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EXPLORING THE NOVEL CONCEPT OF BUSINESS RESCUE UNDER THE SOUTH AFRICAN COMPANIES ACT 71 OF 2008

DESSERTATION SUBMITTED IN FULFILMENT OF THE REQUIREMENTS OF THE LLM DEGREE AT THE UNIVERSITY OF VENDA

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SCHOOL OF LAW

SOUTH AFRICA

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(2017)

DECLARATION

I, **KUDZAI MPOFU**, student number 11625694 hereby declare that the dissertation for the LLM degree at the University of Venda, hereby submitted by me, has not been submitted previously for a degree at this or any other university, and that it is my own work in design and execution, and that all reference materials contained herein have been duly acknowledged.

STUDENT

Signature……. Date……..

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DEDICATION

To my brothers Rodwell and Mike Mpofu, the end of knowledge is character.

ACKNOWLEDGEMENT

I thank the Lord because it is through His providence that this work has become a success. Without His divine love and grace I would have lost hope and strength. But because He is faith to His word today I stand amongst the great.

A lot of appreciation and acknowledgment goes to my supervisors Prof A.O Nwafor and Adv Selala for their guidance and support in realizing this work. It is because of their urge to mentor and groom profound scholars that I was able to complete this work.

I wish to thank my brothers, Rodwell and Mike Mpofu, for their prayers and encouragement, may we continue to inspire and enable one another to achieve great things. There are so many people who worked behind the scenes to mention but a few; Saneliso Thambo, Keiven Sithole and Camp Mpasi. I hope you all realize how extremely important you are to me.

“If I have seen further it is by standing on the shoulders of giants” Sir Isaac Newton.

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ABSTRACT

Business rescue provisions are meant to assist a financially distressed company. It seems that the success of business rescue rests on three factors, namely a competent business rescue practitioner and a practicable business rescue plan; the consent and cooperation of shareholders and creditors. However, academics and case law point out concerns as to the regulation of the aforementioned essential ingredients. The purpose of this study is to ascertain the level of the efficacy of the Companies Act provisions on business rescue as contained in Chapter 6. The researcher compares the current business rescue regime and the previous judicial management procedure to find out how the current regime can be improved. Since the business rescue regime was adopted from other jurisdictions the researcher also compares the practices in some of those jurisdictions with that of South Africa to establish the goals and expectations of business rescue in modern corporate operations.

Keywords: Business rescue, judicial management, financially distressed company, rehabilitation, going concern, affected persons

CHAPTER ONE

1. INTRODUCTION

1.1 Brief Background

In a market-based economy, companies are susceptible to failure.[1] This, however, is not an indication of a failed economy but is actually recognised as an indication of a healthy economy.[2] If a company cannot compete in the marketplace, it is reasonable and acceptable that the company concerned be taken over by stronger companies or be wound up.[3] There are various causes of financial distress in companies; for example, factors in the company's spheres of operation, a demand of a particular product locally and abroad, poor marketing strategies or maladministration are all causes of financial difficulties. The failure of a company can rarely be attributed to a single factor.[4]

It is worth noting that companies in South Africa have become an essential component of the country's economy.[5] It is beneficial, therefore, to the economy of a state and its citizens to give a financially distressed company a second chance.[6] Cilliers and Banade are of the view that:

> A developing economy cannot lightly permit companies which help to comprise its industries and commercial enterprises to be dissipated by winding up and dissolution due to some temporary setback in cases where there is a reasonable probability that they would, if granted a moratorium, be able to overcome the difficulties, discharging their debts and become successful concerns.[7]

This can best be achieved by rehabilitating the company so that it can trade profitably and remain a stable and viable concern.[8] Where such assistance is not rendered, it is undeniable that there are negative consequences faced by both the state's economy and affected parties who have interests in the failing company.[9] The chain reaction from company failure can be potentially disastrous to shareholders, creditors,

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[1] D Davis, 'Business rescue proceedings and compromise' in W Geach, T Mongalo, D Butler, A Loubser, L Coetzee and D Burdette (ed) *Companies and other Business Structures in South Africa* (2013) 235.
[2] *Ibid*.
[3] *Ibid*.
[4] *Ibid*.
[5] R.S Dzvimbo, 'Should the Zimbabwean Companies Act Move Away From Judicial Management and Adopt Business Rescue?' Unpublished LLM Dissertation, University of Cape Town (2013) 1.
[6] *Ibid*.
[7] H.S Celliers and ML Benade, 'Judicial Management' in JJ Henning, JJ Du Plessis, PA Delport , LT Pretorius (ed) *Corporate Law* 3rd ed (2000) 478.
[8] F.H Cassim, 'Business Rescue and Compromises' in MF Cassim, R Cassim, R Jooste, J Shev, J Yeast (ed) *Contemporary Company Law* (2012) 863.
[9] *Ibid*.

employees and community that it must not be overlooked.[10] The demise of a company in addition to rendering people jobless and disgruntling creditors and shareholders and the society at large through loss of service delivery, also hugely disrupts the economy of the country.[11]

In the light of these observations, it is imperative for a state to have an effective business rescue regime that assists financially distressed companies.[12] The main objective of business rescue is to salvage companies and not to oversee their liquidation. If a company is successfully rescued or turned around, it follows that creditors will be paid, jobs will be saved and the company will be able to pay its taxes.[13] In *NLRB v Bildisco*[14], the court held that the fundamental purpose of business rescue or reorganization is to prevent a debtor from going into liquidation, the attendant loss of jobs and possible misuse of economic resources.

The South African business rescue regime is regulated by Chapter 6 of the Companies Act 71 of 2008. The Chapter 6 procedure is aimed at providing temporary measures to facilitate the rehabilitation of a financially distressed company.[15] In terms of Chapter 6, a business rescue practitioner must oversee the company's management and all legal proceedings against the corporation are stayed.[16] The rehabilitation or rescue itself is effected through a business rescue plan.[17] Under a business rescue plan, the company's affairs, property, debts and liabilities are restructured in a manner that maximizes the likelihood of the company continuing in existence on a solvent basis or if this is not possible, results in a better return for the company's creditors or shareholders than would result from the immediate liquidation of the company. This is in tandem with the Cork Report in the UK which emphasized that one of the aims of modern insolvency law is to diagnose and treat an imminent

[10] Dzvimbo (note 5 above) 1.
[11] Cassim (note 8 above) 863.
[12] S Conradie and C Lampretch 'Business Rescue: How can its success be evaluated at company level' (2015) Volume 19 Issue 3 *Southern African Business Review* 1.
[13] Cassim (note 8 above) 863.
[14] 465 US 513 (1983) 528.
[15] R Bradstreet, 'The leak in Chapter 6 Life boat: Inadequate Regulation of Business Rescue Practitioners May Adversely Affect Lenders' Willings and the Growth of the Economy' (2010) Volume 22 *South Africa Mercantile Law Journal* 195.
[16] *Ibid*.
[17] *Ibid* 196.

insolvency at an early rather than at a late stage.[18] The earlier a company reorganizes itself, the better the chances of success and avoidance of liquidation.[19]

1.2 Statement of Problems

Although the current provisions contained in Chapter 6 of the Companies Act 2008 have been welcomed as a vast improvement on the previous judicial management mechanism,[20] their success needs to be evaluated. The Companies and Intellectual Property Commission, requires that the success of business rescue legislation in South Africa must be monitored closely to ensure that South Africa sets an example not only nationally, but also internationally.[21]

The researcher is of the view that the success of the business rescue regime in South Africa will be predicated on a number of factors such as: competent business rescue practitioners, good business rescue plans, the consent and contribution of affected persons and a flawless business rescue procedure. Hence the study is intended to find out whether these essential ingredients are properly regulated and are in line with the objectives of business rescue. At present the success of business rescue is doubtful; the current framework for the business rescue regime in South Africa is far from settled as witnessed by the inconsistent and contradictory judicial opinions.[22] For instance, in *Advanced Technologies and Engineering Company Pty Ltd v Aeronautique et Technologies Embarquees SAS*[23] the court held that section 129 required full compliance with the prescribed procedural requirements in subsections (3) and (4) and did not provide for the possibility of mere substantial compliance being sufficient or for condonation of non-compliance. But the matter is far from settled because in Exparte *Van den Steen NO and South Gold Exploration (Pty) (Ltd)*[24] the court held to the contrary. It held that substantial compliance with the notification requirements is allowed by section 6 (9) of the Act. Such judicial inconsistency and contradiction does not create strong precedent and without precedent there would be no uniform application of the law. Furthermore, lawyers and academics have described some of the provisions as badly worded, incomplete

[18] Insolvency Law and Practice: Report of the Review Committee, Chairman Sir Kenneth Cork CBE (Cmnd 8558(1982)) cited by Cassim (note 8 *supra*) 862.
[19] Cassim (note 8 above) 862.
[20] Dzvimbo (note 5 above) 6.
[21] Conradie and Lampretch (note 12 above) 2.
[22] *DH Brothers Industries Pty Ltd v Gribnitz NO and Others* 2014 (1) SA 103 (KZP), *Africa Bank Corporation of Botswana Limited v Kariba Furniture Manufacturers Pty Ltd and others* 2013 (6) SA 471 (GNP).
[23] Unreported case no 72522/ 20110 (GNP).
[24] Unreported case no 3624/2013 (WCC).

and unclear.[25] This study, therefore, intends to examine the reliability and effectiveness of the Chapter 6 provisions as effective tools for rescuing financially distressed enterprises.

1.3 Hypothesis

The term hypothesis is conceived as supposition or proposed explanation made on the basis of limited evidence as a starting point for further investigation.[26] In other words, it is a proposition made as a basis for reasoning, without any assumption of its truth.

This work is based on the hypothesis that the winding up or dissolution of companies does not only affect persons with direct interest in the company, but has negative economic and social consequences. Therefore, an effective business rescue regime will not only guarantee the rehabilitation of a financially distressed company, but will also revive the company's influences on both the economic and social needs of the society. However, for a business rescue regime to be effective there must be competent business rescue practitioners, a good business rescue scheme and the cooperation of creditors, shareholders and employees.

1.4 Aim

The aim of the study is to examine the efficiency and efficacy of Chapter 6 of the Companies Act 71 of 2008 in ensuring the sustainability of corporate operations in South Africa.

1.5 Objectives

In pursuing the above aim, the researcher will address the following objectives:

- The importance of business rescue regime in ensuring the sustainability of the corporate enterprises.
- The protection of the rights and interests of stakeholders during the course of business rescue.
- The role of the business rescue practitioner in realising the essence of the business rescue as outlined in section 7 (k) of the Companies Act of 2008.

[25] Davis (note 1 above) 244.
[26] B Garner *Black's Law Dictionary* 8th ed (2004) 760.

1.6 Research Questions

The research hopes to answer the following questions:

- How does the business rescue regime revive the financially distressed companies?
- How is a balance of the interests of stakeholders maintained during business rescue?
- What are the roles of the business rescue practitioner in ensuring the sustainability of financially distressed companies?

1.7 Research Methodology

The study is a desktop-based research. The researcher will rely on information obtained from the library and on the internet. Thus, the study will refer to case law, textbooks, and national and international journal articles. The researcher will make use of the doctrinal approach. In this regard the primary source of information will be the Companies Act 71 of 2008. The researcher will objectively scrutinize the Act to find out the current provisions on business rescue and expose the gaps in the Act.

The South African business rescue regime was adopted from other jurisdictions; therefore, to clearly examine its efficacy the researcher will compare the South African business rescue regime with those of other jurisdictions such as the United States, Canada, Australia and United Kingdom.

In order to find out whether the Act properly regulates the office of the business rescue practitioner, the researcher will examine the responsibilities and qualifications of a business rescue practitioner. Furthermore, to establish whether the procedure to be followed under Chapter 6 is flawless, the researcher will discuss both South African and international case law and legislation. The current procedure will be compared with the previous procedure followed under judicial management.

1.8 Literature Review

Conradie and Lampretch examined how business rescue success can be evaluated internationally. Four international regimes were compared and a number of evaluation criteria were identified and examined in view of the goals of Chapter 6 of the South African Companies Act.[27] The investigation showed that the key indicators of a successful business rescue plan are the going concern status on existing business rescue and whether the return to creditors was maximised as opposed to

[27] Conradie and Lampretch (note 12 above) 1.

liquidation.[28] The researcher is of the opinion that the above indicators are not the only pointers of a successful business rescue. The study will reveal that business rescue is not only meant to profit creditors. Shareholders and employees must also be considered in evaluating the success of a business rescue plan. In other words, the researcher's work is intended to find a fair balance of the rights of affected persons during the implementation of business rescue plan.

Pretorius and Smith carried out an investigation into the expectations of a business rescue plan.[29] They collected details of four different international regimes namely the United Kingdom, Australia, Canada and the United States of America, and examined their goals and expectations.[30] The enquiry revealed that, from an international perspective, a business rescue plan serves as a tool for feasibility declaration, a medium of communication, an enabler of transparency and serves to attract and secure post-commencement funding.[31] These findings were qualified as general business rescue plan expectations. The expectations were then aligned with Chapter 6 of the South African Companies Act to determine whether the Act complied with the general expectations of a business rescue plan. It was found that there exists a significant contrast between international business reorganization plans and those being submitted in South Africa under the newly adopted business rescue regime.[32]

This study will focus on both international and national expectations of a business rescue plan. Pretorius and Smith's investigation indicated that three of the international regimes required that a business rescue plan be approved by the court while the South African regime requires the approval of creditors. Hence, the researcher will focus on both international and regional business rescue regimes to find out how a business rescue plan contributes to the sustainability and revival of a financially distressed company.

According to Bradstreet, the adoption of business rescue into the companies' legislation in South Africa brought about the end of judicial management and can be viewed as a response to the worldwide trend of restructuring financially distressed

[28] *Ibid* 2.
[29] M Pretorius & W. R Smith, 'Expectations of a business rescue plan: International Directives for Chapter 6 implemented' (2013) Volume 18 Issue 2 *Southern African Business Review* 108.
[30] *Ibid*.
[31] *Ibid*.
[32] *Ibid*.

corporations rather than overseeing their dissolution.[33] This worldwide trend can be traced back to the increasing recognition of the value to affected persons of the revival of financially ailing companies and the resuscitation of economically viable enterprises to restore production capacity, investment and employment.[34] In light of Bradstreet's assertion, a financially distressed company is of more value under reorganization rather than dissolution. The researcher will make use of Bradstreet's paper in explaining the rationale behind business rescue as compared to liquidation. However, the study will include an analysis of the previous mechanism in order to reveal some of the practices and procedures that can be incorporated into the current business rescue regime.

The Report of the Insolvency Law Review Committee on Insolvency Law and Practice in the United Kingdom (Cork Report) acknowledged that 'the success of an insolvency regime was heavily dependent on those who administer it'.[35] However, Pretorius expressed concerns with regards to the qualification and duties of a business rescue practitioner. He points out that the qualifications of a business rescue practitioner are complex, vaguely stated and involve a wide range of competencies not accessible to the average business person.[36] He further notes that at present, proposed selection guidelines for BRPs appear to be aligned with generally defined competencies of leaders and change agents and can, at best, be described as vague. [37] He argues that details about what exactly practitioners do during a rescue need to be determined in order to guide licensing and build a qualifications framework for the education of business rescue practitioners.[38] Pretorius goes on to explore the qualifications and responsibilities of practitioners. He found that business rescue practitioners are responsible for taking control, investigating the affairs, compiling a rescue plan, implementing the plan and complying with the statutory process. The researcher will refer to Pretorius' work in explaining the role of a business rescue practitioner in ensuring the sustainability of a financially distressed company.

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[33] Bradstreet (note 15 above) 195.
[34] *Ibid* 196.
[35] Cassim (note 8 above) 863.
[36] M Pretorius, 'Tasks and Activities of the business practitioner: a strategy as practice approach' (2013) Volume 17 Issue 3 *Southern African Business Review* 1.
[37] *Ibid* 1.
[38] *Ibid* 3.

Rael Gootkin discusses case law that dealt with obtaining consent from shareholders.[39] He highlights how courts construe the nature of the 'binding offer' that an affected person could make for the voting interests of opponents of the business rescue plan. He observes that the courts have handed down conflicting decisions, for instance in the case of *DH Brothers Industries (Pty) Ltd v Gribnitz NO & Others*[40]. Gorven J held that a 'binding offer' is one that could not be withdrawn by the offeror and could be accepted or rejected by an opponent of the plan.[41] If accepted, it gives rise to an agreement of sale- a sale for cash.[42] The acceptance or rejection had only to take place after the value of the voting interests had been determined, and this determination had to take place within five days.[43] In other words, according to Justice Gorven, a "binding offer" denotes an offer that cannot be withdrawn by the offeror but is open for acceptance or rejection by the opposing creditors to whom it is made.

In *African Banking Corporation of Botswana Limited v Kariba Furniture Manufacturers (Pty) Ltd & Others*[44] the court held a different view. Kathree-Setiloane J contended that the 'binding offer' envisaged in section 153(1) (b) (ii) of the Companies Act of 2008 is not an 'option' or 'agreement' in the contractual sense of the term but is rather a set of statutory rights and obligations from which neither party can resile.[45] Thus, the binding offer will be binding on both the offeror and the offeree once it has been made.[46] Failure or refusal by the offeree to accept the binding offer is of no consequence.[47]

Gootkin concluded that courts have adopted a varied approach regarding whether or not, in pursuing a business rescue plan, the creditors and/or shareholders who vote against prospective business rescue plans can be compelled to accept the plan on the basis that the creditors' voting interests are acquired through a binding offer. The case of *AG Petzetakis International Holdings Ltd v Petzetakis Africa (Pty) Ltd and Others*,[48] is a notable example where the court stressed the importance of having the

[39] R Gootkin, 'The problem of compelling shareholders to approve business rescue plan' (2014) Volume 14 Issue 4 *Without Prejudice* 21.
[40] *DH Brothers* case (note 22 above).
[41] *Ibid* 129.
[42] *Ibid*.
[43] *Ibid* 130.
[44] 2013 (6) SA 471 (GNP).
[45] *Ibid* 483.
[46] *Ibid.*
[47] *Ibid* 486.
[48] 2012 (5) SA 515 (GSJ).

upfront, in principle support of the major creditors of a financially distressed company before a court would be prepared to grant a business rescue application under section 131 of the Companies Act. The court remarked that "if an achievable draft rescue plan which has substantial support is provided at the time of the Court application for the rescue order that will improve the prospects of the application", but at the same time "the absence of a final plan at the Court application phase will not necessarily be fatal to the application."[49]

The following dictum from *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* is along similar lines.[50] In that case, Brand J said that "if the majority creditors declare that they will oppose any business rescue scheme based on those grounds, I see no reason why that proclaimed opposition should be ignored, unless, of course, that attitude can be said to be unreasonable or mala fide."[51] A majority of court decisions as discussed by Gootkin, observed that where creditors express concerns, the courts are inclined not to approve business rescue plans. The researcher shall examine what constitutes unreasonable and mala fide opposition. The researcher will further examine whether compelling shareholders to comply with a business rescue plan aligns with the main current international and national goals of business rescue.

1.9 Definition of Key Concepts

Affected persons: means a shareholder, creditor or a registered trade union representing employees of the company or each employee who is not represented by a trade union or the representative of such employee.[52]

Business rescue: as defined by the Companies Act 2008, aims to facilitate the rehabilitation of a company that is "financially distressed" by providing for: the temporary supervision of the company and management of its affairs, business and property by a business rescue practitioner and the imposition of a temporary moratorium on the rights of claimants against the company.[53]

[49] *Ibid* 9.
[50] 2013 (4) SA 539 (SCA) at para 38.
[51] *Ibid* 555.
[52] Davis (note 1 above) 443.
[53] Cassim (note 8 above) 865.

Practitioner: means a person appointed as a business rescue practitioner, as envisaged in Chapter 6 of the Companies Act, to oversee a company during the business rescue process.[54]

Financially distressed company: means a company that appears to be reasonably unlikely to be able to pay its debts as they become due and payable within six months or a company that appears to be reasonably likely to become insolvent within the ensuing six months.[55]

Going concern: refers to an accounting concept connoting a business that is operational and sustainable in that it is expected to continue to operate for the foreseeable future.[56]

Rescue: refers to the reorganisation of a company in order to restore it to a profitable entity and thereby avoid liquidation.[57]

Moratorium means an automatic stay on legal proceedings or executions against a company under business rescue, its property and its assets and on the rights of creditors of the company.[58]

1.10 Overview of Chapters

Chapter One: Introduction

This chapter covers the background and justification of the study. The researcher also spells out the aims and objectives of the study, the research methodology, literature review and definition of key concepts.

Chapter Two: The Business Rescue Scheme

The chapter focuses on the essential procedures laid down in the Companies Act for business rescue from commencement to termination. The researcher discusses the various ways in which business rescue procedure can be instituted, the requirements for initiating the process and the provisions that allow the participation of all stakeholders during business rescue.

Chapter Three: The Business Rescue Practitioner

Chapter three examines the office of the business rescue practitioner. In this chapter the researcher discusses the requirements for the appointment of the business rescue practitioner and the possible grounds on which he or she may be removed from office. The researcher also explains the various duties of the business rescue

[54] Davis (note 1 above) 446.
[55] *Ibid* 449.
[56] *Ibid* 450.
[57] Cassim F.H.I *The Practitioner's Guide To The Companies Act 71 of 2008* (2013) 144.
[58] Cassim (note 8 above) 878.

practitioner and how he or she is required to discharge such duties which include the drafting of a business rescue plan.

Chapter Four: The moratorium in business rescue

This chapter is indispensable to the whole research. Its importance lies on the fact that it explains the purpose and contribution of moratorium to the success of business rescue. The researcher explains the meaning of moratorium and the rationale behind imposing it during business rescue. In addition to the meaning, the researcher also describes when a moratorium starts and when it ends.

Chapter Five: Conclusion and Recommendations

The last chapter embodies the conclusions drawn from the research and provides recommendations emanating from the study.

1.11 Limitation of study

The primary resource for this research work is the University of Venda law library. The state of the law library in terms of law material resources is not very strong. Thus the researcher was supposed to visit law libraries in South Africa but due to the lack of funds this could not be carried out.

The researcher is a budding academic and not a business rescue practitioner. Therefore, the views expressed in this work by the researcher may not attain the level of perfection as could be expected from an established researcher. But that in itself is a positive commendation for a work of this nature which is mostly opinionated, thus opening rooms for criticism and further research in the field.

CHAPTER TWO
BUSINESS RESCUE SCHEME

2. Introduction

Business rescue scheme is a novel concept in South African company law. It is, therefore, imperative to explain the meaning and purpose of this mechanism before examining its applicability in the South African corporate world. In this chapter the researcher will discuss the fundamental principles underpinning business rescue and elaborate on the statutory definitional elements of business recue procedure.

2.1 The concept of business rescue

Business rescue may be defined as the reorganization of a financially distressed company to restore it to a profitable entity in order to avoid bankruptcy.[59] Section 128 of the Act provides that "business rescue means proceedings to facilitate the rehabilitation of a company that is financially distressed" by providing for –

(i) the temporary supervision of the company, and of the management of its affairs, business and property;
(ii) a temporary moratorium on the rights of claimants against the company or in respect of property in its possession; and
(iii) the development and implementation, if approved of a plan to rescue the company by restructuring its affairs, business property, debt and other liabilities, and equity in a manner that maximizes 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 and shareholders than would result from the immediate liquidation of the company;[60]

From the above definition, the main aim of business rescue is to keep financially distressed companies in business by resuscitating them. In *Southen Palace Investments 265 (Pty) Ltd v Midnight Storm Investment 386 Ltd* [61] Ellof J observed that the South African and the Australian[62] rescue schemes are aimed at achieving the same goal, that is, "to render it possible for companies in financial difficulty to avoid winding-up and to be restored to commercial viability."[63] In other words, business rescue involves a major intervention to avert subsequent failure. Pretorius is of the view that the business rescue scheme is acting as a critical scenario driver, as it appears to dictate the overall rescue industry's future.[64] This means that one of the mechanisms

[59] Cassim (note 57 above) 144.
[60] The Companies Act 71 of 2008 (hereinafter the Act).
[61] 2012 (2) SA 423 (WCC) para 2.
[62] Part 5.3A of the 2001 Australian Corporations Act, amended in 2007.
[63] *Southern Palace Investment* case (note 61 above) para 2.
[64] M Pretorius 'The debtor-friendly fallacy in business rescue: agency theory moderation and quasi relationship' (2016) Volume 19 Issue 4 *South African Journal of Economic and Management Science* 480.

that need to be considered in safeguarding the future of commercial activities in South Africa is the business rescue scheme.

The Act uses the term 'business rescue' rather than 'corporate rescue'.[65] However, despite the fact that these terms are often used interchangeably, the term 'corporate rescue' is more accurate because it refers to the rescue of corporate entities than the term 'business rescue', which might be considered to refer more broadly to include the rescue of business debtors that are not corporate entities.[66] However, it is perhaps worth noting that "in these rescue mechanisms the real emphasis falls less on the survival of the juristic person and more on that of the enterprise, that is, the real business carried on by the juristic person, in whole or in part so that the term 'business rescue', even in the context of corporate legislation, might be considered more appropriate."[67]

2.1.1 Scope of Application of Chapter 6 Provisions

The Chapter 6 business rescue provisions apply to companies and close corporations.[68] However, business recue provisions in the new Companies Act do not apply to sole traders or trusts or cooperatives. One of the questions that arises within the context of a company is whether a foreign company with operations in the Republic will qualify as a company for the purpose of Chapter 6 of the Act. In terms of the Act, a company is only recognized as a company where such entity falls into one of the three categories. The first, being a company that is incorporated in terms of the provisions of the Act.[69] The second category caters for a foreign company that has transferred its registration to the Republic, and the third category is that of juristic persons that were incorporated under the legislation repealed by the Act as well as entities previously recognized as companies under the provisions of the 1973 Act.[70] Delport is of the view that:

> It needs to be emphasized that the term "juristic person" as used in the definition of "company" under section 1 must not be confused with the definition of a "juristic person" which appears separately in section 1, and which includes foreign companies. The use of the term "juristic person" in the definition of "company" therefore only refers to juristic person as created by the Companies Act 1973, and the Close Corporations Act 1984 (the latter only if the close corporation has been converted to a company in terms

[65] Davis (note 1 above) 237.
[66] P Omar 'Thoughts on the Purpose of Corporate Rescue' (1997) Volume 12 Issue 4 *Journal of International Banking* 127.
[67] *Ibid*.
[68] Section 1 of the Act and section 66 (1A) of the Close Corporations Act 69 of 1984.
[69] Section 1.
[70] *Ibid* (The Act repealed the Companies Act 61 1973 and the Close Corporations Act 1984 with regards to the latter only if the close corporation has been converted to a company in terms of Schedule 2).

> Schedule 2). However, where the word "juristic person" is used in the context of rest of the provisions of this Act, it will then include a foreign company.[71]

Hence, "external companies" are specifically excluded by para (a) (i) of the definition of "company". An external company would therefore not qualify to make use of business rescue provided in Chapter 6 of the Act. Even though the company is conducting business in South Africa it is excluded from using the Chapter 6 life boat.[72]

In determining whether a company should be placed under business rescue the courts also may examine the lawfulness of the business of the company. In *Registrar of Banks v Dafel and others*,[73] the court found that the respondent Dafel received and deposited money from the public. In other words, the respondent was carrying on the business of a bank and this was in contravention of sections 17 and 18(a)(i) of the Banks Act. Section 17 of the Bank Act provides that if one operates the business of a bank he or she or it must be registered as a bank. Section 18(a)(i) states that if such person is not registered, they must be authorized by the registrar. The court then held that an order to put Dafel under rescue will further the unlawful activities of the business whilst preventing creditors from enforcing their rights against Dafel. The application to commence business rescue was dismissed. Therefore, the business rescue procedure is not available to companies conducting unlawful business regardless of the amount the company owes to its creditors.

2.1.2 Financial Distress

Before a company initiates business rescue proceedings, it must be established that the company not only is financially distressed, but that there exists a reasonable prospect that it may be revived.[74] In terms of section 128(1)(f) ''financially distressed'', in reference to a particular company at any particular time, means that—

> (i) it appears to be reasonably unlikely that the company will be able to pay all of its debts as they fall due and payable within the immediately ensuing six months; or
> (ii) it appears to be reasonably likely that the company will become insolvent within the immediately ensuing six months;

Hefer postulates that "the definition of financially distressed points to the likelihood that a company will be unable to pay all of its debts within the next six months or will become insolvent in the next six months."[75] In other words, it is when the company is

[71] P.A Delport *Henochsberg on the Companies Act* Volume 1 Issue 12 (2016) 455.
[72] *Ibid*.
[73] [2015] JOL 28714 (GSJ).
[74] Section 129.
[75] L Hefer *Notes on South African Companies Act* (2015) 419.

showing signs of pending insolvency but where it has not yet reached the stage of actual insolvency.[76]

At this stage the company is not yet insolvent, either balance sheet insolvency or cash flow insolvency.[77] Rushworth points out that "the cash-flow test can be the more critical, as it is generally fairly clear when a company simply cannot meet its liabilities from its cash flow.[78] However, establishing values for a balance-sheet test at any particular time can be subject to many variables and uncertainties, for instance the basis of valuation and whether a guarantee of another company's debts is treated as a liability."[79] In addition, the test for financial distress applies on a day-to-day basis, whereas companies would probably not expect to prepare balance sheets on a frequent basis. Rushworth recommends that directors need to be aware that, if there is concern about the company's viability, balance sheets may need to be prepared on a regular basis.[80]

The Act, however, does not clearly spell out the meaning of 'insolvent' but it appears that it refers to technical insolvency, that is, liabilities exceeding assets.[81] In *Boschpoort Ondernemings Pty Ltd v ABSA Bank Ltd* [82] the court held that:

> The retention by the legislature in the context of a winding-up of a solvent company in the new Act, of the deeming provisions as to when a company is unable to pay its debts as contained in s 345 of the old Act, is a clear indication of what is meant by an insolvent company in the new Act. It can only mean a company that is commercially insolvent. It therefore follows that a solvent company must be the converse, namely a company that is commercially solvent.

This dictum, however, clearly refers to the concept of solvency in respect of winding up. Nonetheless, without well-defined guidelines, it is clear that many tactics will be employed by the management of companies to exploit the gap between solvency and pending insolvency.[83] In the case of *Gormley v West City Precinct Properties Pty Ltd*[84] it was held that the second part of the definition of financially distressed used the words 'will become insolvent' and thus referred to the future insolvency of the company. Davis argues that in this context, a company that is already insolvent does

[76] Delport (note 71 above) 451.
[77] Hefer (note 75 above) 419.
[78] J Rushworth 'A critical analysis of the business rescue regime in the Companies Act 71 of 2008: Part III' (2010) Volume 2010 Issue 1 *Acta Juridica* 377.
[79] *Ibid.*
[80] *Ibid*.
[81] Hefer (note 75 above) 419.
[82] 2014 (2) SA 518 (SCA) para 21.
[83] Delport (note 71 above) 451.
[84] [2012] ZAWCHC 33 (WCC).

not meet the requirements of the definition and therefore cannot be placed under business rescue.[85]

However, in *Swart v Beagles Run Investments 25 Pty Ltd*,[86] the company was already insolvent and unable to pay its debts. The court did not mention this as a reason for dismissing the application for commencement of business rescue proceedings but as one of the factors to be taken into consideration when determining whether there was a reasonable prospect to rescue the company. It is submitted that the latter approach is a better approach taking into cognizance the main objective of business rescue, that is, to give a second chance to viable enterprises in financial difficulties.

In *Welman v Marcelle Props 193 and another,*[87] the court held that "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."

2.2 The purpose of business rescue

The idea of corporate or business rescue is born out of the conception that calculated risk should be encouraged and if failure occurs then there should be a system in place to help minimize the adverse effects that it may have on affected parties.[88] Hence the "purpose of corporate insolvency has many aspects, mostly designed to create opportunities for action rather than laying down consequences for stipulated state of affairs."[89] Business rescue scheme is one of the legal actions that can be adopted where an enterprise faces insolvency or liquidation.

The new South African Companies Act is aimed at facilitating the creation of a corporate rescue system appropriate and applicable to the needs of a modern society. This is clearly spelled out in section 7(k) which provides that one of the objectives of the Act is to "provide for the efficient rescue and recovery of financially distressed companies, in a manner that balances the rights and interests of all

[85] Davis (note 1 above) 246.
[86] 2011 (5) SA 422 (GNP).
[87] [2012] JOL 28714 (GSJ) para 28.
[88] J M Wood 'Corporate Rescue: A Critical Analysis of its Fundamentals and Existence' Unpublished Thesis University of Leeds (2013) 11 available at http://.www.etheses.whiterose.ac.uk/view/iau/Leeds=2ERC-SLAW accessed on 25 August 2016.
[89] *Ibid*.

relevant stakeholders". In *African Banking Corporation of Botswana Ltd v Kariba Furniture Manufacturers (Pty) Ltd* [90] it was clearly stated that:

> The end sought by the business rescue regime in Chapter 6 of the Act is the efficient rescue or rehabilitation of a company that is financially distressed and in doing so, the interests of all stakeholders are to be taken into account.

At the heart of business rescue is the rehabilitation of a financially distressed company. In fact, the purpose of business rescue proceedings is stated as being "proceedings to facilitate rehabilitation of a company."[91] However, the term 'rehabilitation' is not defined in the Act. The term would imply to intimate the return of a company to complete solvency and the effect of such 'rehabilitation' is continuation of business. In *Ex parte Le Roux*[92] it was held that the effect of rehabilitation of an insolvent is to restore him fully to the market place and more importantly to the obtaining of credit.

In essence, rehabilitation under insolvency law means the company is now able to operate its business and also obtain credit. However, in terms of the definition of business rescue if the company cannot continue on a solvent basis, then an outcome that ensures a higher return for creditors than they would receive under liquidation is acceptable.[93] Delport argues that this is clearly not rehabilitation in any sense of the word and the situation provided by the words.[94] Notably, there are two main objects of business rescue, the first one being that the company must be rehabilitated and secondly, where it is not possible the company must be given time to operate business under a plan that would give a better return to creditors. Kleitman and Masters postulate that "when looking at the definition of 'business rescue' in s128(1) of the Companies Act, it suggests that there is a permissible alternative to rescuing the company, namely: giving the creditors and shareholders of the company a better return than would an immediate liquidation of the company."[95]

The dichotomy was addressed in *AG Pertzetakis International Holding Ltd v Pertzetakis Africa Pty Ltd and others.*[96] Coetzee AJ observed that "the status of the alternative object in the South African Companies Act depends primarily on an interpretation of that Act. The creation of the alternative object will probably give rise to more litigation. It is, for example, strange to create an object for a new remedy in a

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[90] *African Banking Corporation* Case (note 44 above) para 40.
[91] Section 128.
[92] 1996 (2) SA 419 (C) 423.
[93] Section 128(1)(b)(iii).
[94] Delport (note 71 above) 448.
[95] Y Kleitman and C Masters 'Better return for creditors- business rescue: company law' (2013) Volume 13 Issue 7 *Without Prejudice* 34.
[96] *AG Pertazetakis* case (note 48 above) para 12.

definition section." Whereas Brand J in *Oakdene Square Properties Pty Ltd v Farm Bothasfontein (Kyalami) Pty Ltd* [97] recognized the second objective and held that it formed part of business rescue. The court held that:

> Although I have no problem with the dictionary meaning of 'rescue' and 'rehabilitation' on which the argument relies, it fails to recognize, I think, that s 128(1)*(b)* gives its own meaning to these terms, which does not coincide with these definitions. As I understand the section, it says that 'business rescue' means to facilitate 'rehabilitation', which in turn means the achievement of one of two goals: (a) to return the company to solvency, or (b) to provide a better deal for creditors and shareholders than what they would receive through liquidation. This construction would also coincide with the reference in s 128(1)*(h)* to the achievement of the goals (plural) set out in s 128(1)*(b).* It follows, as I see it, that the achievement of any one of the two goals referred to in s 128(1)*(b)* would qualify as 'business rescue' in terms of s 131(4).

In *Southern Palace Investment 265 Pty Ltd v Midnight Storm Investment 386,*[98] the court directed that:

> In relation to the alternative aim referred to in section 128(b)(iii) of the new Act, being to procure a better return for the company's creditors and shareholders than would result from the immediate liquidation thereof, one would expect an applicant for business rescue to provide 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. It is difficult to see how, without such details, a Court will be able to compare the scenario sketched in the application with that which would obtain in an immediate liquidation of the company. Mere speculative suggestions are unlikely to suffice.

However, it is interesting to note that neither section 129 or 131 specifically states the second objective as a requirement for entering the business rescue procedure.

Under the Australian rescue mechanism, the purpose of corporate rescue is provided for in section 435A of Part 5.3 A which provides that "The object of this Part is to provide for the business, property and affairs of an insolvent company to be administered in a way" that:

> (a) maximizes 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 than would result from an immediate winding up of the company.[99]

Case law strongly suggests that Australian courts recognize that where it is not possible to rescue the company, a better return for creditors must be achieved. This

[97] *Oakdene Square* case (note 50 above) para 26.
[98] *Southern Palace Investment* case (note 61 above) at para 25.
[99] Corporations Act (note 62 above).

second objective was recognized in *Dallinger v Halcha Holdings Pty Ltd (in admin) & Another* [100] where Sundberg J said:

> The machinery provided by the Part should be available in a case 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 than would be the case with an immediate winding up.

It seems that both domestic and foreign courts admit that there exists an alternative goal where rehabilitation cannot be achieved.

2.2.1 Rehabilitating financially distressed companies

In *Griessel and Another v Lizemore*[101] it was held that the primary objective of business rescue is to prevent viable companies from closing down by allowing them an opportunity to regain solvency through the mechanism of business rescue provided that this can be achieved within a reasonable time. The thinking is that a company in financial difficulties may be worth more as a going concern than if it is liquidated with its assets realized on a piecemeal basis.[102] Modern corporate rescue and reorganization seeks to take advantage of the reality that in many cases, an enterprise not only has substantial value as a going concern, but that its value as a going concern exceeds its liquidation value. The value of a business as a going concern will generally be greater that its liquidation or breakup value. Creditors will also overtime receive a better return if the company survives as a going concern.[103] Thus in *United States v Whiting Pools Inc*,[104] the court stated that under the reorganization provisions of the US Bankruptcy Code, a troubled enterprise may be restructured to enable it to operate in the future.

In addition, the assets of a debtor are likely to be more valuable if used in a rehabilitated business than if 'sold for scrap.'[105] Corporate rescue provides an alternative to using insolvency laws to convert a debtor's assets to cash by "restructuring the financial structure of the debtor involving the issuance of new debt and equity in accordance with the claimant's priorities".[106] The general duties of the liquidator are to recover all the assets and property of the company, sell these to satisfy the costs of the winding up and the claims of creditors in so far as possible and then to ultimately distribute the balance of the insolvent estate (the free residue)

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[100] [1995] 14 ACLC 263 at 268.
[101] [2015] 4 All SA 433 at para 78.
[102] Cassim (note 8 above) 862.
[103] *Ibid*.
[104] 462 U.S 198 (1983).
[105] Cassim (note 8 above) 863.
[106] A Smith 'Corporate Administration: A Proposal Model' (1999) Volume 32 *De Jure* 81.

to those legally entitled to it.[107] Unlike a liquidator, a business rescue practitioner is expected to make use of the debtor's assets to meet the firm's obligations and if possible to rehabilitate the whole business.

2.2.2 Balancing the rights of stakeholders

Business rescue does not only benefit creditors but also employees and shareholders. By permitting reorganisation, the business can continue to provide jobs and produce a better return for its owners.[108] In *Oakdene Square Properties Pty Ltd v Farm Bothasfontein (Kyalami) Pty Ltd,*[109] the court stated that:

> The general philosophy permeating the business rescue provisions is the recognition of the value of the business as a going concern rather than the juristic person itself. Hence the name "business rescue" and not "company rescue". This is in line with the modern trend in rescue regimes. It attempts to secure and balance the opposing interests of creditors, shareholders and employees. It encapsulates a shift from creditors' interests to a broader range of interests.

The thinking is that to preserve the business coupled with the experience and skills of its employees, may, in the end prove to be a better option for creditors in securing full recovery from the debtor.

2.2.3 Business rescue as economy rescue

The economy suffers when a company is shut down. In *Koen and another v Wedgewood Village Golf & Country Estate (Pty) Ltd and others,*[110] Binns Ward J observed that:

> It is clear that the legislature has recognized that the liquidation of companies more frequently than not occasions significant collateral damage, both economically and socially, with attendant destruction of wealth and livelihoods. It is obvious that it is in the public interest that the incidence of such adverse socio-economic consequences should be avoided where reasonably possible. Business rescue is intended to serve that public interest by providing a remedy directed at avoiding the deleterious consequences of liquidations in cases in which there is a reasonable prospect of salvaging the business of a company in financial distress, or of securing a better return to creditors than would probably be achieved in an immediate liquidation.

The strong underpinning approach is that the regulatory framework within which companies function should promote growth, employment, innovation and international competitiveness.[111] At the heart of the Companies Act is the reaffirmation of the concept of a company as a means of achieving economic and

[107] Cassim (note 8 above) 922.
[108] *Ibid* 863.
[109] 2012 (3) SA 273 (GSJ) para 12.
[110] 2012 (2) SA 378 (WCC) para 14.
[111] Cassim (note 57 above) 6.

social benefits.[112] For instance, if a company is successfully rescued or turned around it will be able to pay tax.[113] At present, tax statistics indicate that a year after the adoption of business rescue there has been an increase. Active companies registered for income tax increased by 7.9% from just over two million in 2011/12 to nearly 2.2 million in 2012/13.[114] Most of these companies were previously inactive and dormant.

2.3 The nature of business rescue proceedings

The previous judicial management procedure failed because it relied heavily upon the courts. This proved to be costly and the proceedings were slow. Nonetheless, the current business rescue model is designed to operate with minimum interaction with the courts. In the *African Banking Corporation case*, the court observed that

> There is a conscious attempt by the legislature, in the chapter 6 of the Act, to keep the role of the court in business rescue proceedings to a minimum. Not only does this assist in making the business rescue cost effective, but also allows for the swift and efficient rescue of the company.[115]

In *Cawthorn v Keira Constructions Pty Ltd*,[116] Young J held that "the statutory scheme under Pt 5.3A intends that the court should keep to the sidelines and become involved only to ensure that the spirit and object of Pt 5.3A are implemented. One instance where the court may leave the sidelines and enter the field of play is where voluntary administration is put in place with a view to securing compliant administration." The legislative approach to rescue proceedings is that it must be swift, efficient and cost effective and this reduces additional unnecessary costs on an already financially distressed company.

The Act envisages a short-term approach to the financial position of the company and that the business rescue process should be a speedy process. In *Koen and Another v Wedgewood Village Golf and Country Estate Pty Ltd and others* [117] it was held that:

> It is axiomatic that business rescue proceedings, by their very nature, must be conducted with the maximum possible expedition. In most cases a failure to expeditiously implement rescue measures when a company is in financial distress will lessen or entirely negate the prospect of effective rescue. Legislative recognition of this axiom is reflected in the tight timelines given in terms of the Act for the implementation of business rescue procedures if an order placing a company under supervision for that purpose is granted.

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[112] Section 7.
[113] Cassin (note 8 above) 863.
[114] I Pillay and L Fuzile *2013 Tax statistics* (2013) 95.
[115] *African Banking Corporation* case (note 44 above) para 51.
[116] 1994 13 ACRS 227.
[117] *Koen* case (note 110 above) para 10.

Furthermore, there is also the consideration that the mere institution of business rescue proceedings, however dubious might be their prospects of success in each case, materially affects the rights of third parties to enforce their rights against the subject company. Hence, business rescue proceedings are meant to be quick and for a short period.

2.4.1 Business Rescue Initiated by the Board

Business rescue may be initiated by the management of the company. Section 129 provides that:

> (1) Subject to subsection (2)(a), the board of a company may resolve that the company voluntarily begin business rescue proceedings and place the company under supervision, if the board has reasonable grounds to believe that—
> (a) the company is financially distressed; and
> (b) there appears to be a reasonable prospect of rescuing the company

Thus Chapter 6 makes provision for a company to commerce business rescue proceedings on a voluntary basis. The rationale for making provision for voluntary route is that the board of a company is in a position to know that a company is financially distressed and is best equipped to pass a resolution that a company be placed under business rescue and to initiate the business rescue proceedings.[118] This is also advantageous to the proceedings because it averts unnecessary delays and costs.

The resolution to commerce business rescue must be passed by the board of directors. Such a resolution must be by a majority vote or by the majority of the board giving written consent.[119] Rushworth argues that "the procedures for majority voting are subject to the company's Memorandum of Incorporation (MOI) providing otherwise,"[120] while Watson and Cason note that a company's MOI cannot alter the provisions in section 129.[121] This means that section 129 is unalterable and the provisions of a company's MOI cannot negate it or limit its application.[122]

This gives rise to the following question; since a company's MOI cannot alter the application of section 129, is it within the ambit of section 15(2)(a)(iii) to impose a restriction upon the directors? It is accepted that in practice, a company's MOI makes the passing of a resolution to commence business rescue proceedings a restricted

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[118] *Lazenby v Lazenby Vervoer VV and others* [2014] ZANWHC 41 at para 23.
[119] Rushworth (note 78 above) 377.
[120] *Ibid*.
[121] K Watson and S Cason 'Altering the requirements of section 129' (2016) Volume 16 Issue 7 *Without Prejudice* 4.
[122] *Ibid.*

matter.[123] Therefore, if the board of directors wishes to resolve a restricted matter it needs the approval of the shareholders.[124] There are two divergent views as to the application of section 129.

One view is that "to require shareholder approval before the directors can make a decision in terms of section 129(1) is contrary to the spirit of the section."[125] The reasons advanced for this argument are:

• Such a limitation amounts to a separate and unrelated requirement, not simply a more onerous requirement as provided for under section 15(2)(a)(iii).
• Section 15(2)(a)(iii) states that an MOI may impose on a company a more onerous requirement. The definition of "company" in the Act does not include the board of directors and section 129(1) gives the power to enter into voluntary business rescue to the board of directors, not the company.
• Furthermore, aggrieved persons should look to section 130, which allows affected persons to apply to court to have a section 129 resolution overturned.[126]

The opposing view is that a board's power to enter into voluntary business rescue proceedings can be validly limited by requiring shareholder approval. The reasons advanced for this argument are:

• Section 7(i) provides that a purpose of the Act is to balance the rights and obligations of shareholders and directors within a company. To deny the shareholders the opportunity to vote on such an important issue would not give proper recognition to the interests of the company's owners.
• Restricting the board's power to commence voluntary business rescue proceedings is normally done by private companies where the board is made up of nominees of the shareholders.
• In such instances, the shareholders generally funded and drove the inception of the company and its business. It is, therefore, appropriate for the shareholders to have the power to veto the voluntary commencement of business rescue as they are equally well-placed to understand the workings of the company.[127]

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[123] *Ibid.*
[124] *Ibid*.
[125] *Ibid*.
[126] Watson and Cason (note 121 above) 5.
[127] *Ibid*.

In *Lennard's Carrying Co Ltd v Asiatic Petroleum Co Ltd* [128] the House of Lords held that "the board of directors is the directing mind and will of the company". Therefore, a restriction imposed on the company is also imposed on its board and vice versa.[129]

In view of the above arguments, the proposition that section 15(2)(a)(iii) applies to the company only and cannot apply to the directors in terms of section 129(1) cannot be sustained. If a director is aggrieved section 131 allows such affected person to apply for compulsory business rescue. Watson and Cason submit that in order to recognize the interests of shareholders the second argument advanced should be preferred.[130] In other words, "a company's MOI should be capable of restricting the directors' power to commence voluntary business rescue proceedings by requiring shareholders' approval."[131] However, it is important to note that in terms of section 15(1) (a) and (b) the MOI[132] of a company must be consistent with the Act and where it is in contravention such provision is null.[133] Thus, a provision in the MOI of a company that limits the power of the directors to make a resolution to commence business rescue is inconsistent with the Act.

2.4.1.1 The board of directors

At present the courts have accepted that the board of directors can pass a resolution to commence business rescue proceedings without the shareholders' approval. However, such a resolution must be passed by a majority vote. In *DH Brothers Industries (Pty) Ltd v Gribnitz NO and others* [134] the applicant brought an action to set aside a resolution to commerce business recue because the resolution had been made by two directors. The court granted an order to set aside the resolution on the grounds that the board was not properly constituted and therefore had failed to meet the requirement set out in section 129. However, this decision was overturned by the Supreme Court of Appeal in *Panamo Properties (Pty) Ltd and another v Nel and others NNO*[135] where the Court held that:

> The passing of a resolution to commence business rescue cannot readily be described as a procedural requirement. It is merely the substantive means by which the company may take that step. The board is under no obligation at all to take such a resolution, although, if it is financially distressed, it may be obliged to inform shareholders and creditors of the reasons for not doing so

[128] [1915] AC 705.
[129] Watson and Cason (note 121 above) 5.
[130] *Ibid*.
[131] *Ibid*.
[132] Section 15.
[133] Section 6(15) (a) and (b).
[134] *DH Brothers* case (note 22 above) para 16.
[135] 2015 (5) SA 63 (SCA) para 23.

> (s 129(7)). It cannot then be described as a 'requirement', much less a procedural requirement.

The board of directors must have a legitimate reason for resolving to begin business rescue proceedings. This view is expressed in *Griessel and another v Lizemore and another* [136] where Spilg J stated that "the most obvious is the requirement that there must be a legitimate business purpose in resolving to place the company under business rescue". The court held that:

> A requirement of good faith is implicit in the scheme of Chapter 6 which seeks to balance the interests of affected parties including creditors and employees. The requirement for good faith is expressly mentioned in the context of a director who may be liable for costs under section 130(5) (c) if the directors' resolution placing the company under business rescue is set aside and he fails to satisfy the court that he acted in good faith when claiming that the company was financially distressed.[137]

If there are objective factors that indicate that the company is in financial distress and the board takes a resolution based on their belief in respect of the factual situation, it is clearly a belief based on reasonable grounds and the resolution will be bona fide.[138]

When resolving to place a company under business rescue, section 129 (1) requires that the board must have reasonable ground to believe that the company is financially distressed and that there are good reasons to believe that it can be saved.[139] However, the term "reasonable ground to believe" is not defined in the Act. It is submitted that the term refers to the company's specific circumstances at the time and which will be known to the board, which is a subjective test based on objective facts.[140] In the *African Banking Corporation case* [141] the Supreme Court of Appeal held that:

> There can be no dispute that the directors voting in favor of a business rescue must truly believe that prospects of rescue exist and such belief must be based on a concrete foundation.

Loubser is of the view that the requirement that the board must have reasonable grounds for believing, and not merely that reasonable grounds must exist, implies that the test is both objective and subjective: whether a reasonable person, with the knowledge, experience and insight (or lack of it) of the directors, would believe that

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[136] *Griessel* case (note 101 above) para 82.
[137] *Ibid.*
[138] Delport (note 71 above) 458.
[139] Watson and Cason (note 121 above) 4.
[140] Delport (note 71 above) 459.
[141] 2015 (5) SA 192 (SCA) para 30.

these circumstances exist.[142] From the above views the board of directors must exercise due diligence and care in passing a resolution to place the company under business rescue.

Section 129(1)(b) further requires that there must be a reasonable prospect of rescuing the company. In other words, the board of directors in resolving to place the company under business rescue must be of the opinion that the company may be rehabilitated. Chapter 6 does not explain the meaning of "reasonable prospect". It is important to point out that the term has the same meaning in the context of section 129 (1) and section 131 (4) in that the board or the applicant must meet this requirement before the adoption of business rescue or prior to obtaining an order to place the company under supervision.[143] As to the meaning of the words "reasonable prospect", in the *Southern Palace Investment* case[144] Elloff JA held that the phrase indicates "something less is required than that the recovery should be a reasonable probability". In *Prospec Investments v Pacific Coast Investments 97 Ltd* [145] Van de Merwe J held that:

> Vague averments and mere speculative suggestions will not suffice in this regard. There can be no doubt that, in order to succeed in an application for business rescue, the applicant must place before the court a factual foundation for the existence of a reasonable prospect that the desired object can be achieved. In my view a prospect in this context means an expectation. An expectation may come true or 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.

When a resolution is adopted by the board of directors it becomes the duty of every director to implement the resolution and this includes those who may have voted against the resolution.[146]

A resolution to begin rescue proceedings must be filed with the Companies and Intellectual Property Commission (the Commission). Section 129(2)(b) of the Act states that a resolution to commence business rescue has no force or effect until it has been filed with the Commission. In terms of section 129(2) a resolution for voluntary business rescue may not be adopted if liquidation proceedings have been initiated by or against the company. Bezuidenhout notes that:

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[142] A Loubser 'Some Comparative Aspects of Corporate Rescue in South African law' LLD dissertation University of South Africa 2010 59.
[143] Delport (note 71 above) 461.
[144] *Southern Palace Investment* case (note 61 above) para 21.
[145] 2013 (1) SA 542 FSB para 11 and 12.
[146] *Re Equiticorp International plc* [1989] BCLC 597 (Ch D) 599c.

> A mere application for a liquidation order should not be interpreted as 'liquidation proceedings' for the purpose of s 129(2)(a), to enable the board of a financially distressed company to commence business rescue proceedings and probably rescue the company, before an application for its liquidation is adjudicated.[147]

When the board of directors has voted to place the company under business rescue, the company is not allowed to vote for a resolution to begin liquidation proceedings unless the period for the realization of a business rescue has elapsed or until the business rescue proceedings have ended.[148]

2.4 Initiating Business Rescue

There are two ways of commencing business rescue proceedings; namely: by means of a resolution of the board of directors or an affected person may apply to a court for an order placing the company under business rescue.

2.4.1.2 Notice to affected persons

Once the resolution has been filed with the Commission, the company must notify all affected persons of the resolution, the date on which it became effective and the grounds under which the resolution was taken.[149] The notice to affected persons must be communicated within five working days. This provision requires strict compliance and not substantial compliance. Section 129 (5) provides that where a company fails to notify affected persons, the resolution to begin business rescue elapses and becomes a nullity. In *Advanced Technologies and Engineering Company Pty Ltd (in business rescue) v Aeronatique et Technologies Embarquees SAS*[150] Fabricius J emphasized that:

> It is clear from the relevant sections contained in chapter 6 that a substantial degree of urgency is envisaged once a company has decided to adopt the relevant resolution beginning business rescue proceedings. The purpose of s129(5), is very plain and blunt. There can be no argument that substantial compliance can ever be sufficient in the given context. If there is non-compliance with s129(3) or (4) the relevant resolution lapses and is a nullity. There is no other way out, and no question of any condonation or argument pertaining to "substantial compliance".

Despite the fact that the learned judge did not specifically say so, it is implicit that an inevitable consequence of the resolution having lapsed would be that the business rescue process would terminate.[151] This approach was also followed in *Panamo*

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[147] S Bezuidenhout 'Rescue the business before liquidation is considered: Feature' (2016) Volume 2016 Issue 561 *De Rebus* 23.
[148] Section 129 (6).
[149] Section 129 (3) (a).
[150] *Advanced Technologies* case (note 23 above) para 27.
[151] *Panamo Properties* case (note 135 above) para 17.

Properties (Pty) Ltd v Nel and Another.[152] However, a contrary approach was adopted in *Ex Parte Van den Steen NO* [153] where Rautenbach AJ held that:

> Fabricius J was dealing only with non-compliance with time limits in regard to the appointment of a business rescue practitioner and not to other aspects of sub-sections (3) and (4). He accordingly held that, where there had been substantial compliance with those provisions, s 129(5) did not operate to nullify the resolution.

In *Re ABSA Bank v Caine NO* [154] Daffue J pointed out that "Fabricius J had not given consideration to the provisions of s 130(1)*(a)*(iii) and that his construction led to anomalies as between s 129 and s 130." Elliot and Weyers are of the view that a better interpretation of section 129(5)(a) is provided in *Panamo Properties* case where the Supreme Court of Appeal adopted a purposive interpretation and reconciled s129(5)(a) with s130(1)(a)(iii) and s132(2)(a)(i).[155] In this case the Supreme Court of Appeal held that Daffue J's finding is correct.[156] The Court further referred to the concerns echoed by Delport and Vorster, who point out that:

> The practical consequences of the resolution that "lapses and is a nullity" are uncertain … From the wording of the section it would appear that the resolution lapses and becomes a nullity automatically, without any intervention from outside parties. From a practical perspective, this could create a number of problems, especially if this has been done intentionally by the company in order to gain the protection of Chapter 6 for a brief period of time, only to exit the procedure due to the resolution lapsing and becoming a nullity at a later date. This could also have unintended consequences where non-compliance with the notice and publication requirements have been minor and unintentional … It is not clear whether non-compliance in such circumstances means that the business rescue process lapses and becomes a nullity, even if the business rescue plan has already been adopted and is in the process of being implemented.[157]

The Supreme Court of Appeal noted that the interpretation offered by Fabricius J does not allow the operation of section 130(1) (a) (iii).[158] There is no need to apply for the setting aside of a resolution on the bases that it has failed to comply with section 129 if that resolution has already lapsed and been rendered a nullity. This is also because the term "procedural requirements" in section 130(1)(a)(iii) refers to the procedural requirements in section 129(3) and (4).[159] The Supreme Court of Appeal further held that section 132(2) is the provision in Chapter 6 that deals with the

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[152] *Ibid* para 18.
[153] 2014 (6) SA 29 (GJ). See also *MAN Financial Services SA (Pty) Ltd v Blouwater Boerdery CC* (GNP case no 72522/2012).
[154] [2014] ZAFSHC 46 paras 24 to 26.
[155] A Elliot and Meyers 'Hot off the business press: company law' (2015) Volume 15 Issue 6 *Without Prejudice* 11.
[156] *Panamo Properties* case (note 135 above) para 18.
[157] Delport (note 71 above) 61.
[158] *Panamo Properties* case (note 135 above) para 20.
[159] *Ibid* para 21.

termination of business rescue proceedings.[160] Whereas, section 132(2) does not provide that where a resolution has lapsed business rescue proceedings will be terminated. In terms of section 132(2)(a)(i) business rescue proceedings will terminate when the court sets aside the resolution that started those proceedings. In essence, when a court grants an order in terms of section 130(5)(a), the effect of that order is that it will set aside the initiating resolution and also terminate the business rescue proceeding.[161]

This means that, business rescue proceedings commenced by that resolution (that has lapsed and became null in terms of section 129(5)(a) has not terminated unless the court grants an order in terms of section 130 (5) (a).[162] In other words, business rescue will only terminate when the court has set the resolution aside. The court may grant an order to set an initiating resolution aside in circumstances where it appears just and equitable to do so.[163] The Supreme Court of Appeal, however, found that this is not an additional ground. Elliot and Meyer note that "over and above establishing one or more of the grounds set out in section 130(1)(a), the court will only set aside the business rescue resolution and terminate the business rescue if it is satisfied that, in the light of all the facts, it is just and equitable to do so."[164] The Supreme Court further held that procedural deficiencies will not, on their own, constitute sufficient grounds to set aside the resolution.[165] This approach precludes litigants, whether shareholders and directors of the company or creditors, from exploiting technical issues in order to subvert the business rescue process or turn it to their own advantage.[166]

When board of directors decides not to initiate proceedings to begin business rescue it must give notice to affected persons. Section 129 (7) clearly provides that:

> If the board of a company has reasonable grounds to believe that the company is financially distressed, but the board has not adopted a resolution contemplated in this section, the board must deliver a written notice to each affected person, setting out the criteria referred to in section 128(1)(e) that are applicable to the company, and its reasons for not adopting a resolution contemplated in this section.

Section 129 is intended to allow affected persons to apply to court to begin business rescue in case the board of directors has made an error of judgment in deciding not

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[160] *Ibid* para 28.
[161] *Ibid* para 28.
[162] *Ibid* para 29.
[163] *Ibid* para 32.
[164] Elliot and Meyer (note 155 above) 11.
[165] *Panamo Properties* case (note 135 above) para 34.
[166] *Ibid*.

to adopt business rescue.[167] It also warns all creditors that the company they are dealing with is financially distressed and that dealing with such company could be at their own peril.[168]

2.4.1.3 Objections to resolution

The business rescue process has a mechanism to reverse the whole process. This mechanism however, is mainly operated by the court. Section 130(1) stipulates that:

> At any time after the adoption of a resolution in terms of section 129, until the adoption of a business rescue plan in terms of section 152, an affected person may apply to a court for an order—
> (a) setting aside the resolution, on the grounds that—
> (i) there is no reasonable basis for believing that the company is financially distressed;
> (ii) there is no reasonable prospect for rescuing the company; or
> (iii) the company has failed to satisfy the procedural requirements set out in section 129;

.

In other words, where affected persons have objections against the resolution such resolution may be set aside by a court order. It can be argued that this provision protects the business rescue scheme from abuse by directors.

An affected person who makes an application to the court in terms of section 130 (1) must serve a copy of the application to the company and the Commission. The applicant must also notify all affected persons of the application.[169] The notification requirements under subsection 3 are described as extremely onerous and place a heavy burden upon the applicant.[170] In any event, it is not clear how an applicant who is at arm's length will be able to obtain information necessary in order to notify all creditors, shareholders and employees not represented by a registered trade union.[171] It is recommended that it would be easier for the business rescue practitioner to perform this task and the legislature should consider amending this provision accordingly.[172]

Nonetheless, a notice in terms of section 130 (3) is sufficient and there is no need for creditors to be joined. This view is demonstrated in *ABSA Bank v Golden Dividend 339 Pty Ltd and others* [173] where the court held that "the Legislature deemed it sufficient for affected parties to be notified of such proceedings and did not deem it

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[167] Cassim (note 8 above) 868.
[168] *Ibid*.
[169] Section 130 (3).
[170] Delport (note 71 above) 474.
[171] *Ibid.*
[172] *Ibid* 475.
[173] 2015 (5) SA 272 (GP) para 29.

necessary for such parties to be joined." Due to the similarities in wording, the principles in *Cape Point Vineyard Pty Ltd v Pinnacle Point Group Pty Ltd*[174] in respect of section 131 (2) pertaining to notice should also apply to section 130 (3).[175] In that case Rogers AJ raises the spectre of thousands of affected persons having to be given notice of an application to place a company under supervision and to commence business rescue proceedings in the case of a large public company.[176] Rogers AJ further questions the appropriateness of the requirement in regulation 124 of the Companies Regulations that the full application must be delivered to affected parties.[177] Hence, to require, in addition to notice, the joinder of all affected parties to an application brought in terms of s 130(1) is even more inappropriate and would lead to insensible and unbusiness like results.[178]

Each affected person has a right to participate in the hearing of an application to set aside a business rescue resolution.[179] *In Cape Point Vineyards Ltd v Pinnacle Point Group*[180] Rogers JA intimated that he did not think the legislature contemplated that an affected person would have to apply for leave to intervene in order to participate in the legal proceedings. However, Delport contends that courts would need to regulate the procedure to be followed, for instance where affected party wishes to file affidavits relevant to the application.[181] This will also ensure fairness to all parties involved. In *Engen Petrolium Ltd v Multi Waste Pty Ltd*[182] the court held that an applicant in terms of section 130 would not require leave of the Court to intervene. However, such leave may be necessary as a procedural requirement.[183]

Section 130 (1) gives an affected person three grounds on which to base the application to set aside business rescue proceedings; the first one being that there is no reasonable ground to believe that the company is financially distressed. In such a case the applicant must prove that the resolution was made in bad faith. In *Griessel and another v Lizemore and others,*[184] Spilg J said that:

> Bad faith will be demonstrated if, for instance, the intention of the directors in passing a section 129(1) resolution is found to be an abuse. This would be

[174] 2011 (5) SA 600 (WCC) para15 and 16.
[175] Delport (note 71 above) 475.
[176] *Cape Point Vineyard* case (note 174 above) at 15.
[177] *Ibid* at 16.
[178] *ABSA Bank* case (note 173 above) at 27.
[179] Section 130 (4).
[180] *Cape Point Vineyard* case (note 174 above).
[181] Delport (note 71 above) 475.
[182] 2012 (5) SA 596 (GSJ) at para 30.
[183] *Ibid*.
[184] *Griessel* case (note 101 above) para 83.

> considered in conjunction with other factors such as the attitude of major creditors, whether the company has assets, whether there are other sources of funding and, depending on the circumstances of the case, whether there was an intention to implement a business plan that meets the avowed objectives of the Act and a reasonable prospect of the plan being implemented.

In other words, the court must take into consideration a number of factors including the sources of funding and whether there exists a reasonable probability that the plan was intended to be implemented. It is interesting to note that the court further held that:

> While good faith does not necessarily mean that a resolution will be saved from being set aside, want of good faith while not the sole factor to be taken into account should certainly play a significant, if not determinative, role in weighing up whether it is just and equitable to set aside the resolution.[185]

Courts have accepted that an application to set aside a resolution can be based on the ground that it is just and equitable to do so. In *DH Brothers Pty Ltd v Gribnitz NO and others*[186] the court made the following obiter remarks:

> Section 130(1)(a) gives to an affected person seeking to approach a court to set aside a resolution only three grounds, or causes of action, on which to base the application. In contrast to this, s 130(5)(a)(ii) empowers a court hearing an application brought under s 130(1)(a) to set aside a resolution on those three grounds but, in addition, to do so 'if, having regard to all of the evidence, the court considers that it is otherwise just and equitable to do so'. On the face of it, the court is empowered to set aside a resolution on four grounds but an applicant is only entitled to base an application on one or more of three grounds. In other words, an application cannot be based on this fourth ground because the application then would not qualify as one brought in terms of s 130(1)(a). The court is only entitled to grant relief in respect of an application brought in terms of s 130(1)(a).

Spilg J emphasized that the intervention of the court in some cases is necessary.[187] The need for the court to intervene is demonstrated in *Resource Washing Pty Ltd v Zululand Coal Reclaimers Proprietary Limited and others*[188] where the court set aside business rescue on just and equitable ground because of the deficiencies in the business rescue plan and noncompliance with section 150. The court held that:

> Challengingly at this nascent stage of the development of the Act the 'just and equitable' power that s 130(5)(a)(ii) confers on courts injects a degree of flexibility necessary to cater for the numerous circumstances that can arise to justify or not justify setting aside the resolution.

This means that the court in exercising its discretion may set aside a resolution by

[185] *Ibid* para 84.
[186] *DH Brothers* case (note 22 above) para 17.
[187] *Griessel case* (note 101 above) para 91.
[188] [2015] ZAKZPHC 21 para 64.

the board where the circumstances demand that it is just and equitable to do so.

The second and third ground that an applicant may base the application to set aside a business rescue resolution on is that there is no reasonable prospect that the company will be rehabilitated and that the board of directors failed to comply with the requirement stipulated in section 129. In *Vincemus Investments Pty Ltd v Louhen Carriers CC*[189] the Court said that what is intended by section 130 (1) (a) (iii) is the granting of a declaratory order, as the resolution that has for instance lapsed is a nullity *ex lege*.

Section 130 (1) makes it clear that an application to set aside a business rescue resolution must be made to the court. Thus, only the court can grant an order to set aside a resolution to place a company under business rescue. However, where an appeal has been lodged against these orders, the status of the company is uncertain.

The court in *Ex parte Nell NO and Others*[190] held that:

> The problem arises because of the following. Firstly, under the common law, noting of appeals did not suspend the operation of sequestration orders. Secondly, by operation of s 339 of the previous Companies Act, this common-law rule, as codified by s 150(3) of the Insolvency Act, was made applicable to an order winding up a company unable to pay its debts. Thirdly, under s 18 of the Superior Courts Act, the legislature has on the face of it created a situation in which (subject to the provisions of ss 18(2) and (3) which are of no present relevance) the operation and execution of *all* court "decisions" (which must include court orders) are suspended upon the lodging of an application for leave to appeal. Fourthly, s 132(2)(a)(i) of the new Companies Act provides that business rescue proceedings end when a court sets aside the resolution or order which began those proceedings.

The court acknowledged that there exists ambiguity between the old Companies Act and the New Companies Act but emphasized that ambiguity was not a problem in this case rather the problem was that these measures need to be interpreted to determine what must happen when a court makes an order to set aside a business rescue resolution made in terms of section 129 and placed the company under a liquidation and such an order has been appealed.[191] The legal question was, whether the business rescue immediately ends upon the order or does not end until the appeal process is finally exhausted and the appeal or appeals adjudicated.[192]

> To my mind there is an inconsistency between s 18 of the Superior Courts Act and s 132(2)(a)(i) of the new Companies Act. In these circumstances I

[189] 2013 JDR 0881 (GNP) para 17.
[190] 2014 (6) SA 545 (GP) para 45.
[191] *Ibid*.
[192] *Ibid.*

> find, against the submission of counsel for the practitioner, that s 5(4)(ii) of the new Companies Act is of application in the interpretation process.[193]

Therefore, the court concluded that the business rescue process ends when the court sets aside the resolution made by the board of directors.[194] The noting of an appeal against the order to place the company under liquidation is regulated by section 150 (3) of the Insolvency Act 24 of 1936 by virtue of the provision of Chapter XIV of the 1936 Act, with the effect that the provisions of the Insolvency Act will apply as if no appeal has been lodged, thereby placing the company under the control of liquidators.[195]

2.4.2 Commencement of business rescue by court order

2.4.2.1 Affected person

Section 131 (1) of the Act provides that where the board of directors has not resolved to place the company under business rescue, an affected person may apply to court for an order placing the company under supervision. In terms of section 128 (1) an ‘‘affected person’’, in relation to a company, means—

> (i) a shareholder or creditor of the company;
> (ii) any registered trade union representing employees of the company; and
> (iii) if any of the employees of the company are not represented by a registered trade union, each of those employees or their respective representatives;

The expression “affected person” is used as a generic term to describe, throughout Chapter 6, the principal stakeholders in the business rescue proceedings that is the creditors, shareholders and employees of the relevant company. The meaning of the term creditor is not defined in the Act, however, in *Resources Washing Pty Ltd v Zululand Coal Reclaimers Proprietary Limited and others*[196] the court stated that the word should bear its normal meaning. However, the ordinary meaning will depend on the application, for instance, in respect of winding up or business rescue. The Companies Amendment Bill[197] contained a definition of creditor in section 1 and provided that it will be a person to whom a company is or may become obligated in terms of any liability or other obligation that would be required to be considered by the company if it were applying the solvency and liquidity test as set out in section 4. This definition was not included in the final Bill. In terms of a similar section 411 of

[193] *Ibid* para 47.
[194] *Ibid* para 56.
[195] Delport (note 71 above) 472.
[196] *Resource Washing* case (note 188 above) para 30.
[197] B40 of 2010.

the Australian Corporations Act [198] (the equivalent of section 311 of the Companies Act of 1973) creditors are all persons with claims against the company for which proof of debt can be lodged, including persons with contingent claims.

Section 1 of the Act provides that "shareholder" means the holder of a share issued by a company and who is entered as such in the certificated or uncertificated securities register. Furthermore, in terms of section 57(1) shareholder also includes a person who is entitled to exercise any voting rights in relation to a company, irrespective of the form, title or nature of the securities to which those voting rights are attached. French, Mayson and Ryan opine that "[n]ormally, in a company limited by shares, every member is a shareholder, so that the term 'member' and 'shareholder' are synonymous."[199] This view is also echoed in *Shree Gopal Paper Mills Ltd v Commissioner of Income Tax, Central, Calcutta*,[200] where Datta J declared with no equivocation that in company law a member is a shareholder and a shareholder is a member.

However, Nwafor contends that "the terms 'shareholder' and 'member', though familiar corporate terms, are not necessarily coterminous and are often misused when describing persons with interests in the company. In a company that issues shares, a shareholder is not necessarily a member of the company and could in some cases never become a member of the company."[201] According to Nwafor, membership is acquired by the fulfilment of two conditions: the obtaining of the company's shares and entering of the name of the holder in the register of members.[202] This view is confirmed in *Commissioner of Inland Revenue v Crossman*[203] where Lord Russel of Killowen held that "[a] sale of a share is a sale of the interests so defined, and the subject-matter of the sale is effectively vested in the purchaser by the entry of his name in the register of members." In *Muir v City of Glasgow Bank*,[204] the entering of a name on the share register was seen by the court as real evidence of membership of a company. The court held that "anyone who is entered on the register of a company as a member in any capacity is quite simply a

[198] 50 of 2001 (the equivalent of section 311 of the Companies Act of 1973 and to an extent, section 155 of the Companies Act of 2008).
[199] D French, S. W Mayson and C. L Ryan, *Mayson, French and Ryan of Company Law 29th ed* (2012) at 167.
[200] [1967] 37 Comp Cas 240; AIR 1967 Cal 560 (CAL HC) para 35.
[201] A Nwafor 'The investors as a member of a company: A reflection on misused concept' (2013) Volume 20 Issue 1& 2 *Lesotho Law Journal* 30.
[202] *Ibid.*
[203] [1937] AC 26 at 66 (HL).
[204] (1878) 6 R 392.

member, with all the relevant right and liabilities."[205]

Therefore, the holder of a company's shares could rightly be referred to as a shareholder. However, such person is not a member of the company unless his name is entered in the register of members. It is important to note that for purposes of business rescue the shareholder must be a registered shareholder even if the entitlement to the shares is disputed. [206]

2.4.2.2 Notice of motion

An application by an affected person to place a company under compulsory business rescue must be in accordance with Form 2 (a) of the First Schedule to the Uniform Rules and such an application cannot be brought *ex parte*. In *Engen Petrolium Ltd v Multi Waste Pty Ltd and others*[207] Boruchowitz J observed that:

> The legislature appears to have been cognisant of the distinction between an *ex parte* application and an application brought using the long form notice of motion. Although in a different context, specific reference is made in s 129(5)(b) to the use of an *ex parte* application. It is safe to assume that had an *ex parte* application been intended in respect of applications brought under section 131(1), the legislature would have said so.

However, in *Oakdene Square Properties Pty Ltd v Farm Bothasfontein (Kyalami) Pty Ltd* [208] the High Court held that "the legislature has deemed it fit to prescribe motion proceedings in matters where an order is sought for the business rescue of a company. Despite that being the case, litigants and their legal representatives must count the costs of bringing matters to court on motion where disputes are to be expected."

2.4.2.2 Service to the Company and Commission

An applicant in terms of section 131 (1) of the Act must comply with section 131 (2). Section 131 (2) stipulates that

> An applicant in terms of subsection (1) must—
> (a) serve a copy of the application on the company and the Commission; and
> (b) notify each affected person of the application in the prescribed manner.

If an application is left at the office of the Commission and is not properly served in accordance with Rule 4 of the Uniform Rules it constitutes an irregularity. In *Engen Petrolium Ltd v Multi Waste Pty Ltd* [209] the Court said that "an application in terms of s131 (1) is clearly a document that initiates proceedings and is thus required to be

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[205] *Ibid* at 399.
[206] *Oakdene Square Properties* case (note 50 above) para 6.
[207] *Engen Petroleum* case (note 182 above) para 16.
[208] Oakdene Square case (note 109 above) para 2.
[209] *Engen Petroleum* case (note 182 above).

served by the sheriff." Furthermore, in *Taboo Trading 232 Pty Ltd v Pro Wreck Scrap Metal CC and others*[210] the Court held that

> For reasons with which I fully agree, Boruchowitz J, in *ENGEN PETROLEUM v MULTI WASTE (PTY) LTD AND OTHERS* held that an application in terms of s 131 of the Companies Act, must be brought in accordance with Form 2(a) of the First Schedule to the Uniform Rules of Court, that is to say, in the long form of the notice of motion. I also agree with Boruchowitz J that insofar as service on the Commission in terms of s 131(2)(a) is concerned, service by the Sheriff, in terms of Rule 4 of the Uniform Rules of Court is required. Notification of affected persons, in terms of s 131(2)(b), must comply with the requirements of regs 7 and 124, read with Table CR3, as well as the requirements of ss 6(10) and (11) of the Act. I also agree with Boruchowitz J that a failure to comply with these requirements constitutes an irregularity.

Section 131 (2) also requires the applicant to notify each affected person in a manner prescribed in Regulation 124. Regulation 124 stipulates that:

> An applicant in court proceedings who is required, in terms of either section 130 (3)(b) or 131 (2)(b), to notify affected persons that an application has been made to a court, must deliver a copy of the court application, in accordance with regulation 7, to each affected person known to the applicant.[211]

In *Cape Point Vineyards Pty Ltd V Pinnacle Point Group Ltd*,[212] Rogers AJ observed that "to notify someone of an application would be to tell the person that the application has been launched. Effectively regulation 124 requires service of the whole application on all affected parties. In so doing, regulation 124 may well travel beyond what may lawfully be prescribed under section 131(2) (b)." In other words, the requirement in regulation 124 is far-fetched and problematic since a company could have thousands of stakeholders and neither physical delivery nor sending such heavy file by email may be feasible.

However, a contrary view was adopted in *Kalahari Resources Pty Ltd v Arcelor Mittal SA.* [213] The court held that:

> I am of the respectful view that the court in *Cape Point Vineyards* case was probably justified in its criticism of Regulation 124, namely, that it went beyond what might lawfully be prescribed under section 131(2)(b) of the new Companies Act, insofar as it required service of the whole application and that such service in most instances would not be practically feasible. However, the requirements of Regulation 124 cannot just be ignored, or be regarded as pro non scripto. Until declared invalid and set aside the requirements of that regulation would have to be complied with.

The court held further that section 6(11) (b) of the new Companies Act provides a solution when it is not practically feasible to deliver the whole application because of

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[210] 2013 (6) 141 (KZP) para 10.
[211] The Companies Regulation 2011.
[212] *Cape Point Vineyard* case (note 174 above) para 16.
[213] [2012] 3 ALL SA 555 (GSJ) para 60.

its bulk.[214] That section provides that it is sufficient delivery if a notice is delivered to each intended recipient making known the document that is to be delivered is available, contains a summary of the contents of the document, complies with any prescribed requirements and gives instructions to the intended recipients as to how to get access to the document.[215]

2.4.2.3 Directions for the Court

Section 131(4) provides for the grounds on which an application for business rescue may be based. It states that;

> 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 financially distressed;
> (ii)the company has failed to pay over any amount in terms of an obligation under or in terms of a public regulation, or contract, with respect to employment-related matters; or
> (iii) it is otherwise just and equitable to do so for financial reasons, and there is a reasonable prospect for rescuing the company;

The first ground on which to base an application for business rescue is that the company is financially distressed. [216] The business rescue proceedings is intended to be used at the earliest possible moment when a company is showing signs of pending insolvency but where it has not yet reached the state of actual insolvency. In *Walman v Marcelle Props 193 CC and Another*[217] the court emphasized that "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." In other words, a court must grant an order placing a financially distressed company under supervision if there is a reasonable prospect that it can be revived.

The second ground is that the company has failed to pay any amount due to its employees, creditors or in terms of a public regulation. The wording 'any' strongly implies that only one missed payment will suffice. Cassim describes the second threshold as "unduly harsh, with an element of overkill."[218] This may be regarded as a fair assessment of the provision in that a technical default may be renegotiated or remedied without the need for a business rescue. It is not clear what the justification is for including this as a ground upon which the Court may grant an order for the

[214] *Ibid* at 60.
[215] *Ibid* at 60.
[216] Section 131(4) (i).
[217] [2012] JOL 28714 GSJ.
[218] Cassim (note 8 above) 847.

commencement of business rescue proceedings.[219] The same ground does not apply under section 129 or 130, and can only have been included in order to assist registered unions in bringing applications for compulsory business rescue proceedings in circumstances where they perhaps do not have information relating to whether or not the company is financially distressed.[220]

Thirdly, section 131(4)(iii) provides that a court may grant an order for compulsory rescue proceedings if it is just and equitable to do so. It is not clear what the legislature intended by including the first part of this ground upon which a company may be placed under compulsory business rescue proceedings.[221] The Court in *Oakdene Square Properties Pty Ltd v Farm Bothasfontein (Kyalami) Pty Ltd* [222] held that:

> The phrase "it is otherwise just and equitable to do so for financial reasons" is extremely vague.[223] The immediate question arises: "for financial reasons of whom, the company, the creditors, shareholders or the employees? Since the company cannot apply to court for a business rescue order, as it is not an "affected" person, one can immediately say that the financial reasons of the company are not referred to. However, that would render this provision absurd as it is primarily the financial health of the company which is at stake. I have little doubt that the Legislature never intended such absurdity. I would, therefore, hold that financial reasons relating to all the stakeholders, except that of the practitioner, contemplated in the business rescue provisions, are to be considered by the court when applying this provision.

A better understanding of the phrase may be found in case law that explains the meaning of section 344 which states that a company may be wound up by the Court if it appears to the court that it is just and equitable that the company should be wound up. In *Moosa NO v Mavjee Bhawan Pty Ltd* [224] Trollip J pointed out that the phrase 'just and equitable' "postulates not facts but only a broad conclusion of law, justice and equity." A clearer explanation is in *Erasmus v Pentamed Investments (Pt) Ltd,*[225] where the court held that "it affords the court a wide judicial discretion in the exercise whereof, however, certain other sections of the Act must be taken into account."

The expression "just and equitable" is not to be interpreted is such a manner as would only include matters *ejusdem generis* the other grounds specified in that

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[219] Delport (note 71 above) 480.
[220] *Ibid.*
[221] *Ibid* 480 (1).
[222] *Oakdene Square Properties* case (note 109 above) para 17.
[223] A Loubser 'The Business rescue proceedings in the Companies Act of 2008: concerns and questions (part 1) (2010) 3 TSAR AT 510.
[224] 1967 (3) SA 131 (T) at 136.
[225] 1982 (1) SA 178 (W) at 181.

provision.[226] In *Moosa NO v Mavjee Bhawan Pty Ltd*[227] the court said that the just and equity are those between the competing interests of all concerned. In the case of business rescue it means the competing rights of creditors, shareholders and employees. In *Kalahari Resources Pty Ltd v Arcelormittal*[228] it was held that:

> There is ample authority that an applicant who relies on the ground that it was just and equitable to liquidate a company, [i.e. under the previous Companies Act], must come to court with clean hands. In other words, it must not itself have been wrongfully responsible for, or have connived at bringing about the state of affairs, which it asserts results in it being just and equitable to wind up the company.[229]

There is no reason why the same principle cannot also apply in the case of business rescue proceedings.[230]

2.4.2.4 Business rescue versus liquidation proceedings

Section 131(6) provides that where liquidation proceedings by or against the company had already commenced, the application for business rescue can still be instituted. In response to this proceedings the courts have refused to postpone the issuing of provisional liquidation orders to give opportunity to affected persons to apply for business rescue.[231] It is important to state that upon applying for the commencement of business rescue such application suspends liquidation proceedings that have already begun until the court has adjudicated on the application for business rescue.[232] Thus, if the application is granted, liquidation proceedings are suspended, until business rescue is completed

This provision has been met with rigorous criticism to an extent that it is described "as badly worded and incomplete." [233] This criticism is justified because indeed it is not clear whether liquidation proceedings refer only to the legal proceedings until final order is issued or to the whole process of winding-up until liquidation and distribution account has been approved. In *Van Staden v Angel Ozone Products CC (in Liquidation)*[234] the court rejected the argument that only liquidation proceedings were meant. Rather it held that proceedings in this context mean the whole liquidation

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[226] *Emphy v Pacer Properties Pty Ltd* 1979 (3) SA 363 (D) at 365.
[227] *Moosa* case (note 224 above) para 136.
[228] *Kalahari Resources* case (note 213 above) para 72.
[229] See *Wackrill v Sandton International Pty Ltd* 1984 (1) 282 (W) at 292, *Lawrence v Lawrich Motors Pty Ltd* 1948 (2) SA 1029 (W) at 1030-1033 and Marshall v Marshall Pty Ltd 1954 (3) SA 571 (N) at 579.
[230] *Kalahari Resources* Case (note 213 above) at 72.
[231] For instance, in *FirstRand Limited v Imperial Crown Trading 143 Pty Ltd* 2012 4 SA 266 (KZD).
[232] Section 131(6).
[233] Davis (note 1 above) 244.
[234] [2012] ZAGPHC 328 (NGP).

process until a final liquidation and distribution account is approved. This implies that even after a liquidation order has been granted an affected person can still apply for business rescue order.[235] Davis maintains that this is an extremely unsatisfactory situation since an almost completed winding up may now be summarily halted by simply filing a spurious and baseless application for commencement of business rescue proceedings.[236] A far more sensible approach would have been for the legislature to limit an application for business rescue to the period before a final liquidation order is issued or at least to provide that the liquidation proceedings will only be suspended from the moment when (and if) the court grants an order for commencement of business rescue proceedings.[237]

Although it seems that the interference of business rescue on liquidation proceedings may result in serious inconveniences, Cassim maintains that "to the extent that business rescue overrides liquidation proceedings these provisions are in accord with the underpinning policy of preserving viable commercial enterprises rather than shutting them down. It also underscores the approach that business rescue is an alternative to liquidation of the company."[238]

In the light of this observation one is inclined to argue that the enquiry as to the meaning of 'liquidation proceedings' would not be necessary if liquidation proceedings are not initiated until business rescue proceedings have ended. In other words, logic would dictate that before liquidating a company one should attempt to rescue it.

It is also not clear when will business rescue proceedings commence where an application for commencement has been lodged in terms of section 131. In *Investec Bank Ltd v Bruyns*[239] the court acknowledged that the Act was not clear as to the exact time of commencement and a problem that the courts would have to decide in due course, but decided that in that particular case it was not necessary to do so.

The court has the power to make an order for the commencement of business rescue at any time during the course of liquidation or proceedings to enforce security against the company.[240] This simply means that the court may issue a business rescue order on its own accord. In such a case, the term 'liquidation proceedings' must be construed to mean court proceedings because the company would not have initiated

[235] Section 131 (6).
[236] Davis (note 1 above) 245.
[237] *Ibid.*
[238] Cassim (note 8 above) 875.
[239] 2012 (5) SA 430 (WCC).
[240] Section 131(7).

the proceedings.[241] In this scenario, business rescue commences when the court makes the actual order for commencement of business rescue.[242]

2.4.2.5 Possible court orders

Section 131 provides that where the court is satisfied that a commencement order is appropriate in consideration of the merits of the case presented before the court, it may also make further order appointing an interim business rescue practitioner. The affected person who made the application has the right to nominate such interim practitioner, provided that the prospective interim practitioner is qualified as a business rescue practitioner as contemplated in the Act.[243] This appointment however, must be ratified by independent creditors, at the first meeting of creditors, who hold a majority of the voting rights.[244]

If the application is dismissed, the court may make any further necessary and appropriate order. Thus, in exercising its discretion the court may order that the company be placed under liquidation rather than business rescue.[245] Conversely, in terms of section 131(7) the court may make an order to place a company under business rescue during liquidation proceedings or proceedings enforcing any security against the company.

With regards to costs of a successful application, section 131 is not clear. However, it may be presumed that such costs are payable as one of the expenses of the business rescue process. The case of *Cape Point Vineyards Ltd v Pinnacle Point Group Ltd,*[246] provides a better understanding of the legal position of an affected party who applied for an order for commencement of business rescue. In that case the court held that if the applicant in a business rescue application were not granted costs, and if the rescue proceedings succeeded and the company is restored to complete financial health, the applicant would be worse off than all affected persons, since he would have to recoup his legal costs out of his claim as a creditor or out of the value of his shareholding as the case may be. This would serve as a disincentive for affected persons bringing proceedings under section 131. Yet if the applicant were to apply for liquidation proceedings his or her costs would form part of the costs of liquidation.[247]

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[241] Davis (note 1 above) 245.
[242] Section 132(1)(c).
[243] Section 138.
[244] Section 131(5).
[245] Section 134(4).
[246] *Cape Point Vineyard* case (note 174 above).
[247] *Ibid*.

The court held that costs of an application fall within the scope of section 135 (3) as a claim arising from the costs of business rescue proceedings. The court further emphasized that the High Court has inherent jurisdiction to make an order for cost in proceedings brought in terms of section 131. This would mean that such an order is supposed to be taxed on an attorney and client scale. Lastly, it is the duty of the company and not the applicant (affected person) to notify each affected person within a period of five days after an order has been granted to commence business rescue proceedings in terms of section 131.[248]

2.5 Abuse of process

The courts are on guard against the use of business rescue for strategic purposes. *Swart v Beagles Run Investments 25 Pty Ltd and others*[249] is a good example of this tendency. In that case the applicant was a sole director and shareholder of the respondent. He applied for the commencement of business rescue in terms of section 131(4) on the ground that the company was financially distressed. However, creditors raised objections against the application. The objections were based on the grounds that the application was an abuse of the process and that it was intended to postpone payment of debts. The court was satisfied that the applicant was indeed insolvent and intended to delay the payments of debts. The court rejected the application and stated that "where an application for business rescue entailed a weighing up of the interests of creditors against those of a company, the interests of the creditors should prevail."

2.6 Conclusion

From the above discussion, it is evident that business rescue means the proceedings aimed at rehabilitating a financially distressed company. The underlining philosophy is that the value of a business as a going concern will be greater than its liquidation value. In an effort to achieve that the proceeding must be applied in a manner that balances the rights of all stakeholders. Hence the process is meant to be a speedy and cost efficient process.

There are two ways of initiating business rescue. It is either the board of directors of a company passes an initiating resolution or an affected person may apply to the Court for an order to place the company under supervision. In each case the board or the affected person must first assess whether the company is financially distressed, if so whether there is a reasonable prospect that the company may be rehabilitated.

[248] Section 133 (1).
[249] 2011 (5) SA 422 (GNP).

Although the objectives of business rescue are noble and commendable the drafting errors of the provisions have left loopholes on the Chapter 6 lifeboat. However, the cases discussed in this chapter evince that the courts in interpreting Chapter 6 provisions endeavor to comply with section 5 (1) which dictates that this Act must be interpreted and applied in a manner that gives effect to the purposes set out in section 7. Section 7(k) states the main objective of business rescue. It states the purpose of the Act is to "provide for the efficient rescue and recovery of financially distressed companies, in a manner that balances the rights and interests of all relevant stakeholders." Attaining this purpose is seemingly the primary aim of the courts while interpreting the various provisions. The following chapter discusses the significance of a business rescue practitioner.

CHAPTER THREE

3. THE BUSINESS RESCUE PRACTITIONER

3.1 Introduction

According to the Cork Report, the achievement of an efficient and reliable insolvency system relies upon its administrators, "If they did not have the respect and confidence of the courts, the creditors, the debtors and the general public, the insolvency system would fall into disrepute and disuse."[250] During business rescue the business rescue practitioner whose role is similar to that of the administrator gives direction to the proceedings. The practitioner drafts the business rescue plan and supervises the company's management in the implementation of the plan. Therefore, the success of corporate rescue relies heavily upon the competency and expertise of the business rescue practitioner. Hence, in assessing the efficacy of Chapter 6 provisions it is pertinent to consider the functions and terms of appointment of the business rescue practitioner.

3.1.1 The meaning of business rescue practitioner

In terms of Chapter 6, business rescue practitioner means a person appointed, or two or more persons appointed to work jointly, to oversee the company during its business rescue proceedings.[251] In other words, a business rescue practitioner is a person appointed to supervise the affairs of a company in financial distress. Delport is of the view that although the definition envisages the possibility of appointing more than one business rescue practitioner to oversee the rescue of a company, none of the other provisions of Chapter 6 appear to cater for this possibility.[252] For instance, none of the provisions dealing with remuneration of the business rescue practitioner makes provision for the division of fees where more than one practitioner has been appointed or for the mechanism that must be applied should a dispute arise.

It is imperative to take cognizance of the fact that in terms of section 1 of the Act the term "person" includes a juristic person. Therefore, it is conceivable that a corporation or a firm may be appointed as a business rescue practitioner.[253] This is, however, in contrast to the Insolvency Act, and Chapter XIV of the Companies Act

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[250] The Report of the Insolvency Review Committee on Insolvency Law and Practice 1982 Cnmd 8558 para 758. This report is also known as the "Cork Report." The chairperson of the Committee was Kenneth Cork. The Cork Report led to the promulgation of the Insolvency Act of 1986 and elements of the Act have been adopted by the Enterprise Act of 2002. The author will make reference to legislation applied in the United Kingdom.
[251] Section 128.
[252] Delport (note 71 above) 451.
[253] *Ibid*.

1973, where only a natural person may be appointed as a trustee or liquidator.[254] It is not clear whether this is an anomaly or whether it was intentional. Because of this lack of clarity there exists an incongruity that may give rise to controversial arguments.

Dworkin is of the view that a proposition can be true even if it cannot be proved to be true to everyone's satisfaction.[255] This is the position with the following proposition; it is submitted that the Act only contemplates the appointment of a natural not juristic person as a business rescue practitioner. This is deduced from section 138(i)(d) which states that a person may be appointed as the business rescue practitioner of a company only if the person would not be disqualified from acting as a director of a company in terms of section 69(8). Whereas, section 69(8)(b)(ii) stipulates that a person is disqualified to be a director of a company if the person is prohibited in terms of any public regulation to be a director of a company. A public regulation includes an Act of parliament such as the Companies Act of 2008. According to section 69(7)(a) of the Act a person is ineligible to be a director of a company if the person is a juristic person. In the light of these provisions, it is submitted that a juristic person may not be appointed as a business rescue practitioner.

Loubser states that there exist similarities between the South African requirements for appointment of a business rescue practitioner and the German Insolvency Code requirements.[256] With that in mind, section 56 of the German Insolvency Code stipulates that only a natural person can be appointed. Thus, in terms of the German Insolvency Code it is not possible to appoint a company or even a firm that will nominate an individual to act. Braun is of the view that "the parliamentary committee amended the original draft legislation that provided for the appointment of firms, because they foresaw difficulties in respect of conflicts of interest and the personal liability of the insolvency administrator for damages caused by a breach of his duties."[257] The difficulties that were avoided by the German parliament are the same difficulties faced by the South African courts in the interpretation and application of the Chapter 6 business rescue. The Act does not adequately regulate the possibility of the appointment of a juristic person. Chapter 6 does not regulate the following aspects that are essential for the smooth regulation of a juristic person appointed as a business rescue practitioner, it does not stipulate;

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[254] Delport (note 71 above) 452.
[255] D Meyerson *Jurisprudence* (2011) 174.
[256] A Loubser 'Some comparative aspects of corporate rescue in South African Company Law) unpublished LLD Thesis University of South Africa (2010) 287.
[257] E Braun *Commentary on the German Code* (2006) at 158 para 479.

- what happens if the juristic person appointed as business rescue practitioner is also financially distressed,
- the qualifications of a juristic person who wishes to be appointed as a business rescue practitioner. At present the qualifications mostly relate to natural persons,
- the allocation of liability if the juristic person fails to perform its duties as a business rescue practitioner, and
- the removal of juristic person as a business rescue practitioner.

Appointing a juristic person in terms of the current Chapter 6 provisions would be challenging and almost impossible.

3.1.2 Appointment of business rescue practitioner

A business rescue practitioner may be appointed by the board of directors or the court upon application by an affected person.

3.1.2.1 Appointment by board of directors

If business rescue proceedings are initiated by the company in terms of section 129, the board of directors is also required to appoint a business rescue practitioner within a period of five business days after filing the initiating resolution with the Companies and Intellectual Property Commission.[258] The appointed practitioner must meet the requirements provided in the Act and he or she must consent to the appointment in writing.[259] Furthermore, within two business days, a notice of the appointment must be filed with the Commission and must be published to all affected within five days.[260] Cassim notes that:

> There is consequently a possible five-day period in which a company under business rescue is not under the control of or supervision of a business rescue practitioner. It is thus within the contemplation of the Act that business rescue proceedings may be commenced without a business rescue practitioner. Presumably, although there is no explicit provision to this effect, during this period of five days, the company or its directors may not dispose of the assets of the company. This is left unclear.[261]

Despite the fact that the five days' period is not catered for in the Act, strict adherence is required. In other words, failure to adhere to the prescribed time nullifies the resolution.[262] In *Madodza Pty Ltd (in business rescue) v ABSA Bank Ltd*[263] the business rescue resolution was held to be void because the business

[258] Section 129(3)(b).
[259] Section 129(3)(b).
[260] Section 129(4)(a) and (b).
[261] Cassim (note 8 above) 869.
[262] Section 129(5)(a).
[263] [2012] ZAGPPHC 165 para 26.

rescue practitioner had not been appointed within five days after filing of the resolution.

The innovative part of Chapter 6 with regards to the appointment of a business rescue practitioner is that; an affected person who is of the view that the appointed business rescue practitioner is not adequately qualified may apply to the court to set aside the appointment in terms of section 130. Bradstreet commends that provision in that if a business rescue practitioner is appointed by the board of directors, it is prudent and cost effective that the practitioner be removed by a resolution of the majority of independent creditors holding voting rights at meeting of creditors.[264]

3.1.2.2 Appointment by court order

If affected person has applied for compulsory business rescue in terms of section 131, the applicant is allowed to nominate a prospective candidate for appointment as a business rescue practitioner. Such candidate may be appointed as an interim business rescue practitioner,[265] "subject to ratification by the holders of a majority of the independent creditors voting interest at the first meeting of creditors" [266] Loubser observes that :

> Although the use of the word "may" in section 131(5) appears to give the court a discretion whether to appoint an interim business rescue practitioner or not, it is difficult to imagine how an order for business rescue proceedings can be issued and implemented without such an appointment. Unlike the position under a provisional judicial management order, there is no provision for the temporary custody of the company's assets until the appointment of a business rescue practitioner. Furthermore, whereas the Master of the High Court is tasked with convening the first meetings of creditors in judicial management, in business rescue proceedings this is the duty of the (interim) business rescue practitioner. Without a business rescue practitioner, this will simply not happen and the business rescue proceedings will not progress.[267]

Under the circumstances Loubser recommends that "the provision should be amended to make the appointment of an interim business rescue practitioner by the court obligatory if an order for commencement of business rescue proceedings is granted."[268] An illustration of this provision is demonstrated in *Van Nierkerk v Seriso 321 (FirstRand Bank Ltd intervening)*[269] In that case, the court had appointed a business rescue practitioner but FirstRand bank had submitted that it wanted to nominate a business rescue practitioner of its own choice and the court held that:

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[264] R Bradstreet 'The leak in chapter 6 lifeboat: inadequate regulation of business rescue practitioners may adversely affect lenders' willingness and the growth of the economy (2010) Volume 22 Issue 2 *South African Mercantile Law Journal* 202-203.
[265] Section 131(5).
[266] Section 131(5).
[267] Loubser (note 256 above) 96.
[268] *Ibid* 97.
[269] 23929/2011 20 March 2012 (CC) at para 34.

"FirstRand [is] entitled to raise any concerns regarding the appointment of the interim practitioner at the first meeting, there being nothing to suggest that the appointed practitioner does not meet the requirements of section 138."[270]

The Act provides that where the court has set aside the appointment of a business rescue practitioner appointed by the company, the same court must also appoint another business rescue practitioner who satisfies all the requirements stipulated in Chapter 6.[271] If a practitioner resigns, or is removed from office or dies a new practitioner must be appointed by the board of directors or the creditors depending on who made the initial appointment.[272]

3.1.2.3 Requirement of security

Business rescue practitioners are not in the normal course of events required to furnish security in order to secure the interests of the company and affected persons.[273] It is only the business rescue practitioner appointed by the board under voluntary business rescue procedure in terms of section 129 who is required to furnish security and only upon application by an affected person.[274] If this aspect of the practitioner's appointment is not challenged under a voluntary business rescue proceeding, the practitioner may never be required to furnish security for the proper performance of his duties.[275] However, the business rescue practitioner appointed by the court in terms of section 131 may not furnish security for the proper performance of his duties.

It is an acceptable practice under South African law that liquidators and trustees must provide security for the due performance of their duties.[276] More importantly, section 431(4) read with section 375 (1) of the Companies Act of 1973 envisage that judicial managers are also required to furnish security. In *Exparte Finnemore NO*[277] the court held that "the sole object for taking security is to indemnify creditors and contributors. The liquidator must give and the Master must require security for the due performance of the liquidator's duties." [278]

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[270] *Ibid* para 35.
[271] Section 130(1)(b).
[272] Section 139(3).
[273] Delport (note 71 above) 474.
[274] *Ibid*.
[275] *Ibid*.
[276] Section 368, 375(1), 429(b)(i) and respectively of the Companies Act of 1973, and section 18(1) and 56(2) of the Insolvency Act of 1936.
[277] 1948 (2) SA 621 (T).
[278] *Ibid* at 625.

Loubser notes that the current position is "in contrast with the current principle of corporate and insolvency law. Therefore, it is difficult to understand why this principle was not adhered to in the appointment of a business rescue practitioner as well, considering that he is put in control of the management and quite probably of substantial assets of a company."[279] Thus considering the powers vested and the position of trust that business rescue practitioner occupies, providing security should be a prerequisite for his or her appointment.[280]

3.1.3 Qualifications of a business rescue practitioner

The qualifications of a business rescue practitioner are regulated in terms of section 138(1). Davis points out that the original version of section 138 envisaged the creation of a dedicated profession of business rescue practitioners who would have been regulated by a regulated authority that functioned "predominantly to promote sound principles and good practice of business turnaround or rescue."[281] This plan however was not followed. The current qualifications for appointment as a business rescue practitioner are fivefold. Section 138(1) sets down those requirements as follows:

> (a) is a member in good standing of a profession subject to regulation by a regulatory authority prescribed by the Minister in terms of subsection (2);
> (b) is not subject to an order of probation in terms of section 162(7);
> (c) would not be disqualified from acting as a director of the company in terms of section 69(8);
> (d) does not have any other relationship with the company such as would lead a reasonable and informed third party to conclude that the integrity, impartiality or objectivity of that person is compromised by that relationship; and
> (e) is not related to a person who has a relationship contemplated in paragraph (d).

Under the English Insolvency Act, a person may not be appointed as an insolvency practitioner (business rescue practitioner) if he is an unrehabilitated insolvent or if he is disqualified from being appointed as such or he or she is a mentally ill person or lacks capacity.[282] Furthermore, section 389(1) of the Insolvency Act 1986 provides that if a person who is disqualified from being appointed as an insolvency practitioner practices as such he or she would have contravened the Insolvency Act for which the offender may be required to pay fine or be imprisoned. Unfortunately, chapter 6 provisions do not include these restrictions and sanctions. The requirements of section 138(1) are now examined in some detail.

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[279] Loubser (note 256 above) 81.
[280] *Ibid*.
[281] Davis (note 1 above) 254.
[282] Section 390(4) of the English Insolvency Act of 1986.

3.1.3.1 Member of a regulated profession

Section 138 (1)(a) provides that a person may be appointed as the business rescue practitioner of company only if the person is a member in good standing of a legal, accounting or business management profession accredited by the Commission. Papaya postulates that "the section presupposes membership to a pre-existing profession and thereafter adds the requirement of accreditation."[283] Regulation 126(1)(a) (Companies Regulations, 2011) states that the Commission must, when considering an application for accreditation of a profession under s 138(1), "have due regard to the qualifications and experience that are set as conditions for membership of any such profession, and the ability of such profession to discipline its members. The Commission may revoke any such accreditation if it has reasonable grounds to believe that the profession is no longer able to properly monitor or discipline its members."[284] This points to a heavy reliance on the manner in which these professions are able to adequately regulate their own affairs. Peradventure such professional bodies fail to regulate their professionals this will have a ripple effect on the efficacy of appointed business rescue practitioners.

It therefore becomes relevant to analyse the professional bodies envisaged in the Companies Act.[285] Section 138(1)(a) explicitly states that practitioners are to be appointed from the legal, accounting and business management professionals. The legal profession is regulated by the four law societies while the accounting profession is regulated by the South African Institute of Chartered Accountants (SAICA) and to a certain extent business management professionals are governed by the Turnaround Management Association (Southern Africa).[286] The Act makes the assumption that these professional bodies are adequately equipped to regulate the conducts of their members who in turn will be appointed as business rescue practitioners.[287] The relationship between such bodies and the CIPC would have to be well-defined in order for the regulation of business rescue practitioners to be effective.[288]

The Act stipulates that the member of these professional bodies must be in good standing with their respective profession.[289] Meskin is of the view that although this provision requires that a person be a "member in good standing" of the relevant

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[283] R Papaya 'Are business rescue practitioners adequately regulated" (2014) Volume 2014 Issue 548 *De Rebus* 29.
[284] *Ibid*
[285] *Ibid*.
[286] *Ibid*.
[287] *Ibid* 30.
[288] *Ibid*.
[289] *Ibid.*

professional body, no provision has been made for the professional body concerned to inform the Commission when a person is no longer a member in good standing for example where an attorney has been struck off the roll.[290] Conversely it is plausible that the onus might lie on the CIPC to ascertain the standing of a practitioner within their professions before appointment. Alternatively, periodic checks regarding a practitioner's standing may also be necessary.

Meskin is of the view that the business rescue profession has primarily been designed to accommodate professionals that are active in the legal, accounting and business management spheres. The fact that persons who are not legal, accounting and business management professionals may also be licensed to practice as business rescue practitioners, suggests that other persons outside these professional spheres such as insolvency practitioners, should also be accommodated if they are suitably qualified.[291] The German Constitutional court has held that acting as an administrator (business rescue practitioner) "is a separate and recognized profession in its own right and therefore is not limited to lawyers or any other professionals." [292]

3.1.3.2 Not subject to order of probation

A prospective business rescue practitioner must not be the subject of an order of probation in terms of section 162. Davis states that since an order of probation may only be issued against a director, who may be an individual, it is unclear how this requirement can be applied to a juristic person who is appointed as a business rescue practitioner.[293] Thus, an interpretation of section 128(d) should not include a juristic person because the provisions of Chapter 6 mostly accommodate natural persons than juristic person.[294] A court may make an order placing a person under probation if the person is a director who; [295]

- Failed to vote against a resolution at a board of director's meeting despite that the company had failed to satisfy the solvency and liquidity test;[296]
- Acted in a manner that is substantially contrary to the duties and obligations of a director;[297]
- Condoned or supported an undertaking by the company to act in a manner that was repressive or unfairly prejudicial in terms of section 163; or[298]

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[290] P Meskin *Insolvency Law and its operation in winding up* Issue 47 (2016) 18-80.
[291] *Ibid*.
[292] BverfG V 92.2005 – 1 BvR 2719/04.
[293] Davis (note 1 above) 255.
[294] See also Subheading *3.1.1 The meaning of business rescue practitioner*.
[295] Section 77(4) see also *Motale v Abhlobo Transport Services (Pty) Ltd and others* [2015] JOL 34696 (WCC).
[296] Section 162(7)(a)(i),
[297] Section 162(7)(a)(ii).

- "Within any period of ten years after the effective date, was a director of more than one company or a managing member of more than one close corporation, and during that time two or more of those companies or close corporations had each failed to pay its creditors or meet its obligations."[299]

The exception to the last ground is where the company or corporation failed as a result of a business rescue plan made by the board of directors in terms of section 129 or a compromise with creditors in terms of section 155 of the Act. However, in terms of section 162(8)(b) a court may declare a director under probation in terms of this ground only if it is satisfied that the manner in which the enterprise was managed led to demise of the company and that the declaration is justified, in view of the circumstances of the corporation's failure, and the director's conduct in discharging his managerial duties at the time. Thus, a director who falls under the stated category cannot be appointed as a business rescue practitioner even if qualified in other respects.

3.1.3.3 Not disqualified as a director

A person disqualified from being a director is not qualified to be appointed as a business rescue practitioner.[300] Section 69(8) provides a list of persons disqualified from being a director of a company. Any person

- forbidden by the court from becoming a director;
- declared to be delinquent by the court;
- who is an insolvent;
- who was proscribed to be a director of a company in terms of any public regulation;
- who was disqualified from being appointed as a trustee because he or she was fraudulent and dishonest in performing his duties.
- who is a convict who has committed theft, fraud, forgery, perjury or other offences specified in section 69(8)(b)(iv) of the Act.

In *Re Magna Alloys and Research Pty Ltd*[301] the court held that these provisions are not designed to punish the individual, but "to protect the public and to protect the corporate structure from being used to the financial detriment of investors, shareholders, creditors and persons dealing with the company. In its operation, it is

[298] Section 162(7)(a)(iii).
[299] Section 162(7)(b).
[300] Section 138.
[301] (1975) 1 ACLR 203 SC (NSW) 205.

calculated to act as a safe guide against the corporate structure being used by individuals in a manner which is contrary to proper commercial standards." With that in mind, the business rescue procedure in Chapter 6 requires a person who is honest, trustworthy and diligent, and as such the legislature saw it fit to disqualify any person who is disqualified to hold the office of director to protect the interest of creditors, shareholders and the public.

3.1.3.4 Independent of the company and its management

Meskin notes that although section 138(1)(e) has not been clearly articulated, it is clear that the purpose of the provision is to ensure that the business rescue practitioner has not had any prior dealings with the company in which he is appointed that would place his independence and impartiality in doubt.[302] However, Delport observed that section 138(1)(e) could simply have stated that the business rescue practitioner must be independent of the company and its management, which is the wording used in section 130(1)(b)(ii) as a ground for the removal of the business rescue practitioner where it is shown that he is not independent of the company or its management.[303]

Despite the purpose of these provisions, the court in *Copper Sunset Trading 220 Pty Ltd v Spar Group Ltd and another*[304] refused to uphold a point raised *in limine* by the respondents that the business rescue practitioner should have been precluded from being appointed in terms of section 138 (1) (e) because he had been the attorney for the company prior to the company being placed under supervision. The court stated that:

> Nowhere in their answering affidavits do the first and second respondents allege or show the factual basis on which it can be said that [the practitioner's] integrity, impartiality or objectivity was compromised by the mere fact that he acted as attorney of record for the applicant prior to the commencement of the business rescue proceedings. In any event the respondents never raised any objection to [the appointment] at any of the three creditors meeting already held. They have acquiesced to his position as the duly appointed business rescue practitioner.

From this case, it would seem that an attorney of a company may be appointed as a business rescue practitioner to that company. If creditors have objections to the appointment of such a practitioner, such objection must be raised timeously when the process of the appointment is initiated.

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[302] Meskin (note 290 above) 18-81.
[303] Delport (note 71 above) 484.
[304] 2014 (6) SA 214 (LP) para 20.

3.1.3.5 Not related to person with compromising relationship

The meaning of relationship in this context is found in section 2(1)(a) which provides that for all purposes of this Act-

> (a) an individual is related to another individual if they-
> (i) are married, or live together in a relationship similar to a marriage; or
> (ii) are separated by no more than two degrees of natural or adopted consanguinity or affinity;

This implies that spouses or life partners cannot be appointed as business rescue practitioners by companies that employed their spouses or life-partners. This also includes persons that are closely related (blood relatives) or adopted relatives.

3.1.2.6 Experience

Currently business rescue practitioners are nominated and appointed in consideration of their experience.[305] This office has been categorized into three namely; senior, experienced and junior business rescue practitioners.[306] In terms of Regulation 127 a senior business rescue practitioner is eligible to supervise a large or medium size company.[307] Thus a nominee for a post as a business rescue practitioner for large companies must satisfy the requirements of section 138 and must be presently engaged in business turn around practice. More so, he or she must have practiced as such for a combined period of ten years.[308]

An experienced business rescue practitioner may only assist a senior business rescue practitioner for a large state-owned company.[309] In practice, experienced business rescue practitioner is eligible to supervise the rehabilitation of medium sized companies.[310] Whereas, junior business rescue practitioners may manage a small business enterprise whose public interest score is less than a hundred.[311] It is important to note that a junior business rescue practitioner may only assist a senior business rescue practitioner or experienced business rescue practitioner for a medium or large company or state-owned company.[312]

Eickmann, Flessner *et al* postulate that an insolvency practitioner (whose position is similar to that of a business rescue practitioner) must not only have experience in his

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[305] Papaya (note 283 above) 30.
[306] Regulation 126.
[307] Regulation 126, large companies being any company whose most recent public interest score as calculated in terms of regulation 26(2) is 500 or more.
[308] Hefer (note 75 above) 428.
[309] *Ibid*.
[310] Medium Companies being a company whose most recent public interest score as calculated in terms of regulation 26(2) is at least 100 but less than 500.
[311] Hefer (note 75 above) 428.
[312] *Ibid*.

field of academic study but must have the experience and expertise in respect of the complexities and challenges of the company to be rescued.[313] Braun adds that such practitioner must be required to have experience in the business of the corporation he seeks to rehabilitate.[314] Braun further argues that the experience will assist the practitioner to supervise the company and also detect any criminal activities that might have been committed by the company's management.[315]

3.1.4 Removal or replacement of a business rescue practitioner

In terms of section 139 only the court is authorized to remove a business rescue practitioner from office either upon application by an affected person or on its own volition. Compared with the UK Insolvency Act, if an administrator was nominated by an affected person or appointed by the board of directors, the same has the right to remove such practitioner if he fails to satisfactorily discharge his duties.[316] The UK provision seemingly reduces costs and unnecessary delay, and ensures that the courts are less involved in the rescue proceedings.

Chapter 6 makes provision for a wide range of grounds in terms of which a business rescue practitioner can be removed from office. Section 139(2) provides that the court may remove a practitioner based on the following grounds:

> (a) Incompetence or failure to perform duties;
> (b) failure to exercise the proper degree of care in the performance of the practitioner's functions;
> (c) engaging in illegal acts or conduct;
> (d) if the practitioner no longer satisfies the requirements set out in section 138(1);
> (e) conflict of interest or lack of independence; or
> (f) the practitioner is incapacitated and unable to perform the functions of that office, and is unlikely to regain that capacity within a reasonable time.

If a person has been licensed by the Commission and thereafter becomes disqualified from appointment as a practitioner, the Commission must by notice in writing revoke the license of such a person.[317] Furthermore, if the Commission has reasonable basis to believe that a person is no longer qualified to be licensed or has contravened the conditions of the license, the Commission may suspend or revoke that person's license.[318] Delport points out that no provision has been made for a copy of the court order to be referred to the Commission in order for the Commission

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[313] D Eickmann, A Flessner, I Friedrich, K Hans-Peter, K Gerhart, L Hans-Georg, M Wolfgang and S Guido *Heidelberger Kommentar.zur Insolvenzordnung* 4ed (2006) 349.
[314] Braun (note 257 above) 159 para 483.
[315] *Ibid*.
[316] Paragraphs 93 and 94 of Schedule B1 to the Insolvency Act 1986.
[317] Regulation 126(7)(a).
[318] Regulation 126(7)(b).

to consider suspending or revoking the license of the relevant business rescue practitioner.[319] There is also no provision compelling a professional body, accredited in terms of the provisions of section 138(1)(a), to inform the Commission should one of the members no longer be a member in "good standing" of that body.[320] Finch states that to guarantee that the same standards and values are maintained, insolvency administrators have been required to write a competence examination prepared by Joint Insolvency Examination Board.[321] This English approach is recommended to South Africa. The grounds of disqualification as contained in section 139(2) of the Act are now discussed in detail.

3.1.4.1 Incompetence or failure to perform duties

Davis notes that although incompetence constitutes ground for removal of a business rescue practitioner, the ability or competence of a person to act as a business rescue practitioner for that particular company is not stipulated as a requirement for appointment.[322] However, Meskin observes that the term "incompetence" is not defined in the Act, hence, courts have to examine each case in the light of its own facts.[323] For instance in *African Banking Corporation of Botswana Ltd v Kariba Furniture* Manufacturers[324] the court stated that the business rescue practitioner appeared not to appreciate his role and the standard to which he was held in terms of the business rescue provisions. He had ignored and even been hostile to enquiries by the appellant. He actually appeared to act as a representative of the respondent rather than as an independent practitioner.[325] Having found that the practitioner's gross improper conduct had been deliberate, the court ordered the practitioner to pay the appellant's costs jointly and severally with two respondents.[326]

In *Griessel and another v Lizemore and others*,[327] the practitioner upon appointment failed to notify affected persons within the stipulated time, did not address the grievances of the employees, failed to keep the company running while negotiating with potential investors to take over the business or sell the assets thereby improving the dividend that creditors could expect. In less than a week the practitioner decided to close the business. The court held that "in the most material way he, as a

[319] Delport (note 71 above) 488.
[320] *Ibid*.
[321] V Finch 'Insolvency Practitioners: Regulation and Reform' (1998) *Journal of Business law* 336.
[322] Davis (note 1 above) 255.
[323] Meskin (note 290 above) 18-56.
[324] *African Banking Corporation* case (note 141 above) para 38.
[325] *Ibid* para 38 and 56
[326] *Ibid* para 40.
[327] *Griessel* case (note 101 above).

competent practitioner, would know that his inaction and decision to simply shut down the business, less than a week from the date of his appointment, was likely to achieve the very antithesis of what business rescue proceedings would achieve."[328]

It seems from these cases that there is no criterion that can be followed to determine incompetence but what is clear is that the courts evaluate the conduct of the business rescue practitioner in the light of what is expected of him. In other words, the courts can make use of the objective test. The question, what would a reasonable practitioner do in a given scenario will have to be addressed to determine incompetence. Should the court find that a business rescue practitioner is incompetent in terms of this section, this will likely have some effect on the license granted to the business rescue practitioner by the Commission.[329] However, at present there is no provision that specifically states that such person's license should be suspended or revoked by the Commission.

3.1.4.2 Failure to exercise proper degree of care

Chapter 6 does not provide guidance as to what is meant by a business rescue practitioner exercising proper degree of care in the performance of his functions. However, during the course of business rescue the rescue practitioner has responsibilities, duties and liabilities of a director as set in sections 75 to 77.[330] Hence, the court will look at all these factors in order to determine whether or not a business rescue practitioner has exercised the proper degree of care in the performance of his functions. Loubser notes that "sections 75 to 77 represent the legislature's attempts to (partly) codify the common-law fiduciary duties and duty of care and skill of directors, and contain most of the basic principles of these duties."[331]

Section 75 deals with the director's duty not to have personal financial interest in future or existing contracts with the company. The basis of this provision is that there exists a fiduciary relationship between the director and the company hence any situation of a conflict between interests and the duty is to be avoided.[332] In *Guinness plc v Saunders* [333] Lord Templeman held that:

> Like other fiduciaries directors are required not to put themselves in a position where there is a conflict (actual or potential) between their personal interests and their duties to the company. The position of a director *vis-à-vis* the company is that of an agent who may not himself contract with his

[328] *Ibid* para 65.
[329] Delport (note 71 above) 488.
[330] Section 140(3)(b).
[331] Loubser (note 256 above) 114.
[332] Delport (note 71 above) 288.
[333] [1990] 1 All ER 652 at 659.

> principal: the company is entitled to the collective wisdom of its directors, and if any director is interested in a contract, his interest may conflict with his duty, and the law always strives to prevent such a conflict from arising.

However, where personal financial interest exists the director has a duty to disclose it to the board of directors.[334]

Considering the nature and objectives of business rescue it seems that section 75 requires a business rescue practitioner to avoid any personal financial interest in pursuing the rehabilitation of a company under rescue. Where conflict arises the business rescue practitioner must disclose and non-disclosure may be met with the removal of such practitioner from office.

Section 76 stipulates the values that should be observed by directors of a company. In *Sanlam Capital Markets (Pty) Ltd v Mettle Manco (Pty) Ltd and another,*[335] Vally J observed that: section "76(3) emphasizes the fiduciary duties of a director to act in the best interest of the company, to act in good faith, with proper purpose and with the degree of diligence and skill to be expected of a reasonable director in the position of the director concerned." It is important to observe that section 76 does not exclude common law. Therefore, common law duties that are not expressly amended by this section or those that are not in conflict will still apply.[336] The Companies Act as a whole is not a codification of the law relating to the fiduciary relationship between directors and their companies with the result that conduct not forbidden by the Companies Act is now sanctioned. [337] Nonetheless, for business rescue proceedings to be a success there is need for strict adherence to these standards and where a business rescue practitioner fails to comply, such failure is a compelling cause for his or her removal from office.

According to section 77 a director of a company may be held liable for any loss, damages or costs sustained as a direct or indirect consequence of the director having acted; without authority,[338] conducted business in a manner that contravened section 21,[339] acted fraudulently,[340] signed a financial statement that was false[341] or a prospectus that was not true.[342] Liability in terms of section 77 is joint and several,

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[334] Section 75(5).
[335] [2014] 3 All SA 454 (GJ) at 42. see also 76(3)(c).
[336] Delport (note 71 above) 290(5).
[337] See also *Kensal Rise Investment (Pty) limited v Marchant* (1523/213) [2014] ZAKZDHC 47 para 12.
[338] Section 77(3)(a).
[339] Section 77(3)(b).
[340] Section 77(3)(c).
[341] Section 77(3)(d)(i)
[342] Section 77(30(d)(ii).

furthermore it is to the company not to third parties.[343] In view of these provisions where a business rescue practitioner is found to have contravened the above provisions he or she may be relieved of his duties and another business rescue practitioner may be appointed.

An instructive case that has persuasive force in South Africa is *Kyrris v Oldham and other* [344] in which it was held that, absent some special relationship, an administrator appointed under the Insolvency Act, 1986, owed no general common law duty of care to unsecured creditors in relation to his conduct during the administration of the company. The court further held that "given the nature and scope of the administrator's powers and duties, there is no basis for deciding that an administrator owes a duty of care to creditors in circumstances where a director would not owe such a duty to shareholders. In each case, the relevant duties are, absent special circumstances, owed exclusively to the company."[345] The administrator will however be liable to compensate the company if he or she acts in breach of a fiduciary duty owed to the company. Cassim notes that under English law, this general principle may possibly have been modified as a general provision that requires the administrator to perform his or her functions in the interests of the creditors as a whole.[346] The South African Companies Act does not contain a similar provision, with the result that the ratio of *Kyrris v Oldham and others* may well apply in South Africa. In *Re Charnely Davis Ltd (no2)*[347] it was held that an administrator owes a duty to the company to take reasonable steps to obtain a proper price for its assets.

3.1.4.3 Illegal act or conduct

Section 139 (2) (c) provides that where a business rescue practitioner engages in illegal acts or conduct he or she may be removed from office. This provision is vague. On one hand, the provision does not clarify whether the conduct to be considered would have been committed in the discharge of his duties or in his personal life. The effect of this ambiguity is that any conduct such as over speeding in a public highway may be a ground for removal. On the other hand, the provision does not require that the business rescue practitioner be found guilty by the court. This is inconsistent with section 35(3)(h) of the Constitution which stipulates that an accused person must be presumed innocent until proven guilty. Currie and De Waal note that this means that the prosecution must prove its case against the accused and during criminal

[343] *Sanlam Capital Markets case* (note 335 above) para 41.
[344] [2004] 1 BCLC 305 (CA) 329.
[345] *Ibid* at 331d.
[346] Para 3(2). Schedule B1 of the Insolvency Act, 1986.
[347] [1990] BCLC 760 (Ch D).

investigation a subject must be treated as innocent at all stages of the criminal process irrespective of the probable outcome of the trial.[348] This means that the courts are the only institutions that have the right to find a person suspected of a crime guilty and before such process has taken place the person in question should be presumed innocent. The wording in section 139(2)(c) need to be restructured so that the provision does not infringe a business rescue practitioner's constitutional right to a fair trial.

Nevertheless, it is submitted that any breach of statutory or common law fiduciary duties, may amount to fraud. For instance, in *S v Gardener*[349] two directors had failed to disclose certain financial interests to the board of directors and had secured substantial amounts of profit as a result of the transactions by the company. The directors were, charged with and convicted of fraud. Heher JA held that:

> The authorities support the view that an intention to cause actual or potential prejudice is a necessary element of the crime of fraud. However, in considering the intention to cause prejudice, it seems unnecessary to be more specific as to the nature of that prejudice. When company directors deliberately withhold information material to the affairs of their company from the board of directors, there is, in the absence of an explanation for such conduct which may reasonably be true, an a priori case of fraudulent non-disclosure. That is so because they know that the company can only make decisions through a board properly informed and that by withholding proper information they render it both blind and mute. Thus, in such circumstances, both prejudice and the intention to prejudice are proved beyond doubt.

In other words, a director has a duty to disclose personal financial interest before contracting on behalf of the company and failure to do so may attract criminal charges such as fraud. Hence, business rescue practitioners who fail to disclose personal interests to the board of directors may be charged with fraud and upon conviction, could be removed as such under section 139(2)(c).

3.1.4.4 Practitioner no longer satisfies the requirements in section 138(1)

If a business rescue practitioner no longer satisfies all the requirements stated in section 138(1) which lays down the basic condition for qualification to assume such position this will provide grounds for removal of the practitioner by the court in terms of section 139. It follows that there is no longer any basis for issuing of the license. Thus, the license could be suspended or revoked.

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[348] I Currie and J De Waal *The Bill of Rights Handbook* 6th ed (2013)754, See also *S v Zuma and others* 1995 (2) SA 642 (CC).
[349] 2011 (4) SA 79 (SCA) at 87 and 97.

3.1.4.5 Lack of independence or conflict of interest

The Act does not provide guidance as to how this ground should be interpreted, however, a business rescue practitioner is expected to perform his duties objectively and impartially.[350] In *African Banking Corporation Ltd v Kariba Furniture Manufacturers,*[351] the court held that

> The practitioner was expected to act objectively and impartially in the conduct of the business rescue proceedings. So too when it came to the institution of legal proceedings, was an objective and impartial attitude to be expected. This was lacking in the extreme. Not only did the practitioner file the principal answering affidavit to the appellant's application in the court a quo, but he actively engaged both in the proceedings in the court below and in this court. He sought to act in his capacity as an attorney to represent not only himself in his capacity as the business practitioner but as Kariba's representative on whose behalf he prepared and signed the heads of argument filed in this court.

In that case, the business rescue practitioner lacked independence. There seems to be no criteria that can be drawn as a footprint to determine whether a business rescue practitioner has acted in conflict with the interests of the company or not, it is up to the courts to determine if a practitioner has transgressed.

3.1.4.6 Business rescue practitioner is incapacitated

A business rescue practitioner may be removed from office if he becomes incapacitated and it is unlikely that he may regain that capacity within a reasonable time.[352] In determining "reasonable time" in this context one must bear in mind the nature of business rescue proceedings; that is, it is a speedy process.[353] With regards to the term "incapacity" the Act does not stipulate what constitutes incapacity. However, the concept incapacity is not foreign to South African jurisprudence. This term is used in labour law under grounds for dismissal of an employee. It is submitted that an interpretation of this term in labour law is relevant to establish the meaning of the same concept as used in Chapter 6 of the Act.

3.1.4.6.1 Incapacity

In labour law incapacity includes incapacity due to poor work performance and ill health.[354] Du Plessis and Fouche state that if an employee is not capable of doing the work because he lacks skills, knowledge or ability and therefore, does not meet the required performance standards, he can be dismissed for poor work performance.[355]

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[350] *African Banking Corporation* case (note 141 above) para 38.
[351] *Ibid*.
[352] Section 139 (2)(f).
[353] *Koen* case (note 110 above) para 10.
[354] J V Du Plessis and M A Fouche *A Practical Guide to Labour Law* 6th ed (2006) 275.
[355] *Ibid*.

If the employee is incapable of doing the work because of poor health or injury he can be dismissed.[356] Incapacity as a result of poor work performance is fairly dealt with in terms of section 139(2)(a) and (b) as incompetence and failure to exercise proper diligence but incapacity as a result of illness or injury is not covered in Chapter 6.

3.1.4.6.2 Incapacity as a result of ill health

A business rescue practitioner like any other human being may be ill or injured. Venter and Levy provide an explanation as to what constitutes incapacity that may result from illness or accident.[357] They point out that if the employee is unable to perform satisfactorily because of the sickness and comes to work but deliver performance that is below acceptable standards, or is unable to come to work, such a condition warrants dismissal.[358] In some instances the employee's attendance may be erratic and unpredictable or is of an unreasonably lengthy duration, this also is a justified ground for dismissal.[359] The explanation offered by Venter and Levy is shallow and cannot be used to set up a framework that can be followed in determining incapacity in the context of a business rescue practitioner. A better understanding is offered in the seminal case of *Lynoch v Cereal Packaging Ltd*[360] which was used by the drafters of the Code of Good Practice and South African courts have acknowledged its relevance.[361] In that case the court held that:

> Every case must depend on its own facts, and provided that the approach is right, the factors which may prove important to an employer in reaching what must inevitably have been difficult decision include perhaps some of the following – the nature of the illness; the likelihood of it recurring or some other illness arising; the length of the various absences and the spaces of good health between them; the need [of] the employer for the work to be done by the particular employee; the impact of the absences on others who work with the employee; the adoption and the carrying out of the policy; the important emphasis on a personal assessment in the ultimate decision and of course, the extent to which the difficulty of the situation and the position of the employer has been made clear to the employee so that the employee realises that the point of no return, the moment of the decision ultimately being made may be approaching. These, we emphasise, are not cases for disciplinary approaches; these are for approaches of understanding.

The reasoning in this judgement has found application in the Code of Good Practise. Item 10 of the Code states that:

> (1) Incapacity on the grounds of ill health or injury may be temporary or permanent. If an employee is temporarily unable to work in these

356 *Ibid*.
357 R Venter and A Levy *Labour Relation* 8th ed (2015) 322.
358 *Ibid*.
359 *Ibid*.
360 [1988] IRLR 510.
361 J Groban *Dismissal* (2010) 331.

> circumstances, the employer should investigate the extent of the incapacity or the injury. If the employee is likely to be absent for a time that is unreasonably long in the circumstances, the employer should investigate all the possible alternatives short of dismissal. When alternatives are considered, relevant factors might include the nature of the job, the period of absence, the seriousness of the illness or injury and the possibility of securing a temporary replacement for the ill or injured employee. In cases of permanent incapacity, the employer should ascertain the possibility of securing alternative employment, or adapting the duties or work circumstances of the employee to accommodate the employee's disability.
>
> (2) In the process of the investigation referred to in subsection (1) the employee should be allowed the opportunity to state a case in response and to be assisted by a trade union representative or fellow employee.
>
> (3) The degree of incapacity is relevant to the fairness of any dismissal. The cause of the incapacity may also be relevant. In the case of certain kinds of incapacity, for example alcoholism or drug abuse, counseling and rehabilitation may be appropriate steps for an employer to consider.
>
> (4) Particular consideration should be given to employees who are injured at work or who are incapacitated by work-related illness. The courts have indicated that the duty on the employer to accommodate the incapacity of the employee is more onerous in these circumstances.

The Code of Good practice offers a proper point of departure in determining incapacity. However, the Code only relates to incapacity as a result of illness or injury it does not cover all forms of incapacity. Nonetheless, considering the role of the business rescue practitioner the application of the Code to business rescue practitioners would require an objective rather than a subjective approach. In *NUM and another v Rustenburg Base Metal Refiners*[362] the court held that it was more appropriate to deal with the matter on the basis of "reasonableness", rather than by applying the contractual principle of impossibility of performance.

3.1.4.6.3 Incompatibility as a form of incapacity

It is submitted that when a business rescue practitioner is unable to relate professionally with the management of the company he or she may be removed on the ground of incompatibility. In *Subrumuny and Amalgamated Beverage Industry*[363] the court dealt with a scenario that is contemplated by the above proposition. In that case, a productions unit manager was dismissed on the grounds that he could not relate professionally with employees who worked under his supervision and also the management. The arbitrator considered the facts surrounding the dismissal and found that the relationship between the employee (production unit manager) and the employer had irretrievably broken down. Thus, the employee was fairly dismissed because there lacked compatibility between the employer and the employee. The

[362] (1993) 14 ILJ 1094 (IC).
[363] (2000) 21 ILJ 2780 (ARB), See also *Jardine v Tongaat Hulett Sugar Ltd* (2002) 23 ILJ 547 (CCMA).

employee appealed against this decision. The court held that although incompatibility is not specifically mentioned as a possible ground of dismissal in the Labour Relations Act, the employee's inability to relate to the employer or colleagues must be treated as a form of incapacity. With regards to the business rescue practitioner section 142 requires the directors to cooperate with the practitioner. This means that the directors must assist the practitioner during the rescue proceeding. However, it is submitted that where the relationship between the business rescue practitioner and the management of the company has irretrievably broken as a result of the business rescue practitioner's fault or unprofessional conduct, the practitioner may be removed.

3.1.5 Powers and duties of a business rescue practitioner

The powers and duties of a business rescue practitioner are provided in the Act. These include the power to develop and implement a rescue plan, take full control of the management of the company, and monitor the affairs of the company with a view to rehabilitating the company.[364] In *Murgatroyd v Van den Heever NO and others*[365] the court held that "the provisions of Chapter VI are not unduly prescriptive or restrictive as far as a practitioner's functions and duties are concerned. His functions and duties are broad and require a variety of steps to be taken. The nature of a practitioner's powers implies that he may in appropriate circumstances appoint advisors, valuators, auctioneers, forensic accountants, lawyers and other experts or persons to assist him in the carrying out of his plenary functions." In terms of the UK administration provisions, "the administrator of a company may do anything necessary or expedient for the management of the affairs of the company"[366] The same should apply to the business rescue practitioner appointed in terms of the Companies Act in the exercise of his powers to administer the affairs of the company.

3.1.5.1 Managerial powers

The business rescue practitioner takes over the full management of the company from the board and other managers.[367] However, the business rescue practitioner has the power to delegate any of his powers and function to a person who was part of the board or the pre-existing management of the company. In the *Murgatroyd case*[368] the court held that:

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[364] Davis (note 1 above) 256.
[365] [2014] 4 All SA 89 (GJ) para 17.
[366] Insolvency Act of 1986, 1A 1986 Schedule B1 para 59 (1).
[367] Delport (note 71 above) 490.
[368] *Murgatroyd* case (note 365 above) para 16.

> After his appointment, a practitioner has the powers and functions set out in s 140 "in addition to any other powers and duties set out in this Chapter'. They include '(a) full management control of the company in substitution for its board and pre-existing management'. Because of the provisions of sub sec 140(1)(a) there might be some doubt whether the 'pre-existing' management retains any powers and what the powers of the practitioner in this respect are. The practitioner has 'full management control', but what about the old management? The practitioner may remove them and appoint new managers (sub sec 140(1)(c)), but in accordance with the maxim *delegatus non potest delegare* he may not delegate his powers unless authorised to do so, either expressly or by necessary implication.

Considering that the directors and the preexisting management will be well acquainted with the operational side of the company, this will be a useful tool for the business rescue practitioner to utilize while exercising his supervisory function as business rescue practitioner.[369]

Although, the business rescue practitioner may delegate any of his powers and functions to a director or a person who was part of the pre-existing management of the company, it should be born in mind that the exercise of any such powers and functions will always be subject to the authority and express instruction or direction of the business rescue practitioner. Braatvedt argues that "the problem with this is that the practitioner must not delegate what is, in fact, a financial disaster to the person who caused the disaster."[370]

The business rescue practitioner may remove from office any person who forms part of the pre-existing management of the company.[371] It is submitted that any such removal would have to comply, in relation to that person, with any employment related legislation, such as the Labour Relations Act.[372] Removal from office of a person who forms part of the pre-existing management can only be effected by a business rescue practitioner.[373] In *Clarke/EH Walton Packing*[374] the court held that this power is due to the fact that full management control of the company is in the hands of the business rescue practitioner, and not by virtue of section 140(1)(c)(i) as this merely states that the business rescue practitioner may effect such removal.

In terms of section 140(1)(c)(ii) a business rescue practitioner has the authority to appoint a person as part of the management of the company. Such a person may fill in a vacancy or may be appointed as an advisor to the company or business rescue

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[369] Delport (note 71 above) 491.
[370] K Braatvedt 'Costs of business rescue' (2014) Volume 14 Issue 9 *Without Prejudice* 23.
[371] Delport (note 71 above) 491
[372] *Ibid*.
[373] *Ibid*.
[374] [2014] JOL 31234 (CCMA) para 101.

practitioner.[375] In *Murgatroyd's* case it was held that "although no specific provision is made for the power of a practitioner to appoint advisors, section 140(2) prohibits a practitioner from appointing certain persons as advisors. A practitioner, therefore, by necessary implication has the power to appoint advisors."[376]

3.1.5.2 Investigate the affairs of the company

The business rescue practitioner must investigate the affairs of the company. Section 141(1) stipulates that:

> As soon as practicable after being appointed, a practitioner must investigate the company's affairs, business, property, and financial situation, and after having done so, consider whether there is any reasonable prospect of the company being rescued.
> (2) If, at any time during business rescue proceedings, the practitioner concludes that—
> (a) there is no reasonable prospect for the company to be rescued, the practitioner must—
> (i) so inform the court, the company, and all affected persons in the prescribed manner; and
> (ii) apply to the court for an order discontinuing the business rescue proceedings and placing the company into liquidation;

The main purpose of this section is to ensure that the business rescue practitioner undertakes proper investigation into the affairs of the company in order to ensure that the company is in fact in financial distress and if it is in financial distress that there is a reasonable prospect of rescuing the company. Delport argues that although the court's decision in *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investment 386 Ltd*[377] has been questioned in regard to the meaning of the term "reasonable prospect" as used in sections 129 and 131, it is submitted that the court's interpretation as to what is meant by "reasonable prospect" would be useful in cases where the business rescue practitioner is expected to express an opinion as to whether there is a reasonable prospect of rescuing the company, as is the case in this section. In that case, the court compared the meaning of the term "reasonable prospect" as used in section 131(4) and the phrase "reasonable probability" used in section 427 of the Companies Act 1973. Eloff AJ observed that:

> The meaning of the term *"reasonable prospect"* as used in this subsection falls to be considered. In terms of section 427(1) of the previous Companies Act, no 61 of 1973, a rather cumbersome and ineffective procedure was provided for reviving ailing companies. That section of the 1973 Companies Act used the phrase *"reasonable probability"* in respect of the recovery requirement. In contrast, section 131(4) of the new Act uses the phrase *"reasonable prospect"* in respect of the recovery requirement. The use of

[375] Delport (note 71 above) 492.
[376] *Murgatroyd* case (note 365 above) para 17.
[377] *Southern Palace Investment* case (note 61 above).

> different language in this latter provision indicates that something less is required than that the recovery should be a reasonable probability.[378]

Thus, the meaning of "reasonable prospect" in the context of section 141 may mean that there must be a reasonable probability that the company may be rehabilitated considering the factual financial status of the company.

At this stage Cassim comments that the financial position of the company must be monitored on a regular basis.[379] Thus, if at any time during the business recue proceedings the business rescue practitioner concludes that there is no reasonable prospect of rescuing the company, he must inform the court, the company, and all affected persons. Thereafter apply for an order to discontinue business rescue proceedings and place the company in liquidation.[380] Davis argues that "section 81(1)(b) specifically provides for a winding-up order to be issued on the application of the business rescue practitioner in this situation although the court only has the power to order the winding up of a solvent company in terms of section 81 and the company at this stage would have been insolvent."[381] In essence the power of the practitioner to seek judicial winding up under section 81(1)(b) could be read as an exception to the general power of the court to wind up a solvent company as provided in section 81(1).

In *Commissioner for the South African Revenue Services v Beginsel and Rennie NNO,*[382] the business rescue practitioners came to the conclusion that there was no longer any reasonable prospect for rescuing the company. Instead of informing the court and all affected persons of this fact and applying for an order discontinuing the business rescue proceedings, the business rescue practitioners proposed a plan in terms of which the assets of the company would be sold and in so doing demonstrated that a better return to creditors as a whole would be obtained than would be if the company was placed under liquidation. In terms of the proposed business rescue plan the claim by South African Revenue Service was treated as unsecured and would consequently receive a concurrent dividend in terms of the plan. The plan was approved and adopted by the majority of the creditors. However, if the company was placed under liquidation proceedings, the SARS claim would be treated as preferent under section 99 of the Insolvency Act and would probably be paid in full. As a result, SARS argued that the business rescue practitioners were obliged in terms of section 141 to apply for an order placing the company in

[378] *Ibid* paras 20 and 21.
[379] Cassim (note 57 above) 151.
[380] Section 141(2)(a)(ii).
[381] Davis (note 1 above) 256.
[382] 2013 (1) SA 307 (WCC) para 57.

liquidation when they realised that the company could not be rehabilitated. Fourie J came to the conclusion that the secondary objective of business rescue, namely, to ensure that a better return for creditors would be achieved than would be if the company was liquidated, would be achieved in this case. Consequently, the court ordered that the business rescue practitioners did not have to apply for the liquidation of the company in terms of section 141(2)(a).

In terms of section 141(2)(c) if at any time during business rescue proceedings the business rescue practitioner arrives at the conclusion that there is evidence in the dealings of the company of voidable transactions or failure by the directors to perform material obligations relating to the company, the business rescue practitioner must take the necessary steps to rectify the matter and may direct the management to do so. The business rescue practitioner is also required to forward to appropriate authorities any evidence of reckless trading, fraud or other contravention of the law and the management may be directed to rectify the matter and recover any misappropriated assets of the company.[383]

The Act does not provide for the meaning of "voidable transaction" and the effect of this anomaly is reflected in *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd.*[384] In that case, the court held that on the current construction of section 141(2)(c) (i) it is doubtful whether the business rescue practitioner will be able to set aside any transaction in the event that one is identified. However, Meskin submits that the provisions of the Insolvency Act 1936 should be applied by business rescue practitioners in determining whether or not there have been any transactions that may be treated as voidable for the purposes of this section.[385]

In *Burmeister v Spitskop Village Properties Ltd,*[386] the court stated that the existence of transactions of dubious validity and other sinister aspects in the management of the company's affairs made the case suitable for liquidation rather than business rescue; since there were no comparable provisions for setting aside transactions or examining directors under the business rescue provisions, liquidation was more appropriate.[387] Since section 141(2)(i) does not contain any sanction for non-compliance, and since transactions entered into by the company with third parties are valid until set aside by the court in terms of the provisions of the Insolvency Act, it is

[383] Section 141(2)(c)(ii).
[384] *Oakdene Square* case (note 109 above) para 49, item 11.
[385] Meskin (note 290 above) 18-92.
[386] Unreported (76408/2013) [2015] GP (16 September 2015).
[387] *Ibid* para 41.

difficult to see how the business rescue practitioner, or for the matter the management of the company, can take steps to rectify the matter without supporting or enabling legislation.[388]

Section 141(2)(b) provides that if at any time during the business rescue proceedings the business rescue practitioner concludes that there are no longer reasonable grounds to believe that the company is in financial distress, the business rescue practitioner must inform the court, the company and all affected persons. If the business rescue proceeding was confirmed by a court order or was initiated by means of an application to the court, the business rescue practitioner must apply to court for an order terminating the business rescue proceedings. Termination may also be carried out in terms of section 141(2)(b)(ii) which provides that the business rescue practitioner may file a notice of termination of business rescue proceedings. This provision is appropriate where the business rescue proceedings were initiated by a resolution of the board of directors.

3.1.6 Remuneration of the business rescue practitioner

The business rescue practitioner is allowed to charge an amount to the company for his remunerations and expenses but it must be in accordance with the tariff provided in section 143(6). This section provides that from time to time the Minister may make regulations stipulating a tariff of fees and expenses. The Minister has made such regulations, basing the tariff for remuneration on the size of the company in which the business rescue practitioner has been appointed.[389] The term “remuneration” in this context means the amount of money a business rescue practitioner is entitled to be paid in accordance with the prescribed tariff in regulation 128(1). Whereas, the term “expenses” refers to the actual cost of any disbursement or expense incurred by the business rescue practitioner to the extent reasonably necessary to carry out his functions and to facilitate the conduct of the company’s business rescue proceedings.[390]

Regulation 128(1) only provides the amounts to be paid but does not specify the services or expenses to be covered. However, in *Murgatroyd v Van den Heever NO and others,*[391] the court held that the test to be applied in determining whether the business rescue practitioner has a valid claim for expenses and disbursements is an objective test. In other words, the court must ascertain whether the expenses were

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[388] *Ibid*.
[389] Regulations 128 (1) (a)-(c), Companies Regulation 2011.
[390] Regulation 128(3).
[391] *Murgatroyd* case (note 365 above) para 21.

reasonably necessary for the furthering of business rescue proceedings or not. “The question is a factual one that must be assessed in the light of circumstances of each case with reference to the size of the company, the functionality of its management, the accuracy and currency of its financial and accounting data. Furthermore, the complexities involved and the scope of the work required to be undertaken by the business rescue practitioner. Nonetheless, the business rescue practitioner cannot claim for services in connection with the preparation of a business rescue plan after it had been concluded that there was no reasonable prospect for the company to be rescued and also not for services provided after the business rescue proceedings had ended.”[392]

3.1.6.1 Contingency fee agreement

Section 143(2) makes provision for a contingency fee to be paid to the business rescue practitioner. However, this fee is subject to certain requirements being met. Meskin describes this fee as an “added incentive for business rescue practitioners to facilitate the adoption of a workable business rescue plan that can rescue a financially distressed company.”[393] With this objective in mind, a business rescue practitioner may propose an agreement with the company under business rescue for further remuneration which is calculated on the basis of contingency[394] related to the adoption of a business rescue plan, or within such a particular time, or the inclusion of any particular matter within such a plan[395] or the attainment of any particular result or combination of results relating to business rescue proceedings.[396]

A contingency fee agreement will only be binding if it is presented to and approved by, the holders of majority voting interests and the holders of a majority of the voting rights attached to shares of the company.[397] These persons must be present at the meeting called for the sole purpose of considering the proposed agreement.[398] In *ABSA Bank Ltd v Golden Dividend 339 Pty Ltd and other*[399] the court held that the agreement relating to the remuneration of the business rescue practitioner was not valid because the meeting had not been conducted in terms of section 143(3). This provision requires an agreement for further remuneration to be approved "at a meeting called for the purpose of considering the proposed agreement.” The court

[392] *Ibid* para 22.
[393] Meskin (note 290 above) 18-94.
[394] Section 143(2).
[395] Section 143(2)(a)
[396] Section 143(2)(b).
[397] Section 143(3)(a).
[398] Section 143(3)(b).
[399] 2015 (5) SA 272 (GP) para 60-70.

held that "having regard to the notice and agenda for the meeting of 22 November 2013, it is evident that the meeting was not called for this purpose."[400]

It is important to note that any creditor or shareholder who voted against a proposal for the payment of a contingency fee to the business rescue practitioner may apply to court within ten working days after the date upon which voting on that proposal took place for an order setting aside the agreement[401] on the grounds that it is not just and equitable[402] or that the remuneration provided is unreasonable having regard to the financial circumstances of the company.[403]

3.1.6.2 Taxation of business rescue practitioner's remuneration

The Act does not provide for business rescue practitioner's remuneration or expenses to be taxed.[404] Meskin maintains that considering the rather liberal hourly and maximum daily tariff the practitioner is entitled to, it is prudent therefore to appoint an independent party in order to avoid abuse by practitioners who may be tempted to charge exorbitant fees. This proposition is confirmed in *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) Pty Ltd*[405] where the court held that:

> There is no provision for the taxation of the fees, costs and expenses of a business rescue practitioner, whereas a liquidator's costs are subject to taxation. There is, therefore, independent control over the costs of liquidation whereas there is currently none in the case of a business rescue procedure. This aspect may be for the Legislature to consider when further amendments to the Act are proposed.

This situation is aggravated by the fact that the tariff set out in regulation 128(1) does not apply to or limit in any way, the additional (contingency) remuneration that a business rescue practitioner may be entitled to in terms of section 143.[406] It is submitted that the remuneration paid by the company to the business rescue practitioner constitutes legitimate income and should be taxed.

3.1.6.3 Ranking of the business rescue practitioner's remuneration and expenses

Section 141(5) stipulates that a practitioner's claim for remuneration and expenses will rank before all secured and unsecured creditors to the extent that it is not fully paid. Meskin argues that the purpose of this provision is not clear. It seems

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[400] *Ibid* para 69.
[401] Section 143(4).
[402] Section 143(4)(a).
[403] Section 143(4)(b).
[404] Meskin (note 290 above) 18-93.
[405] *Oakdene Square Properties* case (note 109 above) para 49 item 10.
[406] Regulation 128(2).

unrealistic and impractical to expect a successful business rescue plan to be implemented in circumstances where there are insufficient funds to pay business rescue practitioner's fees.[407] If this becomes the case the amount of the practitioner's remuneration and expenses that remain unpaid will be paid in preference to all the secured and unsecured claims against the company. In *Industrial Development Corporation of SA Limited and another v Schroeder NO,*[408] Nhangulela ADJP reiterated that "section 143 provides for the remuneration of the business rescue practitioner, not the Liquidators. Section 136 (4) provides that the liquidator is the creditor of the company but without giving preference to such a creditor above others. It would seem that the liquidators' claim against the company is protected only under the liquidation proceedings, and they are the concurrent creditors under business rescue." Thus, the payment of liquidators does not enjoy the preference guaranteed in section 143 for the remuneration and expenses of business rescue practitioners.

Nevertheless, the outstanding remuneration and expenses of the business rescue practitioner, rank after the costs as set out in section 97 of the Insolvency Act. An elaborate interpretation of this provision is found in *Diener NO v Minister of Justice.*[409] In that case, JD Bester Labour Brokers CC (the close corporation) was financially distressed hence it appointed Mr Diener as the business rescue practitioner. Shortly after his appointment the business rescue practitioner applied to court for an order commencing business liquidation. The Master of High Court (Master) appointed Mr Murray as one of the liquidators. It follows that the liquidator prepared the liquidation and contribution account and submitted it to the Master. The account excluded the business rescue practitioner's costs for services rendered.

The business rescue practitioner sort to set aside the account. He contended that charges for his services must be included in the account because section 135(4) guaranteed their payment. The practitioner further argued that the charges represented "a claim of a super preferent nature." This meant that he was to be preferred over any secured creditor's claim against an encumbered asset.

The liquidator argued that the business rescue practitioner's remuneration is not within the scope of "administration costs" in terms of section 97 of the Insolvency Act.[410] Hence, such costs cannot be afforded preferential status. The liquidator further submitted that if a business rescue practitioner wishes to claim his

[407] Meskin (note 290 above) 19-95.
[408] Unreported case (1958/25) [2015] ZAECMHC (17 September 2015) para 42.
[409] Unreported case 30123/2015 (GP) paras 29, 50 and 60.
[410] 21 of 1932

remuneration for services rendered he must forward a claim which must be accompanied by supporting documents. Otherwise, to pay the practitioner after a mere demand would mean that a creditor is getting paid in respect of an unproven claim. Such an outcome would be inconsistent with the objectives of the Insolvency Act.

The court held that although section 143(5) and section 135(4) affords the business rescue practitioner's remuneration preferential status these provisions do not dictate that such costs should also be construed as administration costs of an insolvent estate. Therefore, for the business rescue practitioner to receive payment from the insolvent estate, he must submit and prove a claim like any other creditor.

3.2 The business rescue plan

The main function or duty of the business rescue practitioner is to draft a business rescue plan and oversee its implementation.[411] Some commentators are of the view that "this is the unique task of the business rescue practitioners".[412] On the other hand, the business rescue plan is the nub around which the rescue of a company will revolve hence a rescue plan. However, before the rescue plan is drafted, certain preliminary procedure must be followed to ensure that the plan is acceptable to the stakeholders.

3.2.1 Consultation with stakeholders

The business rescue practitioner's first step is to consult with the stakeholders before drafting a business rescue plan. Section 150(1) precisely provides that "the practitioner, after consulting the creditors, other affected persons, and the management of the company, must prepare a business rescue plan for consideration and possible adoption at a meeting held in terms of section 151."

In this context, consultation means that there must be sufficient information available for the affected party (for example a creditor) and that they must actually be consulted.[413] In *Scalabrini Centre, Cape Town and other v Minister of Home Affairs and others,* [414] the court held that: "at a substantive level, consultation entails a genuine invitation to give advice and a genuine receipt of that advice." In *R v Secretary of State for Social Services*, [415] Webster J held that:

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[411] M Pretorius 'A competency framework for the business rescue practitioner profession: Original research' (2014) Volume 14 Issue 4 *Acta Commercii* 9.
[412] *Ibid*.
[413] Delport (note 71 above) 518.
[414] [2013] 2 All SA 589 (WCC) para 72.
[415] [1986] 1 All ER 164 (QB) at 167G-H.

> In my view, it must go without saying that to achieve consultation sufficient information must be supplied by the consulting to the consulted party to enable it to tender helpful advice. Sufficient time must be given by the consulting party to the consulted party to enable it to do that, and sufficient time must be available for the advice to be considered by the consulting party. Sufficient, in that context, does not mean ample, but at least enough to enable the relevant purpose to be fulfilled.

In respect of procedural compliance, consultation may be prescribed by legislation, this means that consultation must be carried out in accordance with the procedures stipulated for its validation.[416] However, the procedure must be the one which enables consultation in the substantive sense to occur.[417]

3.2.2 The proposed business rescue plan

The proposed business rescue plan must include all the necessary information that may assist an affected person to vote for or against the plan.[418] This means that sufficient information must be provided to enable an interested person to make an informed decision to vote to accept or reject the plan. In *Commissioner of South African Revenue Services v Beginsel and Rennie NNO,*[419] Fourie J held that:

> A perusal of section 150 (2) of the Act shows that the legislature has prescribed the content of a proposed business rescue plan in general terms. The content can, by its very nature, not be exactly and precisely circumscribed, as it would differ from case to case, depending on the peculiar circumstances in which the distressed company finds itself. It follows, in my view, that, upon a proper construction of section 150 (2), substantial compliance with the requirements of the section will suffice. This would, in my view, mean that, where sufficient information, along the lines envisaged by section 150 (2), has been provided to enable interested parties to take an informed decision in considering whether a proposed business rescue plan should be adopted or rejected, there would have been substantial compliance.

This finding suggests that substantial compliance with section 150(2) will suffice because not all details required in section 150(2) will apply in every case.[420] Braatvedt suggests that the business rescue practitioner should also include the difficulties he or she has encountered during the investigation of the affairs of the company in terms of section 141.[421] For example, if the practitioner discovers that essential data, figures and information of any nature is missing, he must share this

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[416] *Hlumisa Investment Holdings (RF) and another v Van der Merwe NO and others* (77351/2015) [2015] ZAGPPHC 1055 (14 October 2015) para 22, see also *Hayes & another v Minister of Housing, Planning and Administration, Western Cape & others* 1999 (4) SA 1229 (WC) at 1242 C-F.
[417] *Ibid*.
[418] Section 150(2).
[419] *Beginsel and Rennie NNO* case (note 382 above) para 38.
[420] Davis (note 1 above) 258.
[421] Braatvedt (note 370 above) 23.

information with the creditors.[422] This approach will help the practitioner make assumptions based on actual information on the ground. Braatvedt further notes that disclosure of the situation will assist in the correction and restructuring of the plan when presented to stakeholders.[423]

3.2.2.1 Background information

The business rescue plan must be divided into three parts namely, the background, proposal and assumptions and conditions. Rushworth states that in each case, the list of requirements is the minimum as to what is required for the contents of the relevant part of the plan.[424] The background information includes a list of the company's assets and the list should identify which assets are held as security by creditors.[425] This section must also include a list of creditors of the company and should state the status of their claim whether they are secured or concurrent or statutorily preferent. In addition, the list should state if the creditors of these claims have furnished proof of their claims.[426] The business rescue practitioner should disclose the probable dividend that may be paid to creditors, in accordance with their ranking, if the company were to be placed in liquidation.[427]

In *Commissioner for the South African Revenue Service v Beginsel and Rennie NNO*[428] it was held that the probable dividend must be stated at the date of the commencement of the business rescue proceedings not at the date of the business rescue plan. Furthermore, in terms of section150(2)(a)(iv) the plan must provide a complete list of the holders of the company's issued securities, as well as a copy of the written agreement concerning the practitioner's remuneration[429] and a statement whether the business rescue plan includes a proposal made informally by a creditor of the company.[430]

3.2.2.2 The rescue plan

In respect of the actual plan, this part "must include information concerning the nature and duration of any moratorium for which the plan makes provision,[431] the

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[422] *Ibid*
[423] *Ibid* 24.
[424] J Rushworth 'A critical analysis of the business rescue regime in the Companies Act 71 of 2008' ed T Mongalo in *Modern Company law for a Competitive South African Economy* (2010) 402.
[425] Section 150(2)(a)(i).
[426] Section 150(2)(a)(ii).
[427] Section 150(2)(a)(iii)
[428] *Beginsel and Rennie NNO* case (note 382 above) paras 46-49.
[429] Section 150(2)(a)(v)
[430] Section 150(2)(a)(vi)
[431] Section 150(2)(b)(i).

extent to which the company is to be released from payment of its debts and the extent to which any debt is proposed to be converted into equity in the company or another company."[432] In *Tyre Corporation Cape Town Pty Ltd v GT Logistics Pty Ltd and others*[433] it was contended that a business rescue plan may not incorporate a compromise for creditors, the averments being that this could only be done in terms of section 155 of the Act. The court rejected this argument, referring to section 150(2)(b)(ii) and section 154 as authority for the fact that elements of a compromise could be incorporated into a business rescue plan. Under administration, an administrator may actually propose a composition or arrangement but the creditors' meeting cannot impose a composition or arrangement; it can only approve the administrator's proposal and in such case further steps must be taken.[434]

With regards to existing agreements and the status of the company, section 150(2)(b)(iii) provides that such information must be included in the plan, which should also include the property of the company that is available to pay creditors' claims under the plan.[435] The plan must include the order of preference in which the proceeds of property will be applied to pay creditors where the plan has been adopted; [436] the benefits of the plan, as opposed to the benefits which would be received by creditors if the company were to be placed in liquidation;[437] and the effect that the plan will have on the holders of each class of the company's issued securities.[438]

3.2.2.3 Assumptions and conditions

In respect of assumptions and conditions, the information must include a statement of the conditions that must be satisfied for the plan to come into operation and be fully implemented;[439] the effect that the proposed plan has on employees and their terms and conditions of employment;[440] the circumstances under which the plan will end[441] and a projected balance sheet of the company. This must also include a projected statement of income and expenses for the following three years.[442] The projected balance sheet and statement of income and expenses must include a

[432] Section 150(2)(b)(ii).
[433] [2016] ZAWCHC 124 (21 September 2016).
[434] *Re St Winding Ltd* (1987) 3 BCC 643.
[435] Section 150(2)(b)(iv).
[436] Section 150(2)(b)(v).
[437] Section 150(2)(b)(vi).
[438] Section 150(2)(b)(vii).
[439] Section 150(2)(c)(i).
[440] Section 150(2)(c)(ii).
[441] Section 150(2)(c)(iii).
[442] Section 150(2)(c)(iv).

notice of any material assumptions on which the projections are based[443] and may include alternative projections based on varying assumptions and contingencies.[444]

The proposed plan must conclude with a certificate by the practitioner stating that the information contained in the plan appears to be accurate, complete and updated,[445] furthermore that the projections provided are estimates made in good faith on the basis of factual information and assumptions as set out in the statement.[446]

3.2.3 Publication of the business rescue plan

In terms of section 150(5) the business rescue practitioner should publish the proposed plan within 25 working days. If the business rescue practitioner needs more time he may apply to court for extension or may seek the approval of the holders of a majority of the creditors' voting interests.[447] In *DH Brothers Industries Pty Ltd v Gribnitz NO and others*,[448] Gorven J observed that:

> Each step of business rescue proceedings is geared to promote certainty as to the status of the proceedings.[449] It is my view, on a conspectus of the structure of business rescue proceedings, that a meeting must be convened and a vote taken in order for it to be said that a majority of creditors 'allowed' an extension of time.[450]

On the contrary, there is authority for the submission that section 150(5) does not require that a meeting be held to determine whether creditors approve or deny extension.[451] Rather all that is required is an extension approved by the holders of a majority of the creditors' voting interests. Therefore, if the purported meeting is invalid due to insufficient notice, the extension purported by a majority of the creditors' voting interests would remain a valid extension.[452] Although the decision in the *ABSA Bank Ltd* case was later overturned, the reasoning of the court remains persuasive considering the fact that in that case there was a single creditor with a majority voting interest.[453]

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[443] Section 150(3)(a).
[444] Section 150(3)(b).
[445] Section 150(4)(a).
[446] Section 150(4)(b).
[447] Section 150(5) (a) and (b).
[448] *DH Brothers* case (note 22 above) para 30.
[449] *Ibid.*
[450] *Ibid* para 32.
[451] *ABSA Bank Ltd* case (note 173 above) para 38-41.
[452] *Ibid*.
[453] *ABSA Bank Ltd* case (note 173 above), see also *Golden Dividend 339 (Pty) Ltd v ABSA Bank Ltd* [2016] ZASCA 78 (30 May 2016).

The Act does not provide what happens if the business rescue practitioner fails to publish the proposed business rescue plan on time.[454] In *DH Brothers Industries* case[455] Gorven J held that the Act's silence on this matter constitutes "yet another drafting *lacuna.*" However, after deliberating on the infringement of creditors right when a corporation voluntarily places itself in business rescue, the court held that where the proposed rescue plan is not published within the stipulated time three consequences may ensue: the business rescue practitioner could file a notice of termination of proceedings, or an affected person would apply to court on just and equitable ground for an order ending the proceedings, or application could be made for setting aside the initiating resolution in terms of section 130(2)(a).

However, Gorven's J decision was not followed in *Shoprite Checkers (Pty) Ltd v Berry Plum Retailers CC and Others.*[456] In that case, Tuchten J held that section 132(2) provides for the grounds and situations where business rescue proceedings could be terminated. Failure to publish business rescue plan timeously is not included as one of the grounds, thus this omission strongly suggests that the intention was not to automatically end business rescue if the proposed plan was not published timeously. The court further held that in the light of the purpose of the Act an interpretation that would lead to an automatic termination of business rescue would be inconsistent with the aims of chapter 6 of the Act. Tuchten J concludes that:

> Section 7(k) provides that one of the purposes of the new Companies Act is to provide for the efficient rescue and recovery of financially distressed companies, in a manner that balances the rights and interests of all relevant stakeholders. I think that an interpretation which would allow a court, on good cause shown, to extend the 25-day period, even after its expiry, would better promote this purpose. To take an extreme example: if a practitioner were to suffer some personal misfortune and be unable to fulfil or neglect his duties during the critical period, so that the plan was published one day late, the inflexible interpretation could cause a deserving rescue to fail. The flexible interpretation, on the other hand, would promote the balancing of the rights and interests of "relevant stakeholders".[457]

Therefore, a flexible interpretation would allow the court to condone the procedural failure for the greater good of the business rescue scheme. Jordaan is of the view that it appears there is no judicial harmony in respect of the consequences of failure to publish a business rescue plan timeously.[458] "It is hoped that an appeal court can settle these uncertainties sooner rather than later."[459] Nonetheless, at present

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[454] T Jordaan 'Business rescue plan not published timeously' (2015) Volume 2015 Issue 554 *De Rebus* 60.
[455] *DH Brothers Industries (Pt) Ltd* case (note 22 above).
[456] Unreported case no 47327/ ZAGPPHC (09 March 2015) para 23.
[457] *Ibid* para 24.
[458] Jordaan (note 454 above) 60.
[459] *Ibid*.

Tuchten's J interpretation seems acceptable bearing in mind the legislature's intention to include Chapter 6 in the new Companies Act that is to rehabilitate viable enterprises that are facing temporary financial setback.

3.2.4 Meeting to determine the future of the company

Once the proposed business rescue plan has been published, there is another short time frame within which the meeting to determine the future of the company must be convened.[460] (That is within ten days after the publication of the business rescue plan). Notice of the meeting must be delivered at least five days before the meeting.[461] The purpose of the meeting is to consider the business rescue plan proposed by the business rescue practitioner in terms of section 150. In the *African Banking Corporation* case[462] the court stated that it is not permissible for an affected person to seek to set aside the proceedings of the meeting of creditors at which a business rescue plan was adopted.

Section 151(1) refers to "a meeting of creditors and any other holders of a voting interest." This implies that there are voting interests other than those of creditors. In *Shoprite Checkers* case[463] the court held that "voting interests means, as defined in section 128(1)(j), an interest as recognised, appraised and valued in terms of section 145 (4) to (6). Section 145(4) to (6) refers to the interests of creditors. It seems, therefore, that the phrase and other holders of a voting interest in s 151(1) is tautologous and that the meeting contemplated in those sections is a meeting of creditors alone. However, under s 152(1)(c), the practitioner is required to provide an opportunity for employees' representatives to address the meeting."

3.2.5 Consideration of the business rescue plan

Section 152 provides for the consideration of the proposed business rescue plan. Meskin submits that the consideration of the business rescue plan under section 152 constitutes the most critical phase of the business rescue process.[464] At this stage, creditors and possibly the holders of any issued security of the company decide whether or not to adopt the business rescue plan. The process of discussing, voting or amending the plan has the potential of being quite a long and convoluted process. Hence, section 153 permits such meeting to be adjourned from time to time. At a meeting convened in terms of section 151, the practitioner must:

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[460] Section 151(1).
[461] Section 151(2).
[462] *African Banking Corporation* case (note 44 above) para 59.
[463] *Shoprite Checkers* case (note 456 above) para 32.
[464] Meskin (note 290 above) 18-110.

> (a) introduce the proposed business rescue plan for consideration by the creditors, and if applicable, by the shareholders;
> (b) inform the meeting whether the practitioner continues to believe that there is a reasonable prospect of the company being rescued;
> (c) provide an opportunity for the employees' representatives to address the meeting;
> (d) invite discussion, and entertain and conduct a vote, on any motions to—
> (i) amend the proposed plan, in any manner moved and seconded by holders of creditors' voting interests, and satisfactory to the practitioner; or
> (ii) direct the practitioner to adjourn the meeting in order to revise the plan for further consideration; and
> (e) call for a vote for preliminary approval of the proposed plan, as amended if applicable, unless the meeting has first been adjourned in accordance with paragraph (d)(ii).

Considering the nature of the business rescue, that is it is a speedy process, it is submitted that the business rescue practitioner should deal with these items in the order that they are listed to save time and avoid unnecessary delays.

3.2.6 Approval of business rescue plan

After presenting the proposed business rescue plan the business rescue practitioner must call for a vote in terms of section 152(1)(e). The proposed plan will be approved on a preliminary basis if it was supported by the holders of more than 75 percent of the creditors' voting interests that were voted; and if 50 percent of the holders of independent creditors 's voting interests voted for the proposed plan. [465] If the proposed business plan is approved on a preliminary basis and does not alter the rights of the holders of the company's securities, such approval will be regarded as the final approval of that plan subject to fulfilment of any condition on which the plan is contingent.[466] If the proposed plan is not adopted on a preliminary basis the plan is rejected and may be reconsidered in terms of section 153.[467]

However, if the proposed plan is approved on preliminary bases but alters the rights of holders of the company's securities, the business rescue practitioner is required to hold a meeting with such affected persons and call a vote as to the approval or rejection of the plan.[468] If a majority votes for the approval of the proposed plan, this implies that the plan is adopted.[469] But if a majority votes against the approval of the proposed plan, this means that the plan is rejected.[470]

[465] Section 152(2)(a) and (b).
[466] Section 152(3)(b).
[467] Section 152(3)(a).
[468] Section 152(3)(c)(i).
[469] Section 152(3)(c)(ii)(aa).
[470] Section 152(3)(c)(ii)(bb).

In *Tyre Corporation Cape Town (Pty) Ltd and others v GT Logistics (Pty) Ltd*[471] the applicants sought an order placing the respondent company in liquidation. The managing director and sole shareholder of the company applied to place the company under business rescue. The proposed rescue plan had categorized creditors into two categories, namely; critical creditors and non-critical creditors. In this context "critical" referred to the contribution offered by the creditor for the continuation of the business of the company. Rogers J rejected the intervening application for business rescue. The court did not recognise the categories of creditor suggested in the proposed business rescue plan. In dealing with whether or not a business rescue plan could contain elements of a compromise and finding that it could and that the business rescue procedure would be deficient if that was not the case, the court however emphasized what it saw as an anomaly in the process for the approval of a business rescue plan. The court pointed out that:

> There may, however, be a different deficiency in the business rescue provisions of the Act. In the case of a s 155 compromise, creditors vote according to classes. The compromise must be approved by at least 75% in value of each class. In the case of business rescue, by contrast, the only requirement for approval is that the plan is supported by the holders of more than 75% of the creditors' voting interests actually voted and by at least 50% of the independent creditors' voting interests actually voted (s 152(2)). Section 131 does not confer on the court a power to create classes of creditors or to vary the provisions of the Act relating to the approval of plans. Nobody in the present case suggested that I had such a power. The absence of such a provision is anomalous, particularly since a plan which affects the rights of the holders of any class of the company's securities requires class approval (s 152(3)(c)).[472]

The court's problem with the approach in the proposed rescue plan was that the creditors could be treated differentially and even unfairly by categorizing them as "critical" and "non-critical."[473] Rogers J further stated that the court was not concerned with the remedies of minority creditors after the commencement of the rescue proceedings, rather it was concerned with the situation where the court is being asked to grant a business rescue order on the basis of a proposed plan which, from the outset, appears to be unfair. This would at least be relevant to the court exercising its discretion in granting a business rescue order or not.[474]

A business rescue plan that has been adopted in accordance with the Act is binding on the company and all the creditors of the company.[475] In *African Banking*

[471] *Tyre Corporation* case (note 433 above).
[472] *Ibid* para 36.
[473] *Ibid* para 37.
[474] *Ibid*.
[475] *African Banking Corporation* case (note 44 above) para 28.

Corporation of Botswana Ltd v Kariba Furniture Manufacturers (Pty) Ltd[476] the court referred to section 152(4) as a "cramdown" provision under Chapter 6 because it binds, every creditor, holder of the company's securities whether or not a person was present at the meeting, whether a person voted in favour or against the plan. The court further held that Chapter 6 does not provide a remedy to affected persons, more specifically disgruntled creditors, regardless of whether such approval and adoption is preliminary or final.[477] Once the business rescue plan is adopted the business rescue practitioner is required to manage and conduct the affairs of the company in accordance with the plan. No court approval is required for the implementation of a business rescue plan after it has been duly adopted. It is also not permissible for an affected person to seek to set aside the meeting of creditors at which the plan is adopted.[478]

Section 152(5) provides that after the adoption of a business rescue plan the company must take all necessary steps to satisfy any condition upon which the business rescue plan is contingent, under the direction and supervision of the business rescue practitioner. When the business rescue practitioner has fully implemented the business rescue plan, the practitioner must file a notice of the substantial implementation.[479] A business rescue practitioner, who has filed a notice of substantial implementation of the business rescue plan, must meet the notifications requirements stated in regulation 125(6). Regulation 125(6) provides that the practitioner must conspicuously display a copy of the notice at the registered office of the company that is undergoing business rescue, on any website that is maintained by the company, if it is listed, on any electronic system maintained by the relevant exchange for the communication and inter-change of information by companies listed on the exchange. The practitioner must also either deliver a copy to each affected person or inform each affected person of the availability of the copy of that notice.[480]

3.2.7 Failure to adopt a business rescue plan

Section 153 makes provisions for various steps that can be taken by the business rescue practitioner or affected person where the proposed business rescue plan has been rejected under the provisions of section 152. Meskin describes section 153 as the last gasp attempt to have a proposed business rescue plan approved by

[476] *Ibid*.
[477] *Ibid* para 59.
[478] *Ibid*.
[479] Section 152(8).
[480] Regulation 125(6)(b)(i) and (ii).

attacking the rejection of the plan by the holders of the creditors' voting interests as "inappropriate" or by seeking approval for the practitioner to prepare and publish a revised plan or by purchasing the voting interests of one or more persons who opposed the adoption of the business rescue plan. If a practitioner does not seek a vote to prepare a revised plan, or advise the meeting that the company may apply to court to set aside the result of the voting as inappropriate, an affected person present at the meeting may call for a vote requiring the business rescue practitioner to prepare and publish a revised plan;[481] or may apply to court to set aside the result of the voting on the ground that it was inappropriate.[482]

In *Copper Sunset Trading 220 Pty Ltd v Spar Group and another,*[483] the court set aside the voting by a creditor as inappropriate on the basis that notwithstanding the fact that the creditor would not get a larger dividend under liquidation, the creditor still voted against the adoption of a business rescue plan.[484] The court in that case took into consideration the position of employees. However, the *Copper Sunset* decision was criticized in *Shoprite Checkers*[485] where the court held that the enquiry into the inappropriateness as a ground to set aside a vote on a business rescue plan should be viewed purely from the perspective of the person who voted against the plan; a consideration such as the loss of jobs by employees was not a factor that a court should consider. Tuchten J held that:

> The purposes of business rescue, broadly stated, are to revive faltering companies or achieve improved dividends for those companies which cannot be revived; in short, to put more money in the pockets of affected persons in general. In this context the interests of creditors, whose own money is at risk, are predominant. Whether either of these results can be achieved in a particular case depends on a forecast, which itself is based on one or more assumptions; in short on an assessment of risk. The business of companies and their creditors, in the present context, is the pursuit of monetary profit. I do not think that the purposes of the new Companies Act will be advanced by vesting in the courts a power to impose upon business people financial risks which they, on honest reflection, judge ill advised.[486]

The courts have adopted different approaches in determining whether a vote against business rescue plan was appropriate or not. There is need for the higher courts to determine the appropriate approach to be employed considering that the making of a business rescue order could be disadvantageous to creditors.

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[481] Section 153(1)(b)(i)(aa).
[482] Section 153(1)(b)(i)(bb).
[483] *Copper Sunset* case (note 304 above).
[484] *Ibid* para 38.
[485] *Shoprite Checker* case (note 456 above) para 44.
[486] *Ibid* para 38.

3.3 Conclusion

The business rescue practitioner is at the heart of business rescue. The practitioner is responsible for the supervision and management of the company during rescue proceedings. Therefore, every business rescue practitioner is required to be well acquainted with Chapter 6 provisions regardless of the field of expertise. It is however unfortunate that Chapter 6 provisions regulating business rescue proceedings are ill drafted and marred with anomalies. On one hand, the Act does not provide for the proper administrative mechanism. While practitioners are not required to furnish security for due performance of their duties the Act does not regulate the charging of contingency fees. The procedure to be followed when drafting and adopting a business rescue plan seem to be clear but certain definitions need to be addressed. The courts have offered divergent interpretations of some of the provisions. The legislature needs to re-examine some of the provisions of the Act so that the procedures offered by the Act become operative and cost effective.

CHAPTER FOUR

4. THE MORATORIUM IN BUSINESS RESCUE

4.1 Introduction

One of the reasons why corporate rescue schemes are not always successful in practise, is due to the fact that creditors cannot be prevented from taking enforcement proceedings while the rescue plan is in the process of being implemented.[487] Hence, "in any corporate rescue system there needs to be a circuit breaker that provides a breathing space whilst a consideration is given to the prospect of saving the company."[488] The success of business rescue, provided in Chapter 6 of the Companies Act of 2008, is guaranteed by a moratorium. In this regard, creditors and any other persons with legitimate claims against a financially distressed company, in business rescue, are prohibited from instituting legal proceedings against such company. Therefore, the moratorium is a crucial element of any corporate rescue mechanism, since it provides the crucial breathing space during which the company is given the opportunity to reorganise and reschedule its debts and liabilities.[489] In essence, without the moratorium, the reorganization of a financially distressed company would simply not be achievable. This chapter explains how the section 133 moratorium guarantees the success of business rescue and how it maintains a balance of the interests of stakeholders during the rescue process.

4.2 Moratorium/ Stay of proceedings

4.2.1 The meaning of moratorium

The concept 'moratorium' in business rescue implies the legal suspension of lawful remedies against debtors during times of general financial distress.[490] In *Investec Bank v Bruyns*[491] the court described the moratorium granted by section 133(1) as a general provision that affords the company protection against legal action on claims in general. Thus, the entire motivation behind business rescue procedures is to offer a financially distressed company some breathing space with a specific goal i.e. to enable its undertakings to be rebuilt so as to keep operating as a fruitful concern. During this period, the business rescue practitioner has the chance to formulate a

[487] Meskin (note 290 above) 18-50(12).
[488] C Anderson 'Viewing the proposed South African Business Rescue provisions from an Australian perspective" (2008) volume 11 Issue 1 *Griffiths Business School Journal* 8.
[489] Cassim (note 8 above) 894.
[490] J Law, A Elizabeth and M A Martin *Dictionary of Law* 8th ed (2015) 405.
[491] *Bruyns* case (note 239 above).

business rescue plan intended to resuscitate the company, but in the event that this cannot be accomplished, gain a better return for creditors.[492]

Cassim notes that as a general rule, the rights of the creditors are not substantially altered.[493] Instead, they are frozen in the sense that creditors may not enforce their rights while the company is under the rescue process without the written consent of the business rescue practitioner or the court.[494] Furthermore, the moratorium applies to all creditors, even dissenting creditors and secured creditors.[495] However, an incidental benefit of moratorium is that it results in an orderly and perhaps more equitable treatment of the claims of creditors.

Lightman and Moss express the opinion that "although it is convenient to describe it as a moratorium, the breathing space that the company is allowed is not an authorization to the company to postpone the payment of its debts but merely a limited immunity against enforcement of some legal rights."[496] In *Southern Palace Investment 265 Pty Ltd v Midnight Storm Investment 386 Ltd*[497] Eloff J also stated with concern that:

> The scheme created by the business rescue provisions in Chapter 6 of the new Act envisages that the company in financial distress will be afforded an essential breathing space while a business rescue plan is implemented by a business rescue practitioner. It is, however, necessary to caution against the possible abuse of the business rescue procedure, for instance, by rendering the company temporarily immune to actions by creditors so as to enable the directors or other stakeholders to pursue their own ends.

In *AG Petzetakis v Petzetakis*[498] Coetzee AJ emphasized that "Chapter 6 of the Companies Act demonstrates a legislative intention that rescue proceedings must be conducted reasonably speedily. The reason is obvious. Rescue proceedings temporarily protects the company concerned from legal proceedings by its creditors for the recovery of legitimate claims without any input of the creditors and removes the unfettered management of the company from the directors. Delays will extend the duration of these temporary statutory arrangements, of which the duration is restricted by way of the procedure prescribed by the Act."[499] It is, therefore, necessary to state that the judicially accepted justification for the moratorium is

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[492] Cassim (note 8 above) 894.
[493] *Ibid* 897.
[494] Section 133(1)(a) and (b).
[495] Cassim (note 8 above) 879.
[496] G Lightman, G Moss, H Anderson, Fletcher I. F and R Snowden *The Law of Administrators and Receivers of Companies* 4 ed (2007) para 2-040.
[497] *Southern Palace Investment* case (note 61 above) para 3.
[498] *AG Petzetakis* case (note 48 above).
[499] *Ibid* para 29.

simply to provide the company a period of grace to restructure its affairs in such a way as would allow it to resume operation on the basis of profitability.[500]

4.2.2 Interim Moratorium

Business rescue proceedings initiated in terms of section 129 (1) or section 131, becomes operational, upon the registering of such proceedings with the Companies and Intellectual Property Commission or on the issuing date of the court order allowing commencement of business rescue respectively. In other words, the moratorium does not apply unless and until either of the two abovementioned incidents is satisfied. This exposes the company to a run on its assets by the creditors in the period between the compulsory notification of the intended application and the order of the court that would result in the automatic moratorium.

To settle this *lacuna* the approach adopted under the English and German jurisprudence could be of assistance. An examination of the legislation in the UK and Germany indicates that the two jurisdictions accommodate some form of interim moratorium at this stage. In the UK an automatic interim moratorium is provided in terms of para 44 Schedule BI[501] which provides that a moratorium applies during the following periods of preparation for administration:

> (a) from when an application is made to the court for an administration order until the court's administration order takes effect or the application is dismissed;
> (b) from when the holder of a floating charge files with the court a notice of intention to appoint an administrator until the appointment takes effect, provided this is within five days;
> (c) from when a notice of intention to appoint an administrator is filed with the court by the company or its directors until the appointment takes effect, provided this is within 10 business days.

Loubser observed that "the scope of the interim moratorium is almost exactly the same as that of the final one, because the provisions of paragraphs 42 and 43 are made applicable to the interim moratorium."[502]

Whereas, in Germany "there is no provision for a general interim moratorium to come into effect automatically, but a stay of execution can be ordered by the insolvency court as soon as an application for the opening of insolvency proceedings has been

[500] A O Nwafor 'Moratorium in business rescue scheme and the protection of company's creditors' (2017) Volume 13 Issue 1 *Corporate Board: Role, Duties and Compositions* 60.
[501] UK Insolvency Act of 1986.
[502] Loubser (note 256 above) 193.

filed and without any specific application for such a stay being necessary."[503] It is submitted that with the exclusion of paragraph 44(b), similar provision as under the UK Insolvency Act Schedule B1 para 44 can be used to create an interim moratorium in the South African Companies Act to protect the company applying for business rescue from legal proceedings, while such application is pending.

4.3 Moratorium on civil legal proceedings

In terms of section 133(1) a company in business rescue is protected by an automatic moratorium from creditors who wish to enforce their claims against the company. The provision stipulates that:

> During business rescue proceedings, no legal proceedings, including enforcement action against the company, or in relation to any property belonging to the company, or lawfully in its possession, may be commenced or proceeded with in any forum except-
> (a) with the written consent of the practitioner;
> (b) with the leave of the court and in accordance with any terms the court considers suitable;
> (c) as a set-off against any claim made by the company in any legal proceedings, irrespective of whether those proceedings commenced before or after the business rescue proceedings began;
> (d) criminal proceedings against the company or any of its directors or officers; or
> (e) proceedings concerning any property or right over which the company exercises the powers of a trustee.

It is clear that the general moratorium created by this section applies only for the duration of the company's business rescue proceedings. In *Investec Bank Ltd v Bruyns*[504] the surety was held liable for the debts of the company under business rescue. The court held that the business rescue plan may protect the surety. Rogers J held that:

> In my view the statutory moratorium in favour of a company that is undergoing business rescue proceedings is a defense *in personam.* It is a personal privilege or benefit in favour of the company. The essence of a defense *in rem* is that the defense attaches to the claim itself in the sense that the defense (if upheld) shows that the claim against the principal debtor is invalid or has been extinguished or discharged. A defence *in personam,* by contrast, arises from a personal immunity of the debtor in respect of an otherwise valid and existing obligation. Clearly the moratorium afforded by section 133(1) falls into the latter class.

In other words, the moratorium provided in terms of section 133 only protects the company, in business rescue, as a principal debtor not its surety or sureties against claims instituted by the creditor. The *obiter dictum* in *Griessel and another v*

[503] *Ibid* 85.
[504] *Bruyns* case (note 239 above) para 18.

Lizemore and another[505] by Spilg J indicated that section 133 is intended to protect the company from claims against or recovery of assets against it, and does not deal with orders that seek to protect or recover property for the company's benefit. The section 133 moratorium applies to legal proceedings and property interests.

The courts and legal scholars have continued to struggle with the interpretation and application of section 133 while striving to preserve the legislative objectives in the enactment of Chapter 6 business rescue provisions. With regards to the interpretation of the term "legal proceedings" and "enforcement action", Delport argues that although no definition of the terms legal proceedings or enforcement action is provided in Chapter 6, it is clear that the intention of the provision is to cast the net as wide as possible in order to include any conceivable type of action against the company.[506] However, Nwafor begs to differ and contends that:

> Legal proceedings and enforcement actions are, by their nature, necessarily ancillary (if not expressly stated) parts of contractual rights and obligations of parties to an existing agreement. Putting a wedge on legal proceedings emanating from a contractual obligation does invariably interfere with the existing contractual right. The application in context of section 133(1), galvanized by the legislative intention of allowing some breathing space to a company in financial distress to return to status of profitability, would not unreasonably entail casting the scope of that provision as wide as to include every conduct of the creditor, based on existing contract with the company, that could materially affect the realization of the purpose of that provision. This would strip the creditors of all vestiges of protection in all contractual relationships with the company during the subsistence of the moratorium except to the extent specifically allowed by that provision.[507]

This would, in principle, mean that creditors are only entitled to the rights protected by that provision.[508] In *Murray NO and another v FirstBank Ltd* [509] Fourie AJA held that:

> The way I see it, the legislature intended to allow the company in distress the necessary breathing space by placing a moratorium on legal proceedings and enforcement action in any forum, but not to interfere with the contractual rights and obligations of the parties to an agreement. Such an intention would, in any event, be contrary to the tenet of our law that the legislature does not intend to alter the existing law more than is necessary, particularly if it takes away existing rights.

In view of Nwafor's contention and Fourie AJA's finding, it is submitted that although the meaning of "legal proceedings" and "enforcement action" are not provided in the Act, their application should not be in a manner that alters the existing rights of creditors for this would not only offend but defile the sanctity of contracting. The

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[505] *Griessel* case (note 101 above) at para 104.
[506] Delport (note 71 above) 480(31).
[507] Nwafor (note 500 above) 61.
[508] *Ibid*.
[509] 2015 (3) SA 438 (SCA) para 40.

meaning of legal proceedings and enforcement action can best be described in the light of the following different cases.

4.3.1 Legal Proceedings

The term "legal proceedings" was dealt with in *Chetty v Hart*.[510] In that case the court had to determine whether arbitration proceedings constituted legal proceedings as envisaged by section 133(1). In order to answer this question, the court took cognizance of the language and the design of the statute as a whole and the purpose of the statute.[511] The court adopted the purposive interpretation and found that "the phrase legal proceeding may, depending on the context within which it is used, be interpreted restrictively, to mean court proceedings or more broadly, to include proceedings before other tribunals including arbitral tribunals. The language employed in section 133(1) itself suggests that a broader interpretation commends itself."[512] This approach was also followed in *Environment Agency v Administrator of Rhondda Waste Disposal Ltd*[513] an English case, where the court had to interpret a similar provision under the UK Insolvency Act of 1986. Section 11(3)(d) of the Insolvency Act provides that

> During the period for which an administration order is in force -
> d) no other proceedings and no executions or legal process may be commenced or continued, and no distress may be levied, against the company or its property except with the consent of the administrator or the leave of the court and subject (where the court gives leave) to such terms as aforesaid.

While interpreting the phrase "no other proceedings"; Scott Baker LJ in *Environment Agency*[514] said that:

> It seems to me that they have a plain and clear meaning. The words: "No other proceedings and no executions or other legal proceedings may commence or continued against the company or its property" cover on their face all judicial and quasi-judicial proceedings. There is no qualification to "other proceedings". The sections do not say "no other civil proceedings"; nor is there any reference to excluding category of proceedings. The words used are entirely apt to include all judicial proceedings.

In *Air Ecosse Ltd and others v Civil Aviation Authority* [515] Lord MacDonald noted that "the restrictions in section 11(3) are directed against the activities of the creditors of the company which might otherwise be available to them in order to secure or

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[510] [2015] 4 All SA 401 (SCA) para 35.
[511] D Lloyd and L Msomi 'Legal proceedings under business rescue' (2016) Volume 16 Issue 7 *Without Prejudice* 33.
[512] *Chetty* case (note 510 above) para 35.
[513] [2000] EWCA Civ 38 para 27.
[514] *Ibid* para 27.
[515] (1987) 3 BCC 492 at 494.

recover their debts." Nwafor opines that "this, incidentally, is the position adopted by South African courts". For instance in *Chetty v Hart*,[516] Cachalia JA held that "It bears mentioning that the moratorium only suspends legal proceedings *against* a company under business rescue and not *by* the company."[517] In that context, the law has certainly placed the company under business rescue in a more advantageous position than the creditors.[518] This should be considered by the court when a creditor applies for leave to institute proceedings against a company during the operation of a moratorium since the aim of business rescue is to revive companies in financial distress and doing so in a manner that balances the rights of all stakeholders.

It is important to state that the court in *Chetty* accepted that arbitration proceedings constitute legal proceedings as contemplated in section 133(1). Potgieter observed that "the court considered section128(1)(b) and decided that the obvious purpose of placing a company under business rescue is to give it breathing space so that its affairs may be assessed and restructured in a manner that allows its return to financial viability. This is the purpose of business rescue and because, like court proceedings, arbitration proceedings also involve diversion of resources, it may hinder the effectiveness of business rescue proceedings. Only an interpretation that includes arbitration within the meaning of legal proceedings in section 133(1) is in harmony with the intention of the legislature."[519] It is therefore submitted that the term legal proceedings includes all legal proceedings which if pursued may hinder or obstruct the realisation of the objectives of business rescue.

4.3.2 Enforcement Action

A clear demonstration of the meaning of the terms 'enforcement action' is found in *Murray and another v FirstRand Bank.*[520] In that case, FirstRand Bank (Wesbank) entered into a sale contract with Skyline Crane Hire (Skyline). In terms of this agreement, Wesbank sold goods to Skyline under the condition that ownership would be transferred from Wesbank to Skyline upon the full payment of the purchase price. Skyline became financially distressed, more so it had arrears in respect of the monthly installment payment due to Wesbank under the agreement. It follows that, Skyline was placed under business rescue and in response Wesbank furnished a letter of cancellation of the agreement. The cancellation letter specified that Wesbank was going to repossess the goods, value and sell them and credit the proceeds to

[516] *Chetty* case (note 510 above).
[517] *Ibid* para 47.
[518] Nwafor (note 500 above) 62.
[519] A Potgieter 'Business rescue moratorium' (2016) Volume16 Issue 2 *Without Prejudice* 20.
[520] *Murray* case (note 509 above).

the Skyline account. The business rescue practitioner consented to the repossession and selling of the goods. However, the business rescue failed and Skyline was placed under liquidation. The liquidators then challenged the cancellation of the contract by Wesbank.

The liquidators argued that the cancellation by Wesbank was not valid, in that, the cancellation amounted to an "enforcement action" as contemplated in section 133. Thus, the cancellation required the written consent of the business rescue practitioner or leave of the court. Hence, according to the liquidators the cancelation was of no force or effect. On the other hand, Wesbank contended that the cancellation did not constitute "enforcement action" thus there was no need for consent or leave of the court. The court had to determine whether cancellation of an agreement constituted "enforcement action" as envisaged in section 133(1) of the Act.

Fourie AJA held that the term "legal proceeding" is common legal expression in the South African legal parlance and usually means lawsuit or 'hofsaak' in the Afrikaans translation. Hence, cancellation of a contract does not constitute legal proceeding in terms of section 133(1). The court did not dwell much on the interpretation of the term "legal proceedings", hence its finding is not conclusive. However, the court accepted that the term "enforce" or "enforcement action" refers to the enforcement of obligations and held that:

> In the context of s 133(1) of the Act, it is significant that reference is made to 'no legal proceeding, including enforcement action'. (My emphasis.) The inclusion of the term 'enforcement action' under the generic phrase 'legal proceeding', seems to me to indicate that 'enforcement action' is considered to be a species of 'legal proceeding' or, at least, is meant to have its origin in legal proceedings. This conclusion is strengthened by the fact that s 133(1) provides that no legal proceeding, including enforcement action, 'may be commenced or proceeded with in any forum'. (My emphasis.) A 'forum' is normally defined as a court or tribunal (see the Concise Oxford Dictionary 12 ed (2011)) and its employment in s 133(1) conveys the notion that 'enforcement action' relates to formal proceedings ancillary to legal proceedings, such as the enforcement or execution of court orders by means of writs of execution or attachment.[521]

Therefore, the concepts of "enforcement" and "cancellation" are traditionally regarded as mutually exclusive. Cancellation means the termination of obligation between parties to an agreement and cannot be construed to mean enforcement action as contemplated in section 133(1) of the Act. As such the correct interpretation of section 133(1) was held to contextually refer to enforcement action by means of legal proceedings. Nwafor observes that:

[521] *Ibid* para 32.

> Although the Supreme Court in Murray had interpreted 'enforcement action' as emanating from the generic phrase 'legal proceeding', thus, suggesting the occurrence of chain of events within the operative course of the statutory moratorium to bar the exercise of the creditor's right, the framing of section 133(1) which uses a comma to separate 'legal proceeding' from 'enforcement action' suggests that both operative phrases could also be read disjunctively. In other words, the provision implies that no 'legal proceedings' or 'enforcement action' may be commenced or proceeded with while the company is under business rescue. Reading it in such a manner entails that even when court action is already concluded and judgment entered before the commencement of business rescue, the enforcement of the order of court cannot be proceeded with while business rescue is in place.[522]

It is submitted that the interpretation by the Supreme Court of Appeal gives effect to the objectives of business rescue projected in section 7(k) that is to provide a financially distressed company a grace period while maintaining a balance of the rights of all stakeholders. Watson and Thakur note that the decision in *Murray* affirms that "it is not the purpose of business rescue to cast creditors and other stakeholders adrift."[523] Nwafor's opinion is double barreled in nature. On one hand, it acknowledges the need to balance the rights of all stakeholders, and on another hand, promotes an interpretation that does not lead the debtor company into incurring more expenses before business rescue is sustainably realized. Tsusi notes that in view of this judgment "a creditor of a company may cancel a contract if such is in breach of an agreement, this cannot, according to section 133(1) be regarded as an enforcement action falling under the notion of moratorium."[524]

4.4 Moratorium on property interest

The exercise of right by a creditor over property owned by the creditor in the possession of the company under business rescue is suspended by the Act. Section 134(1)(c) provides that

> (1) Subject to subsections (2) and (3), during a company's business rescue proceedings;
> (c) despite any provision of an agreement to the contrary, no person may exercise any right in respect of any property in the lawful possession of the company, irrespective of whether the property is owned by the company, except to the extent that the practitioner consents in writing.

The interpretation of this section has led to different conclusions. The South African perspective seems to lack clarity hence scholars have resorted to foreign case law to find an acceptable interpretation. The discussion below is an example of the

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[522] Nwafor (note 500 above) 61.
[523] S Watson and C Thakur 'Interpreting enforcement action' (2016) Volume 16 Issue 7 *Without Prejudice* 30.
[524] R Tsusi 'Interpretation of section 133(1) of the Companies Act 71 of 2008- the principle of moratorium redefined under business rescue (2015) Volume 2015 Issue 554 *De Rebus* 52.

difficulties encountered by the courts and scholars in the interpretation of this provision.

4.4.1 Lawful possession

According to section 128 business rescue means "proceedings to facilitate the rehabilitation of a company that is financially distressed by providing; … for a temporary moratorium on the rights of claimants against the company or *in respect of property in its possession*." Whereas, section 133(1) states that "during business rescue proceedings, no legal proceeding, including enforcement action, against the company, or in relation to any property belonging to the company, or *lawfully in its possession*, may be commenced or proceeded with in any forum…" The moratorium provided by section 128 protects the property in the company's possession. In essence that provision does not specify whether the possession is lawful or unlawful. What is factual is that the company must be in possession of the property for it to be protected by the moratorium. However, in section 133(1) and section 134(1)(c) the legislature added another requirement, that the company must be in lawful possession of the property. Therefore there are two possible interpretations that can be ascribed to the word "possession" in section 128, 133(1) and 134(1)(c). In *JVJ Logistics Pty Ltd v Standard Bank and others*[525] Olsen J attempted to interpret the meaning of these three provisions and remarked that "[t]he interpretive exercise in this case is not free from difficulties."[526]

In that case, the court addressed the question whether mere factual possession meets the requirements of s 133(1). Olsen J held that possession is the compound of a factual situation and a mental state, comprising the actual control or detention of an item of property coupled with the will to possess the thing.[527] In other words, possession is a correlation of two facts: physical detention of the property coupled with the existence of an intention to possess or keep control of the thing. However, the fact of possession does not of itself speak to any right of the possessor to possess the property. The court further held that:

> The mere fact of possession generates a right which is generally referred to as the *jus possessioni* The content of that right does not proceed beyond the right to the assistance of the courts to restore factual possession when dispossession against the will of the possessor takes place without the sanction of law. It is only to that extent that the spoliation remedy is a

[525] [2016] 3 All SA 813 (KZD).
[526] *Ibid* para 20.
[527] C G Van Der Merwe and A Pope 'PART III Property' ed F du Bois, G Bradfield, C Himonga, D Hutchison, K Lehmann, R le Roux, M Paleker and D Visser *Wille's Principles of South African Law* 9th ed (2007) 445.

> reflection of a right. It is not a right which is acquired from any person; it is automatically generated by a state of affairs – i.e. the fact that the property is possessed.[528]

Cameron JA had the following to say about the spoliation remedy in *Tswelopele Non-Profit Organisation and Others v City of Tshwane Metropolitan Municipality and Others;*[529] "Under it, anyone illicitly deprived of property is entitled to be restored to possession before anything else is debated or decided (*spoliatus ante omnia restituendus est*). Even an unlawful possessor – a fraud, a thief or a robber – is entitled to the *amendment's* protection. The principle is that illicit deprivation must be remedied before the Courts will decide competing claims to the object or property." The court in *JVJ Logistics*[530] observed that:

> When the law protects mere factual possession it does not do so because of the lawfulness of the possession, but in order to address the unlawfulness of the deprivation of possession. Accordingly, the requirement of s 133(1) of the Act, that to enjoy the benefits of the moratorium against proceedings in respect of property possessed by a company, the possession should be "lawful", cannot be established merely by the fact that the company happens to possess the property at the time when business rescue commences. It is correct that the definition of "business rescue" in s 128 of the Act speaks of a moratorium protecting "possession" (i.e. without the qualification that it should be lawful), whilst the operative provisions (the one under consideration and s 134(1)(c)) address only the protection of lawful possession. To the extent that it may be said that there is a conflict it can only be resolved in favour of the operative provisions as, whilst they can be read consistently with the definition, the converse is not true if the word "possession" in the definition is read to encompass possession of any kind or origin.

Olsen J concluded that there are two meanings that can be ascribed to the term "lawful" as envisaged in section 133(1). The first one being that the company in possession of the property lacks the so-called *jus possidendi*.[531] In other words, it does not have "a right which justifies a person's claim to have a thing in his possession".[532] On this approach the requirement of section 133(1) is that the company's possession should be lawful when judged from any perspective; or if not that, then lawful when judged from the perspective of any claim by a third party to possession of the property.[533]

In *Southern Value Consortium v Tresso Trading 102 Pty Ltd*[534] the court held that:

> My interpretation of section 134(1)(c) is also supported by considerations of reasonableness and practicality. If an owner of a thing cannot vindicate it

[528] *JVJ logistics* case (note 525 above) para 22.
[529] 2007 (6) SA 511 (SCA) para 21.
[530] *JVJ Logistics* case (note 525 above) para 24.
[531] *Ibid* para 25.
[532] *Ibid*.
[533] This approach found application in *Madodza Pty Ltd v ABSA Bank Ltd and others* (38906/2012) [2012] ZAGPPHC 165 (12 August 2012).
[534] 2016 (6) SA 501 (WCC) para 33.

> from an unlawful possessor it would give rise to a stalemate situation. The owner (applicant in casu) would in effect be deprived of his power to exercise his ownership in the thing whilst the possessor (respondent in *casu*) would be unable to use it as such use would be unlawful. In my view it could not have been the legislature's intention that the company in business rescue would restructure its affairs by utilising assets to which it has no lawful claim.

It is submitted that the court in *JVJ Logistics* did not take into consideration the differing opinions on whether possession is a fact or a real right. Several South African writers and court decisions have adopted the view that the possessor acquires a real right.[535] Conversely, it is also suggested that possession should not be seen as a real right, but rather as an adjunct to the law of property or as a right *sui generis*. The key to the solution to this dilemma lies in maintaining a clear distinction between the fact of possession and the right flowing from possession. Van der Merwe and Pope conclude that "[e]mphasis on the fact of possession easily leads to the conclusion that possession is a fact; emphasis on the rights flowing from possession leads to an approximation of possession to real right."[536] In consideration of this assertion and the court's views it is submitted that there exists two interpretations as to the meaning of possession. Possession may be regarded as a fact or as a real right.

In *JVJ Logistics Pty Ltd v Standard Bank of South Africa*[537] the court concluded that the requirement of the Companies Act section 133(1) that to enjoy the benefits of moratorium against a company during business rescue proceedings in respect of property possessed by the company, the possession should be lawful, cannot be established merely by the fact that the company happens to be in possession of the property at the time when business rescue commences. If the requirement for the operation of the moratorium is merely that the company's possession should not be criminally unlawful, the potential for substantial period of operation of the moratorium imposed by the section suggests that the burden it would impose on the owner of property is too great to meet the requirement that there should be a balance of rights and interests.

The issue of possession becomes complicated and intricate where the company merely asserts the right of possession over the property, especially where the property is in actual possession of a third party, there will be the question as to whether the property is indeed in the possession of the company? To address this

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[535] Van der Merwe and Pope (note 527 above) 446. See *Matthee v Schietekat* 1959 (1) SA 344 at 347, *Buchholtz v Buchholtz* 1980 (3) SA 424 (W) at 425, *Chiloane v Maduenyane* 1980 (4) SA 19 (W).
[536] Van der Merwe and Pope (note 527 above) 446.
[537] [2016] 3 All SA 813 (KZD) at M1112.

question, Nwafor refers to foreign case law for direction.[538] In *Towers and Co Ltd v Gray,*[539] the court held that the term "possession" is always giving rise to trouble. His Lordship referred to the statement made by Earl Jowitt in *United States of America and Republic of France v Dollfus Mieg et Cie SA and Bank of England*[540] that "[t]he person having the right to immediate possession is, however, frequently referred to in English Law as the 'possessor'- in truth the English law has never worked out a complete logical and exhaustive definition of 'possession'". However, Lord Parker held that:

> [T]he meaning of possession depends upon the context in which it is used…In some contexts, no doubts, a bailment for reward subject to lien, and where perhaps some period of notice has to be removed , could be of such a nature that the only possession that there could be said to be would be possession in the balilee. In other cases it may well be that the nature of the bailment is such that the owner of the goods who has parted with the physical possession of them can truly be said to still be in possession.

The Constitutional Court had in *FNB v Commissioner SARS.*[541] held that the possession of a movable property requires both physical control (detention) and the necessary state of mind (animus). In *S v Brick* [542] Thompson CJ notes that the precise meaning to be assigned to the word "possession" occurring in a penal statute is often a matter of considerable difficulty. The difficulty may sometimes be lessened if the word is used in association with "custody". In the ultimate analysis, however the decision vitally depends upon the intention of the legislature as reflected in the context of a particular statutory enactment. Therefore, the meaning to be assigned to the term "possession" should be in line with the purpose and objective of the statute in which it was used.

The UK Court of Appeal in *AIB Capital Markets Plc v Atlantic Computer Systems Plc & Others,*[543] preferred a purposive approach to the interpretation of 'possession' in a similar provision in section 11(3)(c) of the UK Insolvency Act of 1986. Nicholls LJ stated:

> The paragraph is dealing with goods which, as between the company and its supplier, are in the possession of the company... Those goods are to be protected from repossession unless there is either consent or leave. It is immaterial whether they remain on the company's premises, or are entrusted

[538] Nwafor (note 500 above) 62.
[539] [1961] 2 QB 351 at 361.
[540] [1952] AC 582 AT 605.
[541] 2002 (4) SA 768.
[542] 1973 (2) SA 571 (A) at 579H.
[543] [1990] EWCA Civ 20.

> by the company to others for repair, or are sub-let by the company as part of its trade to others.[544]

It is submitted that "the provision of section 134(1)(c) is amenable to a similar line of construction taking into consideration the legislative intention and purpose of that provision as the guiding approach. The provision refers to 'lawful possession' and not 'actual possession'. This would ordinarily include actual and constructive possession so long as the company can legitimately lay a claim on the property while under business rescue."[545]

4.5 Exceptions to the moratorium

The application of the moratorium is not without restriction. Section 133 provides a list of circumstances where the moratorium does not apply which includes, when a creditor has obtained the written consent of the practitioner or leave of the court; where the transaction is a set-off or where there are criminal proceedings against the company.

4.5.1 Consent of the business rescue practitioner

Section 133(1)(a) provides that an affected person may obtain consent from the business rescue practitioner if he wishes to institute proceedings against the company in business rescue. In respect of the requirement that the consent must be in writing, the Supreme Court of Appeal made the following (obiter) remark in the *Murray* case: "I do not believe that the requirement of writing should necessarily be regarded as peremptory rather than directory. In this regard, it is important to note that there is no sanction added in case the requirement is not met, nor does the section state that a failure to meet the requirement of written consent should be visited with nullity."[546] However, subsection (2) is clear on the formal requirements and the fact that there is no sanction or an express provision that non-compliance will result in the action being a nullity, does not imply that informal consent, even by way of conduct of the practitioner should be sufficient.

The written consent of the practitioner should also indicate the intention in giving such consent especially in instalment sales.[547] The consequences of such consent are such that it should be in writing, because in the case of an instalment sale it could

[544] *Ibid* para 42.
[545] Nwafor (note 500 above) 63.
[546] *Murray* case (note 509 above) para 24.
[547] *Ibid* para 22.

have the effect that possession is restored to the seller.[548] This power of the business practitioner shows the differences between business rescue and winding up.

4.5.2 Leave of the court

In terms of section 133(1)(b) a creditor who wishes to institute or continue legal proceedings against a company in business rescue must either obtain consent of the business rescue practitioner or apply for leave of the court. A question that arises when the court is approached under section 133(1) for the continuation of legal proceedings is whether a separate application for leave to institute or continue with legal proceedings needs to be brought, or whether such leave may be sought as part of the application for the relief sought. In *Elias Mechanics Building and Civil Engineering Contractors (Pty) Ltd v Stedone Developments (Pty) Ltd and others* [549] the court found that the moratorium on legal proceedings against a company has the result that leave to institute proceedings must be obtained by way of separate proceedings before the commencement of proceedings and not as part of the relief in the main proceedings. A contrary view was held in *African Banking Corporation of Botswana Ltd v Kariba Furniture Manufacturer (Pty) Ltd*[550] where the requisite leave to commence proceedings was granted as part of the relief claimed in the main proceedings. In *Safari Thatching Lowveld CC v Mist Mountian Trading 2 (Pty) Ltd* [551] the court held that "it is legally competent for a litigant to request the requisite leave to continue with the already commenced legal proceedings during those proceedings when faced with a subsequent application to commence business rescue proceedings and the moratorium imposed thereon by section 133(1)."

A related question in the context of section 133(1)(b), is what test should be applied by the court in determining whether or not to grant leave for a party to institute or continue with legal proceedings against a company in business rescue. In *Merchant West Working Capital Solutions v Advanced Technologies and Engineering Company Pty Ltd* [552] the court defined the phrase "leave of the court". Kgomo J held that:

> "*Leave of the court*" as laid down in section 133(1)(b) cannot be a simple one that can be advanced from the bar. Such leave in my view and finding must be motivated in the same way, just like, for instance, as criteria for departure from the Rules of Court to justify a prayer for urgency. A court being asked for leave to proceed against a company under business rescue, thus during a

[548] Delport (note 71 above) 480(43).
[549] 2015 (4) SA 485 (KZD).
[550] *African Banking Corporation* (note 44 above).
[551] 2016 (3) SA 209 (GP) para 4.14.
[552] (13/12406) [2013] ZAGPJHC 109 (09 May 2013) at para 67.

> moratorium, must receive a well-motivated application for that so that it could apply its mind to the facts and the law if necessary and then be in a position to make a ruling in accordance with any terms it may consider suitable in the peculiar circumstances.

This approach was also acknowledged in *Redpath Mining South Africa Pty Ltd v Marsden NO and others*.[553] In that case, the court held that a court may only permit litigation against a business rescue plan or issues related thereto in exceptional circumstances. However, in both cases there are no indications as to what the requirements are for a "well-motivated application" or the minimum threshold that must be met for an applicant to obtain such leave. In *Matobe and others v Van der Merwe NO and another*[554] it was required that an applicant seeking to obtain leave under section 133 must as a minimum requirement establish a *prima facie* case against the company. Boruchowitz J went on to provide a list of some of the factors the court can take into consideration. The court held that:

> There is no closed list of the factors that may be taken into account in deciding whether or not to grant leave as each case must be determined on its own facts. Without being prescriptive in any way, the following considerations are relevant: (a) The effect that the grant or refusal of leave would have on the applicants' rights as opposed to other affected persons and relevant stakeholders; (b) The impact that the proposed legal proceedings would have on the well-being of the company and its ability to regain its financial health; and (c) whether the grant of leave would be inimical to the object and purpose of business rescue proceedings as set out in sections 7(k) and 128(b) of the Act.[555]

The court emphasized that exceptional circumstances is not a prerequisite for the launching of such an application.[556] According to Boruchowitz J, if the legislature had intended that the application be limited to exceptional circumstances, a test would have been provided in the Act.[557] Van Niekerk expresses a concern with regards to the findings of the court. He submits that "to find that an applicant has to merely show that an envisaged action needs only pass the scrutiny of being a triable issue, not even having to show that such action will be successful on an unopposed basis – is (at least in my mind) setting the bar too low."[558] In other words, an applicant merely has to formulate a pleading that is not excipiable. If this is the case, business rescue practitioners will, in all probability, be spending most of their time enmeshed in litigations.

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[553] 18486/2013 14 June 2013 (GSJ) para 71.
[554] (2015/40324) [2016] ZAGPJHC 185 (8 July 2016) para 16.
[555] *Ibid* para 28.
[556] *Ibid* para 29.
[557] *Ibid.*
[558] B Van Niekerk 'In the matter of moratorium' (2016) Volume 16 Issue 9 *Without Prejudice* 8.

In *2001 Management Services (Pty Ltd v Anappa and another* [559] the court held that the bona fides of the initiator of business rescue proceedings is an important consideration when leave is sought to lift the moratorium in terms of section 133. In order to enable the court to exercise its discretion judiciously in considering the leave sought, it is incumbent upon an applicant who seeks such leave to take the court into confidence and disclose to the court the legal proceedings which he intends to initiate.

4.5.3 Set-off

In terms of section 133(1)(c) legal proceedings against the company may be proceeded with if it amounts to set-off against any claim made by the company in legal proceedings, irrespective of whether the proceedings commenced before or after the commencement of the business rescue.[560] This provision may prove to be an incentive for creditors to intervene in liquidation proceedings by making an application for business rescue where they have counter-claims against the company, and which they would not be entitled to set-off against their own claims should formal insolvency intervene.[561] A secured creditor can, apparently, apply for set-off, a bank can set-off the credit balance in one account to reduce the debit balance on another account. This example is demonstrated in *Kritzinger and another v Standard Bank of South Africa,*[562] where the court held that:

> [A] secured creditor is entitled *ex lege* to apply a set-off. Section 133(1) does not, on the facts, preclude the bank from applying the credit balance in one account to reduce the debit balance in another account. The bank has a common law right to do so. But even if I am wrong, it would be inequitable, in this instance, to order the respondent, whose security has been drastically diminished if not completely eroded by the applicants, to reverse the set-off transaction and to release the affected funds to the very same parties whose collaborative and subversive conduct has rendered its security for repayment of the overdraft facility meaningless.

4.6 Sureties and guarantees

Section 133(2) states that the moratorium has no effect on guarantees and sureties. In *Investec Bank Ltd v Bruyns*[563] the court had occasion to distinguish between the moratorium provision contained in section 133(1) and the specific provisions relating to sureties and guarantees as contained in section 133(2). In making this distinction, Rogers AJ stated that:

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[559] (88079/14) [2016] ZAGPPHC 353 (20 May 2016) at para 42.
[560] Amended by section 84 (a) Companies Act No 3 of 2011.
[561] Meskin (note 290 above) 18-50 (18).
[562] (3034/2013) [2013] ZAFSHC 215 (19 September 2013) para 77.
[563] *Bruyns* case (note 239 above).

> Section 133(1) is a general provision and affords the company protection against legal action on claims in general except *inter alia* with the written consent of the business rescue practitioner or (presumably failing such consent) with the leave of the court. Section 133(2) is a special provision dealing specifically with the enforcement of claims against the company based on guarantees and suretyships, and stipulates that in such cases the claims against the company may be enforced only with the leave of the court. The business rescue practitioner is not empowered to consent to the enforcement against the company of claims based on guarantees and suretyships. Section 133(2), as the special provision, would apply to the exclusion of s 133(1) insofar as claims based on guarantees and suretyships are concerned.

The defendant in this case was being sued as surety for the debts of two companies and *inter alia* raised as a defence the statutory moratorium in terms of section 133(1) in favour of the principal debtors (the two companies) which would preclude the plaintiff from enforcing the claims against the principal debtors. In response to this defence, the court found that the statutory moratorium created by section 133(1) is a defence in *personam* and would not have the effect of extinguishing or discharging the obligation of the principal debtor.[564] In *African Banking Corporation of Botswana v Kariba Furniture Manufacturers Pty Ltd and others*[565] the court emphasized that:

> [T]he interests of sureties do not fall within the scope of the objective of the business rescue regime. This is clear from the provisions of s 133(1) of the Act, which provides that during the course of business rescue proceedings no legal proceedings, including enforcement action against the company, or in relation to any property belonging to it or in its possession, may be commenced or proceeded with, except under certain circumstances. Section 133(2) provides that during business rescue proceedings, a surety by a company in favour of any other person may not be enforced by any person against the company, except with the leave of the court.

The court held further that "the moratorium provided for in section 133 is directed exclusively at protecting the interests of the company in business rescue. By parity of reasoning, if the legislation does not suspend the indebtedness of a surety pending the outcome of the business rescue proceedings, it is difficult to see how it could deprive entirely a creditor of its rights against a surety."[566] Thus, section 132(2) protects the interests of creditors by allowing them to institute proceedings against sureties instead of principal debtors where the principal debtor has failed to pay its debt.

In *Tuning Fork Pty Ltd t/a Balanced Audio v Greeff and another 2014 (4) SA 521 (WCC)*,[567] the legal question was whether a creditor loses its claim against a surety if a duly adopted and implemented business rescue plan provides for the creditor's

[564] *Bruyns* case (note 239 above) paras 17 to 19.
[565] *African Banking Corporation* case (note 44 above) para 70.
[566] *Ibid* para 71.
[567] 2014 (4) SA 521 (WCC).

claim against the principal debtor to be compromised in full and final settlement of such claim." The adopted business rescue plan provided for a reduced payment to the creditor in full and final settlement of all its claims. When the sureties were sued for the balance of the debt owing to the creditor, they argued that the compromise contained in the adopted plan released them from liability. The court upheld the sureties' case because the deed of suretyship provided that such a right.

On the other hand, in the case of *New Port Finance Company (Pty) Ltd v Nedbank,*[568] the position was different in that the deed of suretyship contained a clause that preserved a right for the creditor to pursue the sureties for any shortfall arising after payment of any compromised claim in the business rescue process. The courts have reached divergent interpretations of section 133(2) and this is an indicator that any conclusion reached will either favour or prejudice the surety. The problem emanates from the fact that "there is no provision in the Act which states that the moratorium does or does not operate in favour of a surety for the distressed company."[569] The legislature needs to revisit section 133(2).

4.7 Protection of property interests

The moratorium applies to creditors but this does not mean that the activities of the company are not limited. The power of the company to deal with its property is restricted during business rescue. Section 134(1)(a) provides that the company may only dispose of property if it takes place:

- in the ordinary course of business; or
- in a transaction in good faith to which the business rescue practitioner has given consent; or
- as part of an approved rescue plan.

Delport states that the purpose of section 134 is to protect the interests of both the company and third parties where the company is placed under supervision in terms of Chapter 6.[570] In broad terms the provisions allow for the disposal of company property in circumstances where it is required for the normal operation of business, or as part of a business rescue plan.

[568] [2015] 2 All SA 1 SCA.
[569] *Ibid* para 28.
[570] Delport (note 71 above) 480(40).

It is not only the actual, physical disposal of property that is covered by this section, but also agreements entered into for disposal of company property.[571] In such a case, the agreement itself will have to comply with the prerequisites set by this provision.[572] In *LA Sports 4x4 Outdoor CC and another v Broadway Trading 20 Pty limited and others*[573] the court held that rights under a contract do not constitute property in possession of the company for purposes of section 134(1). This dictum however is in respect of the rights of a third party to cancel a contract or compel performance of a contract, which are as stated in that case, clearly not property in possession of the company but in possession of the third party.

The expression in the 'ordinary course of business' has not been defined in the context of Chapter 6. However, direction is offered by section 29 of the Insolvency Act dealing with voidable preferences. In *Griffiths v Janse van Resburg NO,*[574] Gorven AJA held that:

> There has been much judicial comment on what is meant by the phrase 'the ordinary course of business'. It is not necessary to rehearse all of it. This court has been consistent over many years in the test to be applied. The test is an objective one. The disposition should be evaluated in the light of all relevant facts. This must be done on a case by case basis. Put traditionally, the disposition 'must be one which would not to the ordinary [person] of business appear anomalous or unbusiness like or surprising.'[575] The question is whether ordinary, solvent, businesspeople would, in similar circumstances, themselves act as did the parties to the transaction.

Applying the principles contained in the case law on the meaning of "in the normal course of business" in respect of section 29 of the Insolvency Act, the determination of whether a disposal of property, or an agreement for disposal of property, is made in the ordinary course of its business should entail a consideration of all the circumstances under which it was made, coupled with a decision as to whether, given such circumstances, it would have occurred between solvent businessmen.[576]

What would amount to "a *bona fide* transaction" is not explained in the Act. However, it is submitted that all that is envisaged here is that the transaction should not be a simulated one, that there should not be a questionable relationship between the company and the other party to the transaction, and that the purchase price should

[571] Delport (note 71 above) 480(41).
[572] Section 134(1). The requirements are that the disposal must take place in the ordinary course of business, or in a transaction in good faith that has been consented by the business rescue practitioner or is part of an approved business rescue plan.
[573] (A513/2013) [2015] ZAGPPHC 78 (26 February 2015) para 47.
[574] [2016] 1 All SA 6 para 11.
[575] *Malherbe's Trustee v Dinner & others* 1922 OPD 18 at 22.
[576] See *Hendricks NO v Swanepoel* 1962 (4) SA 338 (AD) AT 345; *Almagamated Banks of South Africa Bpk v De Goede* 1997 (4) SA 66 (SCA) at 78C-D and *Van Zyl and others NNO v Tuner and another* 1998 (2) SA 306 (SCA) para 8.

reflect the fair market value of the property being disposed. The only additional requirement is that the transaction must have been approved in writing by the business rescue practitioner prior to the disposal. It is further submitted that the limitation on the company's power to dispose of property by section 134(1)(a) is equivalent to a moratorium for the objectives of both are to ensure that the financially distressed company is revived and in doing so the rights of all stakeholders are to be considered.

4.8 Consistency with the Constitution

4.8.1 Protection guaranteed by section 25 of the Constitution

The moratorium provided in Chapter 6 has attracted constitutional scrutiny. The moratorium restricts creditors from enforcing their rights against a debtor. The question that arises is: does this infringe the creditor's Constitutional right protected by section 25? Section 25 of the 1996 Constitution provides *inter alia:*

> 25(1) Property–
> No one may be deprived of property except in terms of law of general application, and no law may permit arbitrary deprivation of property.
> Property may be expropriated only in terms of law of general application-
> for a public purpose or in the public interest; and
> subject to compensation, the amount of which and the time and manner of payment of which have either been agreed to by those affected or decided or approved by a court. (4) For the purposes of this section –
> (a) the public interest includes the nation's commitment to land reform, and to reforms to bring about equitable access to all South Africa's natural resources; and
> (b) property is not limited to land.

This section guarantees protection to the holding of property and this protection applies to both natural and juristic persons. Furthermore, property in the context of section 25 does not only include land but also movable property. In the *First National Bank* case[577] the Constitutional Court held that ownership of a corporeal movable was a right clearly at the heart of the constitutional concept of property, both as regards the nature of the right as well as the subject of the right. In other words, the relationship between the two is the main focus of section 25 of the Constitution. Ackermann J explained that "any interference with the use, enjoyment or exploitation of private property involves some deprivation in respect of the person having title or right to or in the property concerned … If the deprivation amounts to an expropriation,

[577] 2002 (4) SA 768 (CC).

then it must pass scrutiny under section 25(2)(a) and make provision for compensation under section 25(2)(b)."[578] Nwafor is of the view that:

> Section 134(1)(c) certainly bears some element of interference with the exercise of the creditor's right of property. Such interference could, however, be justified as being in terms of the law of general application and that it is not arbitrary. Thus, there is no issue on compliance with section 25(1) of the Constitution. A similar conclusion cannot, however, be attained in relation to section 25(2). The contention here is that the provision of section 134(1)(c) of the Companies Act amounts to an expropriation of property to the extent that the creditors are denied of rights (albeit temporarily) over their property in possession of the company under business rescue. The purpose of the expropriation is convincingly settled as being in the public interest or for public purpose. The requirement of section 25(2)(a) of the Constitution is thus satisfied to that extent. But not so with section 25(2)(b) which demands that compensation should be paid to the owners of the expropriated property.[579]

It is submitted that if a company under business rescue is required to pay compensation in terms of section 25(2)(b) this would not be consistent with the objectives of business rescue that is, to provide a breathing space for a company in financial distress. Providing compensation would also disadvantage other creditors in that the provision would create preferential rights.

In *AIB Capital Markets Plc & Anor v Atlantic Computer Systems Plc and Others*[580] the court gave directions as to how the interpretation of a similar provision in section 11(3) of the UK Insolvency Act of 1986 was described by the Court of Appeal as having an expropriating effect to the extent that it precludes the owners of land or goods from exercising their proprietary rights while the company is under administration. The court was, however, persuaded that, among others, the right granted the creditors to apply to the court for leave, in the absence of agreement by the administrator, to exercise their rights over such property, provides sufficient protection.

4.8.2 Equal treatment of surety and principal debtor

The moratorium provided in section 133 protects the principal debtor from legal proceedings that may be instituted by the creditor. The question that arises is; does section 133 protect the surety and if not does it amount to unfair discrimination in terms of section 9 of the Constitution? In *New Port Finance Company (Pty) Ltd v Nedbank,*[581] Tsakiroglou alleged that his fundamental constitutional rights to equality, dignity and property were infringed by section 133 as currently interpreted. The nub of the constitutional attack was that section 133 precludes creditors from instituting

[578] *Ibid* para 49.
[579] Nwafor (note 500 above) 64.
[580] [1990] EWCA Civ 20.
[581] 2016 (4) SA 390 (WCC).

legal proceedings against a company during business rescue proceedings but permits the creditors to bring legal proceedings against a guarantor or a surety of the same company.

The court held that where section 9 of the Constitution is invoked to attack a legislative provision on the ground that it differentiates between people or categories of persons in a manner that amounts to unequal treatment or unfair discrimination, the first enquiry is whether the impugned provision does differentiate between people or categories of people. If it does, then in order not to fall foul of section 9, there must be a rational connection between the differentiation and the legitimate government purpose it is designed to further or achieve. The court held that:

> The main purpose of the moratorium is designed to allow business practitioners, in conjunction with the creditors and other affected parties, to formulate a business rescue plan to achieve the purpose of the process in restructuring the affairs of the company or close corporation. The differentiation between natural persons and juristic persons in section 133 of the Act clearly serves a legitimate government purpose. The criteria applied by the legislature to achieve this differentiation are not arbitrary but serves a particular purpose. There can in any event be no suggestion that the expressed purpose of section 133 of the Act as set out above would find any application insofar as natural persons is concerned.[582]

Fuhrmann and Manko note that this means that although section 133 discriminates against natural persons the discrimination is for a legitimate purpose.[583]

4.9 Duration of moratorium

The moratorium created by Chapter 6 applies only for the duration of the company's business rescue proceedings. The business rescue procedure provided for under Chapter 6 has been designed to last for a period of only three months. Thus during this period, the moratorium restricts creditors from instituting legal proceedings against the company, while the business rescue practitioner investigates the affairs of the company, drafts a business rescue plan and implements that plan. When the moratorium commences and when it ends, will depend on the manner in which business rescue proceedings are commenced or terminated. However, from the provisions of section 150(2)(b)(i) a business rescue plan may make provisions for a moratorium that extends beyond the duration of the business rescue proceedings. For as long as a moratorium is in place section 133(1)(b) permits the courts to grant leave to a person to institute legal proceedings.

4.10 Conclusion

[582] Ibid para 5.
[583] T Fuhrmann and V Manko 'General moratorium on legal proceedings under attack' (2016) Volume 16 Issue 10 *Without Prejudice* 21.

The moratorium provided for by section 133 protects the company from legal proceedings that may be instituted by creditors. It is meant to give a company in distress a grace period, to organise its affairs and operate on a solvent basis. During business rescue the company is allowed to make use of property belonging to a creditor provided that in doing so it is not in contravention of any law. This does not mean that the creditors are totally barred from instituting legal proceedings against the company, they can do so but must obtain the business rescue practitioner's consent or the leave of the court. Furthermore, creditors may also seek payment of outstanding debts from sureties depending on the business rescue plan. Where a plan specifically states that a surety is protected from paying the outstanding debts, the creditor no longer enjoys the right to claim outstanding debts from the surety. Section 133 has received different interpretations by the courts which calls for legislative intervention to attain some level of clarity.

CHAPTER FIVE

5. CONCLUSION AND RECOMMENDATIONS

5.1 Conclusion

The discussions in this work show that the business rescue scheme is aimed at facilitating the revival of financially distressed companies. The rationale behind the scheme is that a company facing temporary setback may be worth more as a going concern than if it is liquidated. The company's assets may be used to resuscitate such company to operate on a solvent basis. Furthermore, business rescue is not only meant to secure payment of debts, by permitting reorganization, the procedure secures jobs and decent return for its owners. In other words, the interests of business rescue are not only confined to that of creditors but also the shareholders, employees and the economy at large. This is in harmony with the idea that an efficient insolvency system is not only aimed at providing procedures for the liquidation of failing companies but also procedures for the rehabilitation of viable enterprises.

The sustainability of business rescue is preserved in its nature. It is a speedy process and this makes the procedure a short lived inconvenience to affected persons. Hence, the Act allows the board of directors to initiate business rescue proceedings where the company is on the verge of collapse as provided in section 129. This approach prevents delays and legal costs that may be involved if the company were to apply to the court. However, to maintain a balance of interests amongst affected persons, section 131 of the Act permits any affected person to apply to court for the commencement of business rescue and also nominate a business rescue practitioner.

Nevertheless, to prevent abuse of process, section 131(4) provides directions for the court when deciding whether or not to approve an application to commence business rescue. The court considers whether the company is financially distressed, or it is just and equitable to do so for financial reasons, and above all if there is a reasonable prospect for rescuing the company. These grounds are intended to cover almost all possible scenarios that may transpire in a modern corporate society.

The success of business rescue does not only depend on the efficiency of the process but also on the competency and expertise of the business rescue practitioner. Thus, the appointment of the business rescue practitioner is based on the person's qualification, experience and the size of the company to be rescued .In section 138 the Act provides three categories of members in the professions that can

be considered for appointment as business rescue practitioners, namely: accountants, lawyers and business experts. However, this does not mean that qualified individuals who are not part of these professions cannot be appointed as business rescue practitioners. Experience is essential to the success of rescue because business rescue involves taking a calculated risk with the good will of the business and the interests of affected persons. Therefore, there is no room for trial and error; it is either the practitioner rehabilitates the company or if this cannot be achieved a better return for creditors should be achieved. Furthermore, this requirement should not be construed to mean only experience in a particular field of study but also to include experience in the business of the company to be rescued.

It is through the resourceful and effective discharge of duties by the business rescue practitioner that the business rescue procedure is sustained. In other words, the day to day decisions made by the business rescue practitioner determine whether a company is going to be rescued or liquidated. The business rescue practitioner is responsible for the management and supervision of the proceedings. He must investigate the affairs of the company, design a business rescue plan and oversee its implementation.

During the investigation of the company's affairs, the business rescue practitioner must take stock of the assets of the company. This will assist in the drafting of the business rescue plan. The Act provides a guideline as to what should be included in the plan in section 150. However, the guidelines are not exhaustive, depending on the circumstances of each case, the business rescue practitioner must add to the plan any relevant facts or material that may be useful in achieving the goals of business rescue. It is not only the business rescue practitioner's effort that will eventuate the rehabilitation of a financially distressed company, there is need for cooperation of the company's management, directors and employees without which failure is possible. Besides ensuring compliance with statutory requirements, cooperation ensures that business rescue is carried-out in a manner that maintains a balance of interests of all stakeholders.

The moratorium provided in terms of section 133 of the Act is one of the cornerstones of business rescue. It is at the core of corporate rescue; it prevents the creditors from instituting a legitimate claim while creating room for the debtor to reorganize its business. In an attempt to achieve this end, the whole process takes into cognizance the rights and interests of stakeholders by imposing exceptions to the moratorium. An affected person may institute legal proceedings against a

company under business rescue after obtaining consent from the business rescue practitioner or leave of the court. This provision is intended to allow all stakeholders with claims that fall within the scope of the rescue process as contemplated by Chapter 6 to have access to the courts. In other words, although moratorium is intended to stay legal proceedings by affected persons, the exercise of this right is not without limit.

5.2 Recommendations

This research reveals that business rescue procedure provided in Chapter 6 of the Companies Act is far from perfect. There are grey areas that need to be visited by the legislature. The following are some of the possible solutions that can be adopted;

5.2.1 Business rescue scheme

External Companies

The current interpretation suggests that external companies do not fall within the scope of companies that may be rescued in terms of the Act. The interpretation of the term 'juristic person' should be objective rather than subjective. It is therefore submitted that since external companies also contribute to the economy, there is need to enquire as to how such companies can be rescued because the main objective of business rescue is to resuscitate companies that are economically viable.

The meaning of insolvency

The term "insolvency" is not defined in the Act. It is recommended that the legislature should provide guidelines as to what is the meaning of insolvency in the context of business rescue. It may be stated that insolvency as contemplated in business rescue is the period at which a company is not yet insolvent as a result of a temporary financial setback but its prospects of rehabilitation fairly estimated are higher than its prospects of insolvency.

The purpose of business rescue

The Act provides that the main objective of business rescue is to revive financially distressed companies and where this cannot be achieved, at least achieve a better return for creditors. The legislature needs to clarify whether one can institute business rescue based on the second ground and if so what are the requirements to be met.

Initiating business rescue

It is recommended that a company's memorandum of incorporation should not restrict the powers of the directors to conclude a resolution to commence business rescue. A restriction would be contrary to section 15 (a) and (b) of the Act which states that the company's MOI should be in line with the Act.

5.2.2 Business rescue practitioner

Appointment of a firm

The current provisions in Chapter 6 do not accommodate the appointment of a juristic person as a business rescue practitioner. Nonetheless, considering the duties and responsibilities of a business rescue practitioner, it is recommended that the legislature should make provisions for the appointment of a firm as a business rescue practitioner.

- Rehabilitating a company as a firm increases collaboration and allows brainstorming. As a result, more ideas are developed and productivity improves.
- Business rescue requires one to be an expert in law, accounting and business management; this may be achieved by very few individuals. However, a firm can employ experts in any field of study which would increase the chances of rescuing a company.
- Liability; a firm is able to defray any liability incurred without facing liquidation. Whereas individuals may be declared bankrupt putting the company under rescue in danger of liquidation.
- Allowing firms to operate as business rescue practitioners would also make it easy for the Companies Commission to monitor who is licensed and who is not by imposing penalties on firms that employ an individual who is prohibited by the Court or any law from practicing. It is easier to monitor firms than individuals.

Before a business rescue practitioner is appointment

Where business rescue proceedings are initiated by the board of directors, the board is required to appoint a business rescue practitioner. The company remains under the management of the board for a period of five days in terms of section 129(3). There is need to impose restrictions on the powers of the directors during this period

because moratorium would have already come into effect meaning that creditors cannot institute legal proceedings against the company.

The situation seems to be the same if an affected person applies to court for commencement of business rescue. Before the application is approved, there exists a gap that can be used by creditors, who may institute proceedings against the company since the moratorium applies only after an order for business rescue has been issued. It is therefore recommended that the legislature includes an interim moratorium in the Act. The interim moratorium would apply automatically upon the application to the court for an order to commence business rescue proceedings.

Requirement for security

The office of the business rescue practitioner is an office of great responsibility. It determines whether a company will be liquidated or be rehabilitated. There is, therefore, need to require business rescue practitioners to furnish security for due performance of mandate.

One Regulatory Board

The Act provides that business rescue practitioners may be appointed from different already existing professions. There are no provisions that require the regulatory boards of these professions to confirm the status of the individual. It is suggested that a board of business rescue practitioners may be put in place and its main responsibilities would be;

- to maintain and enhance the professional standards, prestige and standing of the profession;
- to promote the knowledge and practices of business rescue;
- to oversee the proper discharge of duties by business rescue practitioners.

The recommendations in this work are not exhaustive. Areas that require improvement will continue to emerge as future researches are conducted on the practical implications of the various provisions contained in Chapter 6 of the Companies Act based on the experiences on the relevant stakeholders.

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