedings are terminated(general moratorium); [88]
- the disposal of the company's property is restricted;[89]
- post-commencement finance will be regarded as preferential claims and will receive a super-preferential status; [90]
- the employees' contracts are protected; [91]
- the business rescue practitioner may suspend, or even cancel, any contracts in certain circumstances; [92]
- the status of issued shares may not be altered, and shareholders may only participate in decisions about business rescue if their interests will be affected; [93] and
- the directors of the company must cooperate with the business rescue practitioner; [94]

Due to the purpose of this dissertation, as well as its limitations, only the general moratorium as a legal consequence of business rescue proceedings will be discussed.

The application of the general moratorium at the commencement of business rescue proceedings is regarded as one of the most important consequences of business rescue. General moratorium results in the enforcement of claims against the company, or property belonging to the company, or that is within its legal possession to be temporarily prohibited and suspended for the entire duration of the business rescue.[95] These legal provisions will only be allowed to be heard in any other forum with the written consent of the practitioner or with the leave of court and in accordance with any terms the court considers suitable. [96] Section 133 (3) provides that if any right or claim against the company is subject to a specific time period, the period during which the company is in business rescue will not be calculated.

It is important to keep in mind the great impact and consequences an indefinite business rescue can have on affected persons, especially creditors. [97] As discussed above, one of the legal consequences of business rescue is a general moratorium which has the effect of suspending

[88] S 133 of the Companies Act 2008. Also see Cassim (n 60) 878.
[89] S 134 of the Companies Act 2008.
[90] S 135 of the Companies Act 2008.
[91] S 136 of the Companies Act 2008.
[92] S 136(2) of the Companies Act 2008.
[93] S 137 of the Companies Act 2008.
[94] S 137 of the Companies Act 2008.
[95] Davis, Cassim, Geach, Mongalo , Butler, Loubser , Coetzee and Burdette (n 58). Also see Cassim (n 60) 879.
[96] S 133 (1) (a) and (b) of the Companies Act 2008.
[97] Wassman (n 5)37.

and prohibiting all legal proceedings to be commenced against the company.[98] Although this breathing space is vital for the company to rearrange its debts and to try and recuperate financially, it provides no relief whatsoever for the aggrieved party as the moratorium can potentially continue indefinitely. [99] Due to this disadvantage, it is suggested that the courts take this into consideration when they determine whether or not to grant an order in favour of business rescue. [100]

3 *LIQUIDATION PROCEEDINGS UNDER THE OLD COMPANIES ACT OF 1973.*

3.1. Winding-up (liquidation) of companies by means of a voluntary liquidation

A distinction needs to be made between a voluntary winding-up by the company's members and a voluntary winding-up by the company's creditors. The first case will apply in instances where the company was able to pay its debts and the members would appoint a liquidator to conclude the administration of the winding-up of the company.[101] In the latter case, a company was unable to pay its debt and a liquidator is nominated by the creditors. [102] In terms of section 349 of the Companies Act 1973 both cases can be initiated by a special resolution by the members of the company and then the resolution must be registered at the then Register of Companies. [103] Prior to the registration of the members' voluntary winding-up, the company must be able to pay all its debt in full. [104] In addition, before the process of voluntary winding-up may continue, security to the satisfaction of the Master must be provided for the payment of the debts of the company within a specific period, not extending twelve months, from the commencement of the winding up. [105] The Master must thereafter dispense with the security received. [106] This procedure is more time and cost friendly because the members control the process and there are no creditor's claims that need to be proved or meetings that need to be held. [107] Insolvency law also applies *mutatis mutandis* here. [108]Nagel[109] submits that when a company is clearly insolvent and unable to pay its debt, the members are still able to take a

[98]Wassman (n 5)37.
[99]Wassman (n 5)37.
[100] Wassman (n 5)37.
[101] S 350 of the Companies Act 1973.
[102] S 351 of the Companies Act 1973. See Nagel (n 53) 577. Also see Cassim (n 60) 918.
[103]In accordance with S 200 of the Companies Act 1973. Also see n 58 above 577.
[104] Sharrock, Smith and van der Linde (n 2) 252.
[105] Nagel (n 55) 577.
[106] Sharrock, Smith and van der Linde (n 2) 252.
[107]Sharrock, Smith and van der Linde (n 2) 252.
[108] Nagel (n 55) 577.
[109]Nagel (n 55) 577.

resolution to place the company in voluntarily winding-up by signifying it will be a creditor's winding-up.

As pointed out above, the voluntary winding-up of a company by its creditors will be used when a company is not able to pay all its debts[110]. This procedure bears a resemblance to winding-up proceedings by the court in that meetings of the creditors are held and the appointed liquidator is subject to the directions of the creditors who have proved claims.[111] This type of voluntary winding-up can be described as voluntary winding-up under 'creditors' supervision'. [112]

3.2. Winding-up (liquidation) of companies by means of a court order

In *Sibakhulu Construction (Pty) Ltd v Wedgewood Village Golf Country Estate (Pty) Ltd* [113] the court held that the court which will have jurisdiction to grant a winding-up order is the High Court having jurisdiction over the area in which the company has its registered address. It must be noted that if there is more than one registered address, the principal place of business will be used. [114]

Section 344 of the Companies Act 1973 sets out the grounds for winding-up a company by means of a court. For purposes of this dissertation and due to its limitations, only section 344(a), (f) and (h) will be discussed due to its relevance. Section 334(a) of the Companies Act 1973 provides that a court may wind up an insolvent company if the company has passed a special resolution to be wound up by the court.

Section 344(f) of the Companies Act 1973 states that a company may be wound up by the court if it is unable to pay its debts. [115]Section 345 of the Companies Act 1973 clarifies when a company is deemed to be unable to pay its debts. Section 345(1) (a) elaborates that when a company is indebted for at least a R 100 (not less) and a creditor has left a demand of payment at the company's registered office which the company still omitted to pay, secure or compromise the claim after three weeks of receiving the demand from the creditor[116]. In

[110]S 343(2) (a) of the Companies Act 1973. Also see Sharrock, Smith and van der Linde (n 2) 252.
[111] Sharrock, Smith and van der Linde (n 2) 253.
[112]Sharrock, Smith and van der Linde (n 2) 253.
[113] 2011 JDR 1565 (WCC) at par 21 and 23.
[114] S 23(3) (b) of the Companies Act 2008.
[115] Sharrock, Smith and van der Linde (n 2) 242.
[116] To deliver a demand of payment at the registered office of the company is peremptory and must be complied with, see *Afric oil (Pty)Ltd v Ramadaan Investments CC* 2004 (1) SA 35 (N) 44. See Sharrock, Smith and van der Linde (n 2) 242.

Hockly's [117] the term 'pay' is defined as the unconditional payment being made. Thus paying a lesser sum 'in full and final settlement' will not be sufficient in order to avoid liquidation. [118]Section 345 (1) (b) of the Companies Act 1973 provides a company will be deemed unable to pay its debts if an issued warrant for execution on a judgment against the company has been returned by the sheriff reporting that there are no disposable property sufficient to satisfy the judgment, or the disposable property he sold did not satisfy the debts of the company. Section 345 (1) (c) of the Companies Act 1973 states if it has been proved to the satisfaction of the court that the company is unable to pay its debts , then this can be accepted. [119] It was held in *Helderberg Laboratories CC & others v Sola Technologies (Pty) Ltd* [120] that the source of the payment is irrelevant, therefore a bid from another person or company besides the company whom is liable to pay the debt can be accepted but its liability to pay the debt must be taken into consideration.

Lastly, section 344 (h) of the Companies Act 1973 provides for the ground when the court finds the winding-up of a company just and equitable. It should be noted that the court does not regard this ground as a "catch-it-all" phrase when dealing with the winding-up of a company. *Hockly's* [121] provides a handful of instances in which the court would consider it just and equitable to wind up a company. The first instance is where the main objective of the company is not possible to accomplish. In *Apco Africa (Pty) Ltd & another v Apco Worldwide Inc* [122]due to a deadlock between the company and its shareholders, the court concluded to wind up the company. The reason for this decision was that the company existence depended on the shareholders referring work to it but, due to the deadlock, this had not been done, resulting in the disappearance of the company's main object. [123] The second instance is where a company's objects are illegal or the motive behind why the company was formed was to defraud the persons invited to subscribe for shares. [124] The third instance is when "there is a justifiable lack of confidence in the conduct and management of the company's affairs." [125] The lack of

[117] Sharrock, Smith and van der Linde (n 2) 242.
[118] See *Body Corporate of Fish Eagle v Group Twelve Investments (Pty) Ltd* 2003 (5) SA 414 (W) at par 13.
[119] It is submitted that when the court is deciding if a company is unable to pay for this debts, it must also consider the contingent and prospective liabilities of the company.
[120] 2008 (2) SA 627 (C) at par 16.
[121] Sharrock, Smith and van der Linde (n 2) 243.
[122] 2008 (5) SA (SCA) at par 29.
[123] Sharrock, Smith and van der Linde (n 2) 244.
[124] *Cuninghame & another v First Ready Development 249 (Association incorporated under section 21)* 2010 (5) SA 325 (SCA at par 35), the court wound up a company incorporated as an association because the real purpose of the company was to conduct a commercial business for gain.
[125] Sharrock, Smith and van der Linde (n 2) 244.

confidence must be related to the conduct of the directors in carrying out the company's affairs. [126]

It must be submitted that court may also wind up a company if it is clear that there is no reasonable prospect of the proposed business rescue proceedings succeeding. In such a case, the court will reject granting an order for business rescue to commence and will make an alternative order which includes making an order for winding-up the company.[127]

3.2.1 Consequences of liquidation

3.2.1.1. Commencement of winding-up

Determining the exact time of when the liquidation of a company will commence is important due to the effect this procedure will have on the company, such as causing a number of consequences to be initiated. [128] Section 348 of the Companies Act 1973 provides that "at the time of the presentation to court of the application for the winding-up" the liquidation procedure is deemed to have commenced. A presentation of an application takes place when the papers are appropriately lodged with the Register of the court. [129] It was held in *First National Bank Ltd v E U Civils (Pty) Ltd; First National Bank (Pty) Ltd v E U Plant (Pty) Ltd; Bassett v EU Civils (Pty)Ltd; E U Holdings (Pty) Ltd v E U Plant (Pty) Ltd*[130] if two or more applications were made, the winding-up of the company will be deemed to have commenced once any one of the applications are lodged with the Registrar of the court, irrespective if the security with regards to the application was lodged first. [131] Unlike the winding-up of companies by means of a court order, voluntary winding-up of an insolvent company, as provided for in terms of section 352(1) of the Companies Act 1973, commences when the special resolution of the members is registered with the commission. [132]

[126]Sharrock, Smith and van der Linde (n 2) 244. For more illustrations on when the court have held it will be just and equitable to wind up a company see Sharrock, Smith and van der Linde (n 2) 244.
[127] S 131 (4) (b) of the Companies Act 2008. See *Oakdene Square Properties (Pty) Ltd & Others v Farm Bothasfontein (Kyalami) (Pty) Ltd & Others*) (609/2012) [2013] ZASCA 68 (27 May 2013) and *Newcity Group Limited (Pty) Ltd v Allan David Pellow N.O and Others* (577/2013) [2014] ZASCA 162(1 October 2014) below.
[128]Sharrock, Smith and van der Linde (n 2) 254.
[129] See Sharrock, Smith and van der Linde (n 2) 253.Also see *Nel & others NNO v The Mater & others* 2002 (3) SA 354 (SCA).
[130] 1996 (1) SA 924 (C) at par 929 D/E/F/G & 929 G/H/I.
[131] See Sharrock, Smith and van der Linde (n 2) 253.
[132]See *Botha & others NNO v Van Heerden NO & others* (unreported, GNP case no 40406/12, 23 July 2012.)

3.2.1.2. Legal consequences of winding-up (liquidation)

Section 359 (1) (a) of the Companies Act 1973 states that all civil proceedings by or against a company will be suspended once the special resolution for the voluntary winding-up of a company has been filed or a winding-up order by the court is made. [133] This stay of proceedings will continue until a liquidator has been appointed. [134] In *King Pie Holdings (Pty) Ltd v King Pie (Pinetown) (Pty) Ltd; King Pie Holdings (Pty) Ltd v King Pie (Durban) (Pty) Ltd* [135] it was held that an application for the winding-up of a company is not considered as a civil proceeding and for that reason such applications will still be allowed even if an application for a resolution for the voluntary winding-up of a company has been registered. Section 359 (1) (b) of the Companies Act 1973 advises that no attachment or execution orders may be enforced against the company; if this has been done it will be void.

Therefore after a liquidator has been appointed, all civil proceedings may carry on as before against the company, but the litigant must within four weeks of the liquidator's appointment provide the liquidator with at least a three weeks' notice in writing before continuing with the proceedings[136] .

Accordingly, after discussing both the business rescue and liquidation proceedings, it appears that due to the supporting and yielding nature of business rescue proceedings (it aims to offer support to financially distressed companies) there will always be the risk that companies with no actual prospect of financial recovery may abuse business rescue proceedings. Companies all too often try and make use of business rescue with the sole purpose of obtaining a temporary respite from creditors in mind. [137] Section 7 (k) of the Companies Act 2008 embodies one of the objects of the Companies Act 2008 providing "for the efficient rescue and recovery of financially distressed companies, in a manner that balances the rights and interests of all relevant stakeholders." It is for this reason that section 7(k) of the Companies Act 2008 will be used by the court for guidance when adjudicating matters. [138] As a result of section 7(k) in

[133] See *Richard Keay Pollock NO v North Copper Wire (Pty) Ltd* [2002] 1 ALL SA 244 (T) as read in Sharrock, Smith and van der Linde (n 2) 255.
[134] S 359 (1) (a) of the Companies Act 1973.
[135] 1998 (4) SA 1240 (D) at 1247C and 1248 H as read in Sharrock, Smith and van der Linde (n 2) 255.
[136] Civil proceedings in this context would include execution proceedings commenced with before the initiation of the winding-up order as read in Sharrock, Smith and van der Linde (n 2) 255. S 359 (2) of the Companies Act 1973 as read in Sharrock, Smith and van der Linde (n 2) 255.
[137] Sharrock, Smith and van der Linde (n 2) 275. See *Swart v Beagles Run Investments 25 (Pty) Ltd (Four Creditors intervening)* 2011 (5) SA 422 (GNP).
[138] *In Newcity Group (Pty) Ltd v Pellow NO and Others, China Construction Branch v Crystal Lagoon Investments 53 (Pty) Ltd and Others* (GSJ) (unreported case no 12/45437, 16566/12, 28-3-2013) the court addressed this

the Companies Act 2008 the court in *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 Ltd* [139] interpreted this section to indicate that business rescue should be preferred to liquidation proceedings, but only where there is an authentic possibility of achieving the aims of the companies act 2008. [140] Despite highlighting the fact that there must be an authentic possibility for the aims of the act to be achieved companies, however, still try their luck in applying for business rescue orders hoping to take advantage of the vague and ill-structured provisions of chapter 6. This approach was clearly witnessed in the matter of *Oakdene Square Properties* [141] which will be discussed in detail below. A comparison between the advantages of business rescue and liquidation proceedings below will clearly illustrate that both proceedings have their advantages and that the one procedure should not just be preferred over the other procedure but the facts of each case should rather be applied to the correct procedure. All the interests of each relevant stakeholder should also be taken into consideration and all these interests need to be balanced accordingly.

concept when asked to deliver judgments on competing applications for liquidations and business rescue. He stressed that the Act favours business rescue over liquidation."

[139] See the *Southern Palace Investments 265* case (n 25) at par 21.

[140] The same conclusion was reached in *Van Niekerk v Seriso 321 CC & another* [2012] ZAWCHC 63 (20 March 2012). Also see Sharrock, Smith and van der Linde (n 2). 275.

[141] See the *Oakdene Square Properties* case (n 14).

CHAPTER 3:
A CRITICIAL ANALYSIS OF THE ADVANTAGES OF BUSINESS RESCUE AND LIQUIDATION PROCEEDINGS COMPARED

1. *INTRODUCTION*

It is no secret that business rescue proceedings are corporate companies' favourite process as opposed to its alternative- winding-up the company. The Companies Act of 2008 has also made its preference- business rescue, clear and the courts have adjudicated relevant matters in a similar manner, interpreting the objects of the Companies Act 2008 in a manner giving means to the preference. Since business rescue's introduction, there have been multiple publications and judgments delivered regarding the advantages that business rescue proceedings hold that liquidation proceedings do not. Loubser[142] made very interesting, as well as persuasive, observations regarding the frequently talked about advantages of business rescue which will be discussed in more detail below.

2. THE ADVANTAGES OF BUSINEES RESCUE AND LIQUIDATION PROCEEDINGS

2.1. Business rescue does not hold the same negative stigma as liquidation

An alleged advantage coupled with business rescue is that it does not carry the same negative stigma as liquidation proceedings does. It is said that business rescue is viewed as a more acceptable option than liquidation and therefore directors will have more of an incentive to initiate business rescue proceedings because the company will stand a better chance of being rescued.[143] There are some misconceptions about this. Loubser [144] recorded in her article that the majority of insolvency practitioners based in England preferred to "sell a company's business by way of a pre-packaged agreement before the formal commencement of administration" because directly after formal proceedings have been initiated, it immediately has a negative effect on the goodwill of the business, further decreasing the price that a

[142] Loubser "Tilting at windmills? The quest for an effective corporation rescue procedure in South African law" 2013 *SA Merc LJ* 437 447.
[143] Loubser (n 143) 447.
[144] Loubser (n 143) 452 referenced Vanessa Finch *Corporate Insolvency Law: Perspectives and Principles* 2 ed (2009) 372 and 457 in her article when referring to the English version of business rescue.

purchaser is willing to pay. [145] Therefore, regardless whether if the formal proceedings are liquidation or business rescue, the reputation and creditworthiness of the company will still be affected. [146]

Abuse of the business rescue proceedings can also cause successful and solvent companies to be prejudiced by companies in business rescue. A company in business rescue operates without paying interests, it does not depreciate and there are no ongoing legal proceedings. As a result, the company is able to market at a cheaper rate which can drive financially sound companies into the ground as well as insolvency. [147] This result has highly detrimental and damaging consequences, not only for solvent companies, but also for our economy. It is of the utmost importance that business rescue only applies to companies in financial distress which have a genuine potential to survive. [148]

This principle is clearly illustrated in the *Oakdene Square Properties* case. [149] In this matter, the court was faced with the task of balancing the interests of the creditors and the company in order to decide whether a business rescue application should be granted or not. [150] The court

[145] Loubser (n 143) 452. Administration proceedings in England are the equivalent to business rescue proceedings in South Africa.
[146] Loubser (n 143) 453.
[147] Loubser (n 143) 453.
[148]Loubser(n 143) 453. It was recorded in *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 Ltd* 2012 (5) SA 515 (GSJ) before any business rescue plan can succeed, the plan must give due consideration to " the cause of the demise or failure of the company's business and offers a remedy therefore that has a reasonable prospect of being sustainable".
[149] The facts of this case are as follows: The company (Farm Bothasfontein (Kyalalmi) (Pty) Ltd) defaulted on payments to certain creditors (par 11). The company applied to the court in order to grant them an application in favour of business rescue (par 12). It was however, alleged by the respondents (Nedbank Limited and Imperial Holdings Limited, who were majority shareholders and creditors) based on their past financing transactions with the company that Farm Bothasfontein (Kyalalmi) was just making use of business rescue proceedings to avoid being placed under liquidation, raising the question, if they have a reasonable prospect of being rescued (par 15,16 and 17). Furthermore, the application was initiated by making use of s 131 of the Companies Act 2008 and one of the directors of the company approached the court with this application. The respondents disputed the director, Mr. Dimetrys Theodosiou, as well the director's brother, Mr. Antonys Theodosiou, and Oakdene Square Properties' Locus Standi to bring the application (Par 3.1, 3.2 and 3.3 of the court *a qou's* judgment and was confirmed by the SCA in par 13 and 14). The court however did not adjudicate on this point because the second applicant, Educated Risk Investment 54 (Pty) Ltd qualified as an affected person and could therefore bring an application in terms of s 131 (par 12). The two respondents were two significant shareholders in the company and therefore qualified as affected persons and creditors of the company, stating that they would reject any business rescue proposal made by the practitioner motion due to having sixty percent vote (par 10). This resulted in a deadlock between the directors and the shareholders of the company and the court was then asked to decide if the company could qualify for business rescue (par1). The High Court dismissed the business rescue application and the applicant's appealed (par 1).
[150]Bradstreet (n 47) 45. Also the duty of a court to weigh up the interests of the creditors against the interests of the company was confirmed in *Swart v Beagles Run Investments 25 (Pty) Ltd and Others (Four Creditors intervening)* 2011 (5) SA 422 (GNP) at par 29 when Makgoba, J stated that '[w]here an application for business

came to the conclusion that it was clear, based on the facts presented to them, that the company was not be able to discharge the first purpose of a business rescue application- to rescue the company from its financial turmoil.[151] Therefore, this application was based on the secondary goal provided for in business rescue provisions-securing a better return for the company's creditors.[152] The main question that arose, was whether the requirement of rescuing the company as contemplated in section 134(4) (a) was satisfied, as it is clear from the outset that the company could never be saved from immediate liquidation and that their only hope was for a better return, the court verified that the requirement must be satisfied. [153] The meaning of a "reasonable prospect" was also addressed by the court. [154] It was held that while the applicant did not have a detailed business rescue plan, as this can be left up to the practitioner after a proper investigation in terms of section 141, it must establish grounds for the reasonable prospect achieving one of the two goals in section 128(1) (b). [155]

The High Court judge, CJ Claassen, in the *Oakdene Square Properties* [156] matter referred to S131(4) of the Companies Act of 2008 in par 16 of his judgment and drilled into the meaning of the term a 'reasonable prospect for rescuing a company' in par 19. Judge Claassen applied the dictum of the Judge Eloff AJ [157] finding that 'reasonable prospect' requires '*something less than that the recovery should be a reasonable probability*'. [158] According to the Supreme Court of Appeal's judgment Brand JA interpreted the meaning of 'a reasonable prospect' as follows:

> I believe it requires more than a mere prima facie case or an arguable possibility. Of even greater significance, I think, is that it must be a reasonable prospect with the emphasis on 'reasonable' – which means that it must be a prospect based on reasonable grounds. A mere speculative suggestion is not enough". [159] "Self-evidently it will be neither practical nor prudent to be prescriptive about the way in which the appellant must show a reasonable prospect in every case"[160]. "But the applicant must establish

rescue...entails the weighing-up of the interests of the creditors and the company the interests of the creditors should carry the day.'

[151] Par 34. Also see s 128(b) of the Companies Act 2008.

[152] Par 34.

[153] Par 23. The court also made reference to an Australian matter, *Dallinger v Halcha Holdings* , 1996 14 ACLA 263 which held that even if the company has no likelihood of continuing its existence as a solvent company, business rescue may still be used if it can secure a better return for the creditors. The respondents however, contended that a better return is not possible and the court agreed at par 24. Also see chap 2, par 2.1.1 above regarding s 131(4) (a) of the Companies Act 2008.

[154] Par 29.

[155] Par 31.

[156] See the Oakdene Square Properties Case (n 14).

[157] As read in the *Southern Palace Investments 265* case (n 25).

[158] Par 19 of the *Oakdene Square Properties* [2012] 2 ALL SA 433 (GSJ) case.

[159] Par 29 of the *Oakdene Square Properties* case (n 14).

[160] Par 30.

> grounds for the reasonable prospect of achieving one of the two goals in s 128(1) (b). [161]

In *Propspec Investments* (*Pty*) *Ltd v Pacific Coast Investments 97 Ltd and Another* [162] the court concluded the following regarding a reasonable prospect:

> "it is not appropriate to attempt to set out general minimum particulars of what would constitute a reasonable prospect in this regard" and "to require, as a minimum, concrete and objectively ascertainable details of the likely costs of rendering the company able to commence or resume its business and the likely availability of the necessary cash resource in order to enable the company to meet its day to day expenditure or concrete factual details of the source, nature and extent of the resources that are likely to be available to the company, as well as the basis and terms on which such resources will be available, is tantamount to requiring proof of a probability and unjustifiably limits the availability of business rescue proceedings." [163]

As to what is meant by "reasonable prospect", the Court stated:

> "In my view a prospect in this context means an expectation. An expectation may come true or it may not. It therefore signifies a possibility. A possibility is reasonable if it rests on a ground that is objectively reasonable. In my judgment a reasonable prospect means no more than a possibility that rests on an objectively reasonable ground or grounds." [164]

Finally, the High Court and Supreme Court of Appeal inferred the following meaning of a reasonable prospect in *Newcity Group (Pty) Ltd v Pellow NO and Others, China Construction Branch v Crystal Lagoon Investments 53 (Pty) Ltd and Others:* [165]

> If objectively there is a possibility or likelihood of those uncertain future events (with reference to the eventual rescue of the company or a better return) occurring, the jurisdictional requirements have been satisfied, and the court can exercise its discretion." [166]

Although Van Eeden AJ agreed with the guidelines laid down by Eloff AJ in *Southern Palace*, he also agreed with Van der Merwe J that the bar must not be placed too high. According to Van Eeden JA a suitable test:

> should be flexible and the circumstances of each case will determine whether viable facts give rise to a reasonable prospect or not" and "speculation cannot create a reasonable prospect. [167]

---

[161] Par 31.
[162] 2013 (1) SA 542 (FB).
[163] Par 13.
[164] Par 12.
[165](GSJ) (unreported case no 12/45437, 16566/12, 28-3-2013.
[166] Par 14.
[167] Par 14.

The Supreme Court of Appeal[168] found that a court may not grant an application for business rescue unless there is a reasonable prospect for rescuing the company. In other words, facilitating its rehabilitation so that it continues on a solvent basis or, if that is not possible, yields a better return for its creditors and shareholders than what they would receive through liquidation. The Newcity Group failed to establish a prospect based on reasonable grounds that business rescue would return Crystal Lagoon to solvency or that it would provide a better return for its creditors and sole shareholder (The Newcity Group) than what liquidation would offer. [169]

Therefore, based on the on the interpretations of the above discussed case law, it can be said that a "reasonable prospect" seems to be interpreted by our courts as holding a lower standard than judicial management's "reasonable probability". [170] I concur that this conclusion is the correct one. Due to the high standard of proof expected of financially ailing companies when attempting to aid themselves back to solvency under the judicial management regime, the majority of the companies fell vastly short of this unrealistic standard. By lowering the bar to an achievable standard, candidate companies are able to prove that either one of the two goals provided for will cross the threshold for obtaining a business rescue order. [171] In addition to proving either one of these two goals, it must be noted that when a court is considering whether an applicant has successfully discharged a business rescue application on the basis of the company being able to be rescued on a 'reasonable prospect', the emphasis must not be on *prospect* alone, but on *reasonable* as well. Consequently, a prospect must be based on reasonable grounds set out by the appellant. [172] The court makes it clear that there is no practical formula for an applicant to apply in every matter in order to show a reasonable prospect. In actual fact, the court strives to apply a flexible test to the unique circumstances of each case and encourages an applicant to discharge one of the two purposes set out in section 128(1) (b) of the Companies Act. Once this has been achieved, grounds for the reasonable prospect of rescuing the company would have been established. It can be deduced from the case law above,

[168] *Newcity Group Limited (Pty) Ltd v Allan David Pellow N.O and Others* (577/2013) [2014] ZASCA 162(1 October 2014).
[169] Par 23.
[170] The court also made reference to an analysis of Loubser *(*n 21)71, regarding a 'reasonable prospect' stating that it will be a 'disastrous for the new procedure' if the same if the same high threshold test used for a judicial management order of "reasonable probability" to is be applied to this provision- par 19 in the court *a quo's* judgment.
[171] S 128(1) (b) of the Companies Act 2008.
[172] Par 29.

that a reasonable prospect needs to be determined and based on an objectively reasonable ground. An applicant needs to take this into consideration and ensure that an objectively reasonable ground exists in their founding papers before applying for business rescue. The courts make it abundantly clear that a mere speculation of a reasonable prospect when rescuing the company will not be sufficient and will not be tolerated. [173]

2.2. The employees' contracts are protected and post-commencement finance will be regarded as preferential claims with a super-preferential status

Another advantage that is associated with the use of business rescue is that it preserves jobs and protects the interests of the employees. [174] The first problem with this theory is that companies tend to retrench people at the first signs of trouble, which might be long before the boat actually starts to sink. [175] Also, the promise cannot apply to all employees simply because certain retrenchments are inevitable- the company is suffering financially and is forced to cut back on certain costs in order to survive its financial depression.

Should a company chose to not make use of business rescue but rather liquidation section 38 (2) of the Insolvency Act [176] states that all contracts of service with its employees are automatically suspended. [177] Therefore, the suspended contracts will only terminate 45 days after the date of appointed of the final liquidator, although is it worth noting that employees who have concluded an agreement with the liquidator regarding the continued employment at

[173] It has been provided that business rescue proceedings do not make provision to directly transition into the winding-up of the company after the proposed business plan has been rejected, as is in Australia (n 3 above 132). According to the Australian provisions, liquidation is provided as a more direct alternative for creditors as oppose to proposals for an alternative plan (Anderson (n 3) 132). In *Creevey & Another v Deputy Commissioner of Taxation* (1996) 19 ACSR 456 the court held the following, "The question of whether an administration should continue, rather than that there be a winding up, is obviously closely related to the further question of whether the creditors could hope to get more by way of payment of their debts from one form of process or administration than from the other. In order to satisfy the court of the matter referred to in s 440A (2) of the Corporations Law, one would expect that there would have to be some persuasive evidence to enable it to be seen that there were assets which, if realised under one form of administration rather than the other, would produce a larger dividend, or at least an accelerated dividend for the creditors." (as read in Hunt and Handa (n 4)15-16). This type of attitude towards liquidation could combat the negative stigma attached to liquidation procedures, something the South African regime is also battling with and struggling to shake off. Therefore, another possible recommendation advocating for the improvement of the South African business rescue proceedings could be to include a provision that would directly facilitate the transition from a rejected business rescue plan to the winding-up of the company (Anderson (n 3) 132).

[174] Loubser (n 143) 450.

[175] Loubser (n 143) 450.

[176] No. 24 of 1936.

[177] This means that employees does not have to render their services and are not entitled to any remuneration.

the company will be exempt from this section. [178] Business rescue, on the other hand, provide in section 136 (1) (a) and section 136 (2) of the Companies Act 2008 that the…

> employee of the company will continue to be employed on the same terms and conditions as before the beginning of the business rescue...employment contracts are specifically excluded from the business practitioner's power to suspend or apply to court for the cancellation of any agreement or part thereof to which the company is a party.

Furthermore, employees' remuneration, reimbursements and other payments that become due and payable during business rescue proceedings will receive a preferential claim in terms of its ranking and will be considered as post-commencement finance. [179] This approach is worthy of praise but is not without fault unfortunately. Firstly, employees are protected in terms of sub-sections 197 and 197A of the Labour Relations Act[180] which provide that the "employment contracts are automatically transferred to the new owner of the business, even those contracts that have been already terminated as a result of the company's liquidation." [181] However, the fact that an interested buyer looking to purchase the business might not want to run the risk of taking over the undisclosed obligations and liabilities of the previous owner towards his employees cannot be overlooked. [182] The interested buyer might, for this reason alone, opt to rather purchase the business from a company that is liquidating, purely because he will be able to purchase the business and start running it on a 'clean slate' without having to take over any liability claims the employees might have had against the previous owner. Secondly, the employees will be in a beneficial position if the company can obtain a post-commencement investor because this would mean their due and payable remuneration, reimbursements and other payments receive a super-preference claim in terms of its ranking. This trick, however, lies in actually being able to obtain post-commencement finance. The company is normally in no position to offer security to the investor due to the financial stress it is under, so there is absolutely no guarantee that the investor will get their money back[183] Loubser [184] therefore phrases the next question perfectly: "Who will be prepared to finance the company knowing

[178] s 38 (9) of the Insolvency Act.
[179] See the obiter remark in *Merchant West Working Capital Solutions (Proprietary) Limited v Advanced Technologies & Engineering Company (Proprietary) Limited & Gainsford* (Unreported, Case No 2013/12406) at par 21. In this judgment the court sets out in no uncertain terms the ranking order of creditors' claims during the business rescue proceedings.
[180] No. 66 of 1995.
[181] Loubser (n 143) 451.
[182] Loubser (n 143) 448.
[183] Loubser (n 143) 451.
[184] Loubser (n 143) 451.

that not only must this money be used to pay the employees first, rather than improving the profitability of the company, but should the company end up in liquidation, the employees will retain this preference for their unpaid claims over the investors preference to get their money back?" Unfortunately, the odds are stacked against this prospect. [185]

2.3. Selling the business as a going concern under business rescue will result in a higher price being realized than liquidating the company.

As discussed above, if the primary aim of business rescue cannot be maintained then an accepted secondary goal or alternative purpose for making use of business rescue is to secure a better return for company's creditors or their shareholders. [186] However the hypothesis that if a company cannot be saved from their insolvent state selling the business or part of it as a going concern will always result in a higher price than it would after a company has been placed into liquidation is not an accurate observation of the facts. [187] In her article, Loubser [188] points out that it is often argued that a liquidator is an expert in breaking up a business and selling it off in bits and pieces whereas business practitioners, on the other hand will carry on managing the business until a purchaser is found. [189] Loubser [190] states that there is adequate proof that should a viable business or parts of a business still exist when a liquidator is appointed, the liquidator will normally try to sell the business as a going concern. Section 386 (3) – (4) of the Companies Act 1973 provides a liquidator with the explicit statutory power to continue to run a business until it is sold after obtaining the permission of the creditors.

Furthermore, it is important for creditors to also take note of the fact that business rescue practitioner's remuneration is not specifically mentioned and therefore not regulated in the Companies Act 2008. As a result, there is no independent control over the fees, costs and

[185] A point of divergence between the two respective jurisdictions is the provisions regarding the position of employees in terms of the rescue proceedings. South African business rescue provisions are clear and suggest that employee's positions within the company will be protected (see chapter 3, paragraph 2) whereas Australian provisions create no special proviso dealing with employees (Anderson (n 3) 119-120). Anderson (n 3) 120) suggests that the visible difference between the two jurisdictions could point to the difference in social structures and conditions present in the respective jurisdictions.

[186] S 128 (1) (b) (iii) of the Companies Act 2008.

[187] Loubser(n 143).

[188] Referred to Sandra Frisby 'Pre-packaged Administrations: Progress Report to the Association of Business Recovery Professionals' (March,2008) 2 ,available at http://www.iiiglobal.org/component/jdownloads/finish/337/4137.html, accessed on 31 August 2013, who made use of statistics showing that almost 50 per cent of company administrations in England involved a sale as a going concern. However, in about 77 per cent of these cases, there was nothing left for distribution to unsecured creditors." at Loubser (n 143).

[189]Loubser (n 143) 448.

[190] Loubser (n 143) 448.

expenses of the practitioner. In other words the practitioner can have an extremely (almost excessive) high daily rate and it cannot be labelled as wrong because there are no provisions in the Act regulating potential excessive and abusive practitioner rates. [191] It can be held that once more clarity and regulatory provisions are implemented regarding the practitioner's fees and costs, the creditors and other stakeholders of the relevant company might consider initiating business rescue more seriously. Creditors, in particular, can be reluctant to appoint a practitioner due to there being no independent control over the fees asked. No independent control over the practitioner's fees can drain the last bit of the company's capital that was meant to compensate the creditors' claims against the company.

Section 135 of the Companies Act 2008 provides the ranking of claims of creditors during the business rescue proceedings. The Act ranks the practitioner's unregulated remuneration fees as first on the ranking list taking preference over all the claims proved against the company and thereafter, the ranking fees of the employees, which become due and payable after the commencement of business rescue. [192] The problem with this principle is that, after paying these preference claims, how much of the additional amount, after having sold the business as a going concern, will be left for the payment to the creditors of the subsequent liquidation. [193] A company and creditors would not be faced with this dilemma had the company gone straight into liquidation. [194]

Applications for business rescue in South Africa has customarily been based on the perception that a "sale of assets or even a single sale of assets by a practitioner will be higher priced than a sale by a liquidator." [195] Our courts have strongly rejected this view and are of the opinion that there is absolutely no valid reason to hold this perception. This principle was boldly illustrated in the matter of *Oakdene Square Properties* case. [196] In the judgment delivered, the court expressed its dissatisfaction with the evidence put forward by the applicant to argue in

[191]Loubser (n 143) 448, fn 61. Also see *Oakdene Square Properties* case(n 14) the court found that business rescue proceedings would be unsuitable because there are no provisions for the taxation of the practitioner's fees but there are for the taxation of the liquidator (Par 49.3 of the court a quo's judgment and the SCA confirmed this in par 34). This provides more independent control over the costs of liquidation than over the costs of business rescue (Par 49.3 of the court a quo's judgment and the SCA confirmed this in par 34).

[192] S 135 (3) (a) of the Companies Act 2008. See Barnett and Levenstein "Where you stand in the business rescue queue" 2013 *Without Prejudice* 10-11.

[193] Loubser (n 143) 448.

[194]Loubser (n 143) 448.

[195] Loubser (n 143) 448.

[196] Par 34. Also see Bradstreet (n 47) 44-45.

favour of the granting of the business rescue application. [197] On the contrary, in this *casu* the court found that it was not convinced that the practitioner would secure a better return for the company's creditors than that of the liquidator, meaning that business rescue proceedings would ultimately be inappropriate and ineffective in this matter. [198] Therefore, the court dismissed the business rescue application and ordered that the company in question be placed into final liquidation.

[197] Par 49(1) court *a quo's* judgment and confirmed by the SCA in par 34.
[198] Par 49(1) court *a quo's* judgment and confirmed by the SCA in par 34.

CHAPTER 4: CONCLUSION

Although Chapter 6 of the Companies Act 2008 holds many advantages and is indeed a major step in the right direction compared to the very stringent requirements of judicial management which made it nearly impossible for companies to qualify for it and contributed to its severe failure, business rescue provisions definitely still call for serious revision, modification and improvement. Due to the confusion and uncertainties caused by the provisions, abuse has crept in and companies have caught a whiff of this, trying their luck at every curve of the corporate insolvency racetrack. The main form of abuse of business rescue proceedings seen thus far is companies applying for business rescue order with no other intention in mind other than buying more time for the company. In return, the party that suffers the most is the company's creditors- becoming frustrated and impatient with the entire system, having to fight for and claw back money that is rightfully theirs in the first place and making them resentful toward the procedure. Business rescue proceedings is a revolutionary concept but will never be recognised for its full potential until it is implemented properly.

In conclusion, It is submitted that Loubser is correct in her observation regarding the advantages of the business rescue and liquidation proceedings compared. Due to the stigma attached to the liquidation of a company, the corporate milieu was relieved when judicial management was repealed and optimistic when chapter 6 containing business rescue was introduced. Unfortunately, this approach towards liquidation has caused financially distressed companies to wince at the very thought or slightest suggestion of winding up the company. As a result, the majority of companies who are experiencing financially choppy waters run for the business rescue lifejacket, even if the jacket does not fit. By applying business rescue incorrectly to matters in the hope that it would somehow assist a company that simply cannot be saved from its financial stresses results in nothing more than abuse of the system provided and frustration on the part of the creditors.

Applications for business rescue in South Africa has customarily been based on the perception that a "sale of assets or even a single sale of assets by a practitioner will be higher priced than a sale by a liquidator." [199] Our courts have strongly rejected this view and are of the opinion that there is absolutely no valid reason to hold this perception. This principle was boldly

[199] Loubser (n 143) 448.

illustrated in the matter of *Oakdene Square Properties* case. In the judgment delivered, the court expressed its dissatisfaction with the evidence put forward by the applicant to argue in favour of the granting of the business rescue application. On the contrary, in this *casu* the court found that it was not convinced that the practitioner would secure a better return for the company's creditors than that of the liquidator, meaning that business rescue proceedings would ultimately be inappropriate and ineffective in this matter

There is a definite need for both proceedings and I submit that the two can live harmoniously but, only if they are applied to the correct circumstances and in the correct manner. There are no grey areas here and there should never be any. Our law does not allow for uncertainty purely because it creates confusion. I further submit, with regret, that chapter 6 of the Companies Act 2008 does create confusion due to its vague and ill-worded provisions.

BIBLIOGRAPHY:

1. Books:

Cassim F, Cassim, M, Cassim R, Jooste R, Shev J and Yeats J *Contemporary Company Law* Juta South Africa (2012)

Davis D, Cassim F, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D *Companies and other business structures in South Africa* Oxford University Press Southern Africa (2012)

Finch V *Corporate Insolvency Law: Perspectives and Principles* 2 ed (2009) 372 and 457

Kunst J *Henochsberg on the Companies Act No 71 of 2008* Lexis Nexis Databasis updated (2011)

Meskin PM *Insolvency law* Lexis Nexis Databasis updated (2014)

Nagel CJ *Commercial law* Lexis Nexis South Africa (2011)

Sharrock R, der Linde K and Smith A *Hockly's Insolvency Law* Juta South Africa *(*2012)

2. Case law:

South African Case Law:

ABSA Bank v Rhebokskloof (Pty) Ltd & Others 1993 (4) SA 436 (C)

Advanced Technologies and Engineering Company (Pty) Ltd (in business rescue) v Aéronautique et Technologies Embaraquees SA and Others (GNP) (unreported case no 72522/11, 6-6-2012

Afric oil (Pty)Ltd v Ramadaan Investments CC 2004 (1) SA 35 (N) 44

AG Petzetakis International Holdings Ltd v Petzitakis Africa (Pty) Ltd & others (Marley Pipe Systems (Pty) Ltd & another intervening) 2012 (5) SA 515 (GSJ)

Apco Africa(Pty) Ltd & another v Apco Worldwide Inc 2008 (5) SA (SCA).

Body Corporate of Fish Eagle v Group Twelve Investments (Pty) Ltd 2003 (5) SA 414 (W).

Botha & others NNO v Van Heerden NO & others (unreported, GNP case no 40406/12, 23 July 2012

Climax Concrete Products CC t/a Climax Concrete Products CC v Evening Flame Trading 449 (Pty) and Others (ECP) (unreported case no 812/2012, 21-6-2012)

Commissioner, South African Revenue Service v Beginsel NO and Others 2013 (1)SA 307 (WCC)

Firstrand Bank Limited v Imperial Crown Trading 143 (Pty) Limited 2012 (4) SA 266 (KZD)

First National Bank Ltd v E U Civils (Pty) Ltd; First National Bank (Pty) Ltd v E U Plant (Pty) Ltd; Bassett v EU Civils (Pty)Ltd; E U Holdings (Pty) Ltd v E U Plant (Pty) Ltd 1996 (1) SA 924 (C)

HBT Construction and Plant Hire CC v Uniplant Hire CC 2012 (5) SA 197 (FB)

Helderberg Laboratories CC & others v Sola Technologies (Pty) Ltd 2008 (2) SA 627 (C)

Le Roux Hotel Management (Pty) Ltd & another v E Rand (Pty) Ltd (2001) 2 SA 427 (C)

Merchant West Working Capital Solutions (Proprietary) Limited v Advanced Technologies & Engineering Company (Proprietary) Limited & Gainsford (Unreported, Case No 2013/12406).

Nel & others NNO v The Mater & others 2002 (3) SA 354 (SCA)

Newcity Group Limited (Pty) Ltd v Allan David Pellow N.O and Others (577/2013)[2014] ZASCA 162(1 October 2014)

Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd and others; Farm Bothasfontein (Kyalami) (Pty) Ltd v Kyalami Events and Exhibitions (Pty) Ltd and others (609/2012) [2013] ZASCA 68 (27 May 2013)

Propspec Investment (Pty) Ltd v Pacific Coast Investments 97 Ltd and Another 2013 (1) SA 542 (FB)

Richard Keay Pollock NO v North Copper Wire (Pty) Ltd [2002] 1 ALL SA 244 (T)

Rosenbach & Co (Pty) Ltd v Singh's Bazaar (Pty) Ltd 1962 (4) SA 594 (D)

Sibakhulu Construction (Pty) Ltd v Wedgewood Village Golf Country Estate (Pty) Ltd 2011 JDR 1565 (WCC)

Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 Ltd 2012 (5) SA 515 (GSJ)

Standard Bank of South Africa Ltd v R-Bay Logistics CC 2013 (2) SA 295 (KZD)
Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 Ltd (2012) (2) SA 423 (WCC)

Swart v Beagles Run Investments 25 (Pty) Ltd (Four Creditors intervening) 2011 (5) SA 422 (GNP)

The Employees of Solar Spectrum Trading (Pty) Ltd v Afgri Operations Ltd and Another; In re *Afgri Operations Ltd v Solar Spectrum Trading (Pty) Ltd* unreported Case nos. 6418/11, 18624/11, 66226/11 (GNP).

Van Niekerk v Seriso 321 CC & another [2012] ZAWCHC 63 (20 March 2012)

Van Staden vs Angel Ozone Products CC 2012 JDR 1945 (GNR)

International Case Law:

Creevey & Another v Deputy Commissioner of Taxation (1996) 19 ACSR 456

Dallinger v Halcha Holdings 1996 14 ACLA 263

3. Journal Article:

Anderson "Viewing the proposed South African business rescue provisions from an Austrlian perspective" 2008 *PER LJ* 104

Braatvedt K "Unscrambling the liquidation egg" 2013 *Without Prejudice* 36

Bradstreet R "Business rescue proves to be creditor-friendly: CJ Classen J's analysis of the new business rescue procure in *Oakdene Square Properties*" *SALJ* 44

Bradstreet R "The new business rescue: will creditors sink or swim?" 2010 *SALJ* 352

Bradstreet R "The leak in the Chapter 6 lifeboat: Inadequate regulation of Business Rescue Practitioners may adversely affect lenders' willingness and the growth of the economy" 2010 *SA Merc LJ* 195

Barnett L and Levenstein E "Where you stand in the business rescue queue" 2013 *Without Prejudice* 10

Frisby S 'Pre-packaged Administrations: Progress Report to the Association of Business Recovery Professionals' (March, 2008) 2, available at http://www.iiiglobal.org/component/jdownloads/finish/337/4137.html, accessed on 31 August 2013.

Girgis J "Corporate Reorganization and the Economic Theory of the Firm" in Jamis Sarra (ed) *Annual Review of Insolvency Law* (2010) 467

Hunt and Handa "A critical comparison between Australian and Canadian creditor protection regimes: Voluntary administration and CCAA" 2005 Available at SSRN 6-7

Joubert T "'Reasonable possibility' versus 'reasonable prospect': Did business rescue succeed in creating a better test than judicial management?" 2013 *THRHR* 550

Loubser A "Some comparative aspects of corporate rescue in South Africa" (2010 LLD thesis) University of South Africa 17.

Loubser A "Tilting at windmills? The quest for an effective corporation rescue procedure in South African law" 2013 *SA Merc LJ* 437

Loubser A "The business rescue proceedings in the Companies Act of 2008: Concerns and questions (part 1)" 2010 *TSAR* 501

Loubser A "The business rescue proceedings in the Companies Act of 2008: Concerns and questions (part 2)" 2010 *TSAR* 689

Rushworth J "A critical analysis of business rescue regime in the Companies Act 71 of 2008' 2010 *Acta Juridica* 375

Smyth S "Detecting 'red flags' early can help a business avoid severe financial distress" 2012 *Tax Professional* 26

Swanepoel J and Gopal C "An inacceptable business rescue mess" 2013 *Without Prejudice* 16

Utz C "Voluntary administration: The Australian experience" 2008 Available on http://www.claytonutz.com/docs/VoluntaryAdministration_TheAustralianExperience.pdf (visited 04 October 2014)

Wassman B "Business rescue-getting it right" 2014 *De Rebus* 36

4. Legislation:

South African Legislation:

Companies Act No. 71 of 2008

Companies Act No. 61 of 1973

Insolvency Act No. 24 of 1936.

Labour Relations Act No. 66 1995.

International Legislation:

Corporations Act 2001 (Cth)

Companies Act 1981 (Cth)

Word count: 15 517 (Excluding cover page, declaration, acknowledgements, summary, table of contents, bibliography)