# A CRITICAL DISCUSSION OF THE AFFECTED PARTIES IN BUSINESS RESCUE PROCEEDINGS

**BY**

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DECLARATION

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ABSTRACT

Section 7(k) of the Companies Act 71 of 2008 provides for the rescue and recovery of financially distressed companies while balancing the rights of the affected parties namely the shareholders, creditors and employees. While the approach under judicial management focused on the creditors without considering the prospects of recovery[1], the new business rescue regime seems to have a more inclusive approach. The new regime protects a wider range of interests and this is visible from the definition of affected persons which includes employees, creditors and shareholders.[2]

The affected persons are vital role players in the business rescue proceedings and can have a significant impact as to whether business rescue is successful or not. If the affected parties do not understand their rights and processes involved, it could cause unnecessary delays which could prove to be detrimental to rescue proceedings. This may lead to liquidation due to a lack of understanding of the purpose of business rescue and liquidation of a company means that the company would cease to exist which would have a domino effect on the economy as the unemployment rate would escalate rapidly in a strained economy. Section 7(e) of the Companies Act clearly states that the purpose of the Act is to enhance the economic welfare of the South African economy. The success of business rescue means retained jobs, satisfied creditors and shareholders and it is therefore imperative that the key role players in business rescue understand their rights, roles and responsibilities. This dissertation seeks to set out the roles and responsibilities of each class of affected person and examine whether there is adequate protection or an over protection of certain rights in some instances.

1 R S Bradstreet 'Business rescue proves to be creditor-friendly: C J Claassen J's analysis of the new business rescue procedure in *Oakdene, Square Properties*' (2013) 130 *SALJ* 44–52 at 44.

2 S 128(1)(*a*) of Act 71 of 2008.

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# CHAPTER 1

## I INTRODUCTION

'*Failure is simply the opportunity to begin again, this time more intelligently*.'

Henry Ford, Founder of the Ford Motor company.

## II BACKGROUND

The concept of business rescue was introduced in 2011 and replaced judicial management which was provided for in the Companies Act 61 of 1973 (hereinafter 'the 1973 Act'). The concept of judicial management was thought to be 'conservative' as highlighted in the case of *Le roux Hotel Management*[1] and found that there is limited scope for judicial management in our jurisprudence and the law requires development of our business rescue mechanism.[2] This progression would require new legislation as the court could not 'regenerate a system which has barely worked since its initiation'[3] and was sought to be abolished on the basis that it had been abused and had low success rates.[4]

In the past, the procedure of judicial management has failed due to various reasons. The reasons include, inter alia, that judicial management was selectively granted under special circumstances. This special treatment implied that judicial management could not be utilised as a method detached from financial difficulties.[5] Furthermore, this route was reserved for larger companies, consequently excluding smaller companies from utilising this rescue mechanism. A major consideration under judicial management was the interests of creditors, while business rescue seeks to adopt a more inclusive approach by considering the rights of the affected parties inclusive of creditors and balancing their interests.

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1 *Le Roux Hotel Management (Pty) Ltd and Another v E Rand (Pty) Ltd (FBC Fidelity Bank Ltd (under Curatorship), intervening* 2001 (2) SA 727 (CPD) ('*Le Roux Hotel*').

2 Ibid para 6.

3 A Loubser 'Judicial Management as a Business Rescue Procedure in South African Corporate Law' (2004) 16 *SA Mercantile Law Journal* 137–163 at 140.

4 M L Benade 'A survey of the main report of the commission of enquiry into the Companies Act' (1970) 3 *Comparative and International Law Journal of Southern Africa* 227–309 at 307.

5 J J Henning 'Judicial management and corporate rescues in South Africa' (1992) 17 *Journal for Juridical Science* 90–105 at 93.

When comparing judicial management and business rescue, the obvious reasons for its failure is highlighted. In the past, judicial management placed a heavy burden on its applicants to prove reasonable probability, and this is regarded as one if its shortcomings.[6]

Business rescue is provided for in Chapter 6 of the Companies Act 71 of 2008 ('the Companies Act') and provides a mechanism to rescue and rehabilitate a 'financially distressed' company.[7] According to the Act, a company is financially distressed if it appears to be reasonably unlikely to be able to pay all of its debts as they become due and payable within the immediately ensuing six months,[8] or a company that appears to be reasonably likely to become insolvent within the immediately ensuing six months.[9]

According to section 128(1)(*b*) of the Companies Act, the process of business rescue provides for the following:

> '(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 maximises the likelihood of the company continuing in existence on a solvent basis or, if it is not possible for the company to so continue in existence, results in a better return for the company's creditors or shareholders than would result from the immediate liquidation of the company'.[10]

Business rescue can commence in one of two ways, namely, by means of section 129 of the Companies Act, where a resolution is passed by the Board of directors, or where an affected person can apply for a court order in terms of section 131 of the Companies Act. An 'affected person' is defined in terms of section 128(1)(*a*) of the Companies Act as:

> '(i) a shareholder or creditor of the company;
>
> (ii) any registered trade union representing employees of the company; and

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6 Loubser op cit note 3 at 144.
7 S 128(1)(*b*).
8 S 128 (1)(*f*)(i) of the Companies Act.
9 S 128 (1)(*f*)(ii) of the Companies Act.
10 S 128(1)(*b*)(i)–(iii) of the Companies Act.

(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.'

There is a clear indication that the new Act did attempt to improve the new rescue regime by including shareholders and employees as affected persons and affording them rights to participate in the rescue proceedings.

Employees are afforded protection in terms of section 136 of the Companies Act. While the company continues operations whilst under the supervision of the business rescue practitioner, the employee's contracts would be unchanged and would retain their jobs. The rights of employees are enshrined in the Constitution,[11] as well as in the Labour Relations Act.[12] It has been suggested that the overprotection of employee rights will be to detriment of the employees.[13] Employees and creditors have the right to form committees and are consulted regarding the business rescue plan while on the other spectrum, shareholders do not form a committee and are not consulted on the business rescue plan.[14]

Employees become creditors if the company owes an employee money with regard to outstanding remuneration which creates an overlap of an 'affected person'.[15] Employees are now protected by virtue of being an affected person, employee and creditor.

Previously, under judicial management, the creditors' interests were preferent. However, business rescue allows for a more debtor friendly approach as the new business rescue regime tries to ensure that wider interests are protected.[16] While the new business rescue regime provides a more inclusive approach, that does not leave creditors without protection which is covered in terms of section 145(1)(a) of the Companies Act. The Companies Act is ensuring that the rights of the affected parties are balanced which is in line with section 7(k) of the Companies Act. This principle was illustrated in *Ziegler South Africa (Pty) Ltd v South African Express Airways SOC Limited*,[17] the court found that it was in the interests of justice and public interest to allow an investigation into the company affairs and draft an appropriate

11 Constitution of the Republic of South Africa, 1996 ('the Constitution').
12 Labour Relations Act 66 of 1995 ('LRA').
13 T Joubert, S van Eck & D Burdette 'Impact of labour law on South Africa's new corporate rescue mechanism' (2011) 27(1) *International Journal of Comparative Labour Law and Industrial Relations* 65.
14 D L Lusinga & K J Fairhurst 'Role of stakeholders in business rescue' (2020) 51 *South African Journal of Business Management* 1–11 at 2.
15 See s 144(2) of the Companies Act.
16 Bradstreet op cit note 1 at 44.
17 2020 (ZAGPJHC) 29 ('*Ziegler*').

rescue plan.[18] Liquidation would result in a forced sale of assets which would result in the assets receiving less than market value and the amount of job losses would be significant which would cause hardships for the families.[19]

## III PURPOSE STATEMENT

The purpose of this study is to critically discuss the affected parties in business rescue proceedings. This study focuses on creditors and examines the manner in which the rights of creditors are affected. The employees' rights are protected in terms of the Companies Act, the LRA and the Constitution. In this research I will examine the manner in which business rescue affects employment contracts and lease agreements, as well as the extent to which the moratorium protects the company in financial distress.

## IV RESEARCH QUESTIONS

In this research, I consider at the following questions in order to enable me to determine how each of the affected parties are affected and to what extent they are affected.

(a) Who is an affected party as defined by the Act?

(b) Who is an employee?

(c) What are the rights of employees?

(d) How are the rights of employees affected?

(e) How are these rights protected?

(f) What are the obligations placed on each party during business rescue?

(g) How are the rights and obligations handled in labour law, corporate law, and contractual law?

(h) Who is recognised as a creditor in business rescue?

(i) What are the rights of the creditor?

(j) How are these rights protected?

(k) Are their interests adequately protected?

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[18] Ibid at 62.
[19] Ibid at 59.

(l) What are obligations placed on the creditor and company during business rescue proceedings?

## V RESEARCH METHODOLOGY

The method of my research is desktop based. In this research I rely on sources such as case law, legislation, journal articles, and textbooks. My research is doctrinal and focuses on the issue of business rescue and specifically the affected parties.

## VI CHAPTER OUTLINE

Chapter 1: History of judicial management and the transition to business rescue

Chapter 2: Commencement of Business rescue and the affected parties

Chapter 3: Creditors as affected parties and the rights of creditors and the protection granted in terms of the Companies Act

Chapter 4: Shareholders and their roles, responsibilities and obligations under business rescue

Chapter 5: Employees as affected parties and the rights of employees and the protection afforded in terms of the Labour Relations Act and the Companies Act

Chapter 6: The effect of business rescue on property owners

Chapter 7: Conclusion

## VII LIMITATIONS OF THE STUDY

This dissertation is restricted to a discussion regarding the affected parties in business rescue proceedings, namely: the creditors; shareholders; and employees. I also discuss the extent to which the practice of business rescue, and especially the business rescue practitioner, affects the relevant parties. The business rescue practitioner is vested with a wide range of powers which are set out in section 140. The business rescue practitioner has the power to suspend certain contracts which could affect other parties such as a property owner.

## VIII RATIONALE FOR THIS STUDY

Employees, creditors, and shareholders are important role players in business rescue proceedings. The previous position was that the creditors' interests were important and played

an instrumental role in deciding whether or not a company could be placed under judicial management.[20] However, Chapter 6 of the Companies Act states that business rescue incorporates employees and trade unions (representing employees) and not just the creditors. Employees influence the court's decision to grant an application of business rescue.[21]

Globally, there is an increase in the number of businesses that enter business rescue proceedings. In the South African context, against the backdrop of its current economic position, it is inevitable that more businesses will become financially distressed. Ultimately, business rescue aims to rescue a company whilst seeking to balance the rights and interests of the creditors, shareholders and employees. Accordingly, I examine the relevant affected parties and discuss the role that each party plays in business rescue proceedings.

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20 *Le Roux* Hotel supra note 1 para 6.

21 *National Union of Metalworkers of South Africa (NUMSA) obo Members and Another v South African Airways (SOC) Ltd and Others* 2020 (6) BLLR 588 (LC) ('*NUMSA*').

CHAPTER 2

COMMENCEMENT OF BUSINESS RESCUE

## I BUSINESS RESCUE UNDER THE COMPANIES ACT 2008

Business rescue under the Companies Act of 2008 can be seen as more inclusive than judicial management. Business rescue can be commenced by the directors, creditors, shareholders, employees, and trade unions (representing employees).[24] Section 7 of the Companies Act illustrates that the new rescue regime is more accessible and does not preclude small businesses from accessing rescue mechanisms. The new regime aims to provide a balance by giving effect to the purpose of this Act which is to:

> '[P]rovide for the efficient rescue and recovery of financially distressed companies, in a manner that balances the rights and interests of all relevant stakeholders.'[25]

Section 7(k) of the Companies Act indicates that the intention of the legislature is to provide a rescue regime that encompasses a balanced approach when dealing with the affected persons. Accordingly, the rescue regime in the South African context should be aimed at protecting employment, especially considering the fact that South Africa harbours a developing economy.[26]

A company is placed under business rescue in the following ways:

(a) When a company is placed under voluntary business rescue by the board of directors;[27]

(b) When an affected person makes an application under section 131,[28] provided that the company has not been placed under business rescue in terms of section 129. An affected person is discussed in detail later in this dissertation.

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24 See s 129 of the Companies Act.
25 See s 7(k) of the Companies Act.
26 A Loubser 'Business rescue in South Africa: A procedure in search of a home?' (2007) *40 Comparative and International Law Journal of Southern Africa* 152–171 at 152.
27 See s 129(2)(*a)* of the Companies Act.
28 See s 131 of the Companies Act.

*(a) Commencement by way of resolution*

A board of directors ('BOD') may pass a resolution by majority vote that the company should commence business rescue proceedings and that the company be placed under supervision in terms of section 129 of the Companies Act.[29] The board must reasonably believe that the company is financially distressed and that a reasonable prospect exists in rescuing the company.[30] This allows a director to seek help at an early stage. A company will be placed under business rescue, provided that: the company is financially distressed; the company has failed to meet its financial obligations (which includes a contractual obligation or an employment obligation); and it is just and equitable to do so.

The term 'financially distressed' means that a company will be reasonably unlikely to be able to pay their debts as they become due within the next six months or the company will become insolvent within the next six months.[31]

Financially distressed is determined by means or a cash flow solvency test. This is applied to determine whether the company is unable to pay its debts when they become due. The second test refers to the balance sheet test, which determines if the value of the company's liabilities exceeds the company's assets.

The last requirement is that there must a reasonable prospect for rescuing the company.[32] The directors must have reasonable grounds for believing that the business can be rescued. To rescue a company, it means that one of the goals of business rescue must be achieved. Business rescue will either ensure that the business can return to a solvent state or that the process of business rescue will provide better returns for creditors.

The notion that business rescue is for 'terminally ill or chronically ill corporations' or for 'ailing companies' must be discarded.[33] This is based on the belief that business rescue is aimed at remedying the company's situation before insolvency. If business rescue is sought before the company is insolvent, it serves as a preventative measure (to insolvency), as opposed to a cure (for an ailing company).

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29 See s 66(1) of the Companies Act.
30 See s 131(4) of the Companies Act.
31 See s 131(4)(*a*) of the Companies Act.
32 See s 129(1)(*b*) of the Companies Act.
33 *Welman v Marcelle Props 193 CC and Another* 2012 (ZAGPJHC) 32 at 28.

Generally, the directors and certain stakeholders are aware of the company's financial status. It is for this reason that business rescue allows a director to seek help at an early stage. This is, however, dependent on the director's ability to identify the company's need for rescuing. Ideally, business rescue should be used as a rescue mechanism and should not be utilised as a method for evading creditor-liability or liquidation.[34]

The directors have no duty to consult the shareholders during this stage and the purpose thereof is to prevent unnecessary delays and costs.[35] The resolution must include a sworn statement of the facts relevant to the grounds on which the board resolution was founded.[36] The company is then required to file a notice of appointment and publish this notice to each of the affected persons. The company must publish a notice of the resolution to every affected person within five business days.

If the directors have reasonable grounds to believe that the company is financially distressed and the board does not adopt a resolution to commence business rescue then they must give reasons to the affected parties for not adopting the resolution.[37] The affected persons can apply to court to commence business rescue proceedings as discussed below.

*(b) Commencement by a court order*

An affected person may make an application to court in order to place the company under supervision. The requirements for this application are extensive as the applicants must satisfy the requirements as contemplated under section 128 of the Companies Act.38 The applicant must satisfy the requirements that the company is financially distressed; that the company has failed to pay over an amount in terms of an obligation (inclusive of a contract or employment related matters); or it is just and equitable to do so for financial reasons; and that there is a reasonable prospect of rescuing a company.[39] The applicant must also notify the affected persons.

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34 J Bell & J Barnett 'South Africa: Business Rescue: Open for abuse?' *Baker Mckenzie* 2017, available at https://restructuring.bakermckenzie.com/2017/01/11/south-africa-business-rescue-open-for-abuse accessed, 20 January 2021.

35 F H I Cassim et al *Contemporary Company Law* 2 ed (2012) at 886.

36 See s 129(3*)(a)* of the Companies Act.

37 See s 129(7) of the Companies Act.

38 See A Loubser 'The Role of Shareholders during Corporate Rescue Proceedings: Always on the outside Looking in' (2008) 20 *South African Mercantile Law Journal* 372–390 at 381.

39 See ss 131(4)(*a*)(i)-(iii) of the Companies Act.

In this part, I investigate the role that employees, creditors, and shareholders play in the decision to grant an application for business rescue proceedings for the purposes of this dissertation. The requirement of 'financial distress' postures a challenge for the affected parties as the affected parties may not have knowledge of the company's financial affairs, rendering this requirement as difficult to prove.[40]

Even if the applicants are able to obtain access to the relevant records, there is no guarantee that it would be a true reflection of the company's affairs. The requirement applicable to the affected parties (and their considerations) are determined with reference to the requirement of 'just and equitable for financial reasons and whether a reasonable prospect exists'.[41]

Employees who have been employed company for a substantial amount of time would have knowledge of the company's performance, the highs and lows of the business, and possible solutions which should also be taken into consideration. The courts should consider different tests in order to determine whether a 'reasonable prospect' exists, depending on who makes the application, in order to give effect to the Act without disadvantaging any employee.[42]

The shift in the attitude towards business rescue was evident in the case of *Oakdene Square Properties v Farm Bothasfontein*.[43] In this case, the shift from a debtor-friendly to a creditor-friendly approach is evident. According to this case, business rescue should aim to achieve one of the two goals, namely: temporary supervision; and a rescue plan (aimed at restructuring the company, enabling it continue operations or yield better returns for the creditors, as opposed to the company being liquidated).[44]

In this case, the High Court initially considered the issue of interpreting 'just and equitable to do so for financial reasons' and found that the phrase is vague.[45] Although the application to commence business rescue was not granted (as there were no employees to

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40 R S Bradstreet, M Pretorius & P Mindlin 'The wolf in sheep's clothing – when debtor-friendly is creditor friendly: South Africa's business rescue and alternatives learned from United State Chapter 11' (2015) 2 Journal of Corporate and Commercial Law and Practice 1–41 at 19.

41 See s 131(4)(*a*)(iii) of the Companies Act.

42 See *Employees of Solar Spectrum Trading 83 (Pty) Ltd v Afgri Operations Ltd and Solar Spectrum Trading 83* (Pty) Ltd 2012 (ZAGPPHC) 359 ('*Solar Spectrum*') para 18.

43 *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd* 2012 (3) SA 273 (GSJ) ('*Oakdene*'). The facts of this case are discussed in more detail in the following paragraphs.

44 Ibid para 23; see also *A G Petzetakis 14 International Holdings Ltd v Petzetakis Africa (Pty)* 2012 (5) All SA 515 (GSJ) ('*A G Petzetakis*') para 11.

45 Ibid *Oakdene* supra note 43 para 17.

consider, and no real business was conducted) this case illustrates that the courts are considering a wider range of interests whilst balancing the rights of creditors.

On appeal, the Supreme Court of Appeal ('SCA') sought to provide the guidelines on the requirement of 'reasonable prospect' and found that the applicant must prove that a prospect exists, and it must be based on reasonable grounds.[46] Brand AJ remarked that it would not be practical or prudent to require the applicant to prove a 'reasonable prospect' in a specific way.[47]

Although there is no specific set of requirements, an applicant must provide a substantial measure of detail.[48] The Court agreed with the judgment of *Propspec Investments v Pacific Coasts Investments 97 Ltd*,[49] where the Court ruled that an applicant must prove that a factual foundation exists for a reasonable prospect.[50] However, the checklist-approach as adopted in Southern Palace investments[51] is not practical enough in order to prove a reasonable prospect. The requirements of the checklist approach cannot be proven when the application is made for an order of business rescue.

This judgment by Eloff AJ has been 'criticised for placing the benchmark too high.'[52] It would be improper to expect employees or certain classes of shareholders to prove to the courts the cause of the failure. A failure to give consideration to the applicant and the information at their disposal may have the effect of importing a requirement that legislature did not intend.[53] This would place a heavy burden on the affected parties and therefore making business rescue inaccessible.

It is evident that 'employees' are included in the definition of 'affected persons'[54] which has been deemed to be a remarkable feature of the rescue regime.[55] Due to the fact that employees being able to initiate business rescue proceedings, it becomes obvious that employees are considered by the courts when granting an order to commence business rescue

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46 *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd* 2013 (3) All SA 303 (SCA) ('*Oakdene* SCA') para 29.

47 Ibid para 30.

48 Ibid.

49 *Propspec Investments v Pacific Coasts Investments* 97 Ltd 2013 (1) SA 542 (FB) ('*Propspec Investments*').

50 Ibid at 11.

51 *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 Ltd* 2012 (2) SA 423 (WCC) ('*Southern Palace*').

52 *Solar spectrum* supra note 42 at para 17; see also E P Joubert 'Reasonable Possibility versus Reasonable Prospect: Did Business Rescue Succeed in Creating a Better Test than Judicial Management' 2013 (76) THRHR 550–563 at 556.

53 Ibid *Solar Spectrum* at 19.

54 See s 128(1*)(a)(*iii) of the Companies Act.

55 Bradstreet, Pretorius & Mindlin op cit note 40.

proceedings. The case *Employees of Solar Spectrum Trading 83 (Pty) Ltd v Afgri Operations Ltd and Solar Spectrum Trading 83 (Pty)* was the first case where the employees applied for an order to commence business rescue. The case indicated the change of our rescue culture and that creditors no longer have an absolute right to liquidate proceedings.[56] The applicant is not required to produce a business rescue plan and requiring such from the applicant would import a requirement not envisaged in the Act.[57] After the Court considered the rights of the employees and creditors, it accordingly granted an order to commence business rescue proceedings.[58] The farm was consequently in a position to enter the retail market and receive better prices for their crops. In order to prevent job losses and housing issues, they illustrated their willingness to contribute to the rescue proceedings.[59]

In the past, judicial management favoured the creditor and has been a crucial factor used to determine whether or not a company can succeed under business rescue proceedings and was granted only under exceptional circumstances, as liquidation was the preferred method.[60] Business rescue under Chapter 6 sought to be more inclusive, as it tried to balance the rights of the affected parties which promotes section 7(k) of the Companies Act.

Section 131(3) of the Companies Act, makes provisions for affected persons to participate in the hearing of the application. In both instances, whether it is by way of a resolution passed by the BOD, or by way of an application made by an affected person, both processes are managed by the business rescue practitioner who is appointed to supervise and manage the affairs of the company. The business rescue practitioner will determine whether the business has a reasonable prospect of being rescued.[61]

## II LEGAL CONSEQUENCES OF A BUSINESS RESCUE ORDER

When a business is under business rescue, there are two consequences that arise from this, namely: first, there is a moratorium placed on legal proceedings of the company; and secondly the business is managed by the business rescue practitioner.

56 *Solar Spectrum* supra note 42.
57 Ibid para 19.
58 Ibid para 33(e).
59 Ibid paras 33(a)–(b).
60 *Southern Palace* supra note 51 para 21.
61 E Levenstein 'Help is at Hand' (2008) 8(10) *Without Prejudice* 12–14 at 12.

A moratorium means that there is a stay (or freeze) on legal proceedings, and on its assets and property.[62] The moratorium is effective until the business rescue proceedings end by means of a court order or when the court converts business rescue proceedings into liquidation proceedings.[63] Creditors cannot enforce their rights while the company is under business rescue and the moratorium applies to all creditors. The reorganisation of a financially distressed company would not be achievable without a moratorium[64] as the moratorium provides protection against creditors who wish to institute action against the company.

A moratorium on legal proceedings is protected in terms of the Act.[65] Execution and enforcement may not take place and if rescue proceedings have begun, the process must be frozen until the written consent of the business rescue practitioner is obtained.[66] The moratorium does not prohibit the exercise of legal proceedings, it just subjects the legal proceedings to written consent of the business rescue practitioner or with leave of the court.[67]

In *Booysen v Jonkheer Boerewynmakery (Pty) Ltd*[68] the court examined conflicting judgments which dealt with the moratorium. In this case, the employee of the company instituted a claim in respect of unpaid remuneration. In terms of the business rescue plan, the payment was a preferent claim. On the one hand, the court found that a separate application must be made.[69] While on the other hand, the application was allowed in the main application to set aside a business rescue order.[70]

In *Moodley v On Digital Media (Pty) Ltd*[71] the applicant who was a minority shareholder seeks leave under section 133(1). The applicant wished to proceed with action against the company and business rescue practitioner as certain transactions were not in accordance with the business rescue plan. The court found that this constituted legal proceedings against the business rescue practitioner and the company in business rescue in connection with the rescue plan. This action is not against the company or its property. The

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62 Cassim et al op cit note 35 at 878.
63 See s 137(1)(*d*) of the Companies Act.
64 Cassim et al op cit note 35 at 879.
65 See s 133(1)(*a*)–(*b*) of the Companies Act.
66 Cassim et al op cit note 35 at 880.
67 See s 133 of the Companies Act.
68 2017 (4) SA 51 (WCC) ('*Booysen*').
69 Ibid para 54; see also *Msunduzi Municipality v Uphill Trading 14 (Pty) Ltd* 2015 (JOL) 33101 para 8; *Elias Mechanicos Building & Civil Engineering Contractors (Pty) Limited v Stedone Developments (Pty) Limited* 2015 (4) SA 485 (KZD) para 12.
70 *African Banking Corporation of Botswana v Kariba Furniture Manufacturers (Pty) Ltd* 2013 (6) SA 471 (GNP) ('*Kariba*') para 6.
71 2014 (6) SA 279 (GJ) ('*Moodley*') para 10.

held that it would be wrong to require every matter seek leave in terms of section 133(1). The moratorium is regarded as a 'breathing space' for companies under business rescue.[72]

Another important consequence of a business rescue order is that a business rescue practitioner obtains control of the business. In this case, it meant that that the directors had to relinquish their roles in order to allow the business rescue practitioner to take over the control of the business. This was in itself an issue, as the business rescue practitioner would not understand the model and dynamics of the business. Generally, the business rescue practitioner is empowered to investigate the company affairs and report any illicit affairs. The practitioner is empowered to suspend any contract or cancel any obligation.

## III CONCLUSION

Under the current rescue regime, the intention of legislature is clearly indicated in the purpose of the Act. It is aimed at providing a rescue regime that has a balanced approach when dealing with the affected persons. The departure from the traditional view of business rescue is evident upon observing the courts' interpretation of the 'reasonable prospect' requirement. This departure has led to the adoption of a holistic and balanced approach, which considers a wider range of interest.

In the past, judicial management relied heavily on court proceedings, which made it expensive for smaller businesses.[73] Similarly, in the past judicial management did not consider the rights of all the affected parties and mainly considered the creditors' interest. It was treated as an extraordinary circumstance because a creditor was entitled to liquidate a company to recover payment.[74]

It must be reiterated that rescuing the company is also an aim of business rescue. Our courts are willing to consider a range of factors (such as the impact of business rescue on employees and shareholders, as illustrated in *Solar Spectrum*) which is in the line with purposes as outlined in section 7(k) of the Companies Act.

The case of *Oakdene* produced important guidelines to prove the requirement of 'reasonable prospect' in which the onus of proof rests on the applicant. This case highlights the

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72 *Cloete Murray v FirstRand Bank Ltd t/a Wesbank* 2015 (3) SA 438 (SCA) ('*Cloete Murray*') para 34.

73 P Kloppers 'Judicial Management Reform – Steps to Initiate a Business Rescue' *South African Mercantile Law Journal* (2001) 13(3) 358–378 at 370.

74 Kloppers op cit note 73 at 377.

impracticality and imprudence of following a required list of requirements in proving reasonable prospect.[75]

Directors are still involved under the new rescue regime. Directors are under the supervision of the business rescue practitioner and there is a balancing of interests when determining whether or not to grant an order to commence business rescue proceedings.[76] In conclusion, directors should be cognisant of when applying to place a business under business rescue. Furthermore, the process should not be abused and used as a means to avoid paying certain creditors or to avoid liquidation proceedings.

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75 *Oakdene* supra note 43.

76 J Rushworth 'A critical analysis of the business rescue regime in the Companies Act 71 of 2008' (2010) *Acta Juridica* 375–410 at 376.

CHAPTER 3

THE ROLE OF CREDITORS IN BUSINSS RESCUE PROCEEDINGS

## I INTRODUCTION

Traditionally liquidation was the preferred avenue to follow when a company was under financial distress and this process is aimed to extract money in order to settle claims[77] and if judicial management was an option then a stigma was attached as it was an extra-ordinary remedy which infringed the rights of creditors.[78]

However, Chapter 6 of the Companies Act provides an alternative to liquidation proceedings to creditors.[79] It has been noted that business rescue provides a holistic approach and seeks to protect more than just the creditor but takes into account the rights of the affected parties and find a balance.[80] In addition, business rescue considers the business and assists to 'get back on its feet', rather than liquidating it (as would have been the case under judicial management).[81]

Creditors are regarded as 'affected persons'[82] and have the right to initiate business rescue proceedings if they find it in their best interest to do so and they will be protected in terms of Chapter 6.[83] Chapter 6 appears to be flexible by allowing a creditor to have some control over a financially distressed company.[84] Creditors can also form a 'creditors' committee' with which the business rescue practitioner will liaise, regarding the business rescue proceedings. The creditors will determine whether or not to appoint a creditors' committee.[85]

It is also important to note that employees can also become creditors which is explored below in more detail. Creditors have the right to participate in court proceedings and are also entitled to notice any meetings and court proceedings relating to the procedure.[86] The incorporation of these rights indicate the shift from creditor orientated approach in that the

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77 R Bradstreet 'The new business rescue: Will creditors sink or swim' (2011) 128 *SALJ* 352–380 at 352.
78 Joubert op cit note 52 at 551.
79 Ibid at 353.
80 Bradstreet op cit note 1 at 44.
81 Ibid.
82 See s 128(1)*(i)* of the Companies Act.
83 Bradstreet op cit note 77 at 365.
84 Ibid at 366.
85 See s 147(1)(*a*).
86 See s 145(a) of the Companies Act.

creditors rights will prevail in judicial management to a more balanced approach which still considering their rights as affected persons.

This approach extends into allowing creditors the right to: vote; amend; approve; or reject, the business rescue plan. If the plan is rejected, creditors have the right to propose an alternative plan.[87] A creditors' committee have the right to receive and consider reports regarding the business rescue plan and the business rescue practitioner is required to provide the committee with information regarding the exercise of his or her functions.[88] The creditors' committee must consist of independent creditors, which means that the creditor must not be related to the company.

## II THE INTEREST OF CREDITORS IN BUSINESS RESCUE PROCEEDINGS

Chapter 6 of the Companies Act is aimed at rescuing a business, as opposed to the intended liquidation as advocated for by its predecessor. Creditors can find comfort in the fact that their rights are protected under the new dispensation. In pursuit of creditor's- protection, creditors must be notified in the event of a BOD decides not to commence rescue proceedings. This requirement confirms the protection afforded under Chapter 6, as creditors are given the opportunity to commence rescue proceedings.[89]

Section 128 of the Companies Act identifies creditors as affected persons while section 131(4) sets out the requirements that must be established for a court to grant the order of business rescue. Employees who are due money would also fall into the category of a creditor and the application should not become a tool of abuse for wage and salary negotiations[90] as an employee s regarded as a super-preferent creditor whose claims rank higher than that of an ordinary creditor. Section 128(1) sets out inter alia that obtaining a better return for creditors or shareholders than if the company were liquidated is one of the aims of business rescue. The concept of obtaining a better return for creditors or shareholders has been decided on in our courts.[91]

As mentioned in chapter 2, the case of *Oakdene*[92] the adoption of a more inclusive approach. The facts of this case serve as a crucial point of departure in order to understand the

87 See s 145 of the Companies Act
88 Cassim et al op cit note 35 at 902.
89 Bradstreet op cit note 77 at 366.
90 Ibid at 358.
91 See s 128(1)(*b*)(iii) of the Companies Act.
92 *Oakdene* SCA supra note 46.

manner in which our courts interpret the requirement of reasonable prospect. The court had to determine the meaning of rescuing a company and weigh up the interests of the affected parties

In this case, the company, Farm Bothasfontein (Kyalami) (Pty) Ltd, was in default of payments to creditors and attempted to use business rescue proceedings in order to prevent the commencement of liquidation proceedings.[93] In order to facilitate the evasion of creditor liability and liquidation proceedings, the director applied to commence business rescue proceedings. Notably, Nedbank and Imperial each held thirty percent of the shares and were also creditors of the company. The creditors who were also the majority shareholders in the company opposed the application.

Classen J in the high court remarked that business rescue is concerned with the actual business and not the company. Business rescue 'encapsulates a shift' from the creditors interests to the interest of other affected parties such as the skills that employees have that will enable a business to be preserved and ultimately provide better returns for creditors. [94]

When an application is brought before the court in terms of section 131, the applicant would need to prove that a reasonable prospect exists.[95] The company is financially distressed but a reasonable prospect did not exist as there was no business to rescue.[96] There was no reason that the liquidator would be less successful in realizing the assets for the best obtainable price than a business rescue practitioner. [97] The courts when interpreting reasonable prospect will interpret it in line with the purposes outline in section 7(k) of the Act together with the goals of business rescue.

The court did not have to consider the employees in this case but had to consider the interest of the creditors and the interests of the company. The court refused to grant the application to commence rescue proceedings because it would not provide a better outcome for creditors than liquidation proceedings. The court noted that the new rescue procedure looks at a broader range of interests.[98] The court refused the application based on the fact that business rescue would not provide better returns for the creditors. In light of the facts of this case, the court found that there was no business to be rescued, and that in this particular situation, the

93 Ibid para 44.
94 *Oakdene* supra note 43 at 12.
95 Ibid at 13.
96 Ibid at 49.
97 Ibid.
98 Ibid para 12.

creditors' interest should carry more weight, and that the applicants failed to show how business rescue would yield better returns for the creditors.[99]

The matter on appeal once again had to determine the requirement of reasonable prospect and reiterated that rescuing a company means achieving one of the goals under section 128(1). The goal of the business rescue plan must achieve one of the two goals; namely that is, to restore the company to the normal healthy state of solvency. The secondary objective, to provide a better deal for creditors and shareholders than liquidation.[100] The SCA found that reasonable possibility must be based on reasonable grounds that goes beyond speculation. [101] The decision in *Oakdene* supra confirms that creditors are protected under the Companies and while an order of business rescue was not granted given the facts of the case.

During liquidation proceedings the South African Revenue Service ('SARS') enjoys preferent status had the company been liquidated. While SARS is considered a creditor of the company (and is therefore entitled to participate in the rescue proceedings), the Companies Act does not prohibit SARS from enjoying 'preferent status' in respect of a claim.[102] The only reported case where SARS was a creditor, is the case of *Commissioner, South African Revenue Service v Beginsel NO and Others*.[103] In this case, SARS challenged the validity of the decision taken to adopt the rescue plan. SARS claimed that the business rescue practitioners had incorrectly determined SARS' voting interests by giving SARS the same voting status as creditors when they should have preference in terms of section 99 of the Insolvency Act.[104]

SARS claimed it should have been treated as an unsecured creditor as contemplated in terms of section 145(4)(*a*), while other creditors are dealt with under section 145(4)(*b*). The court rejected the idea of SARS being treated as a preferent unsecured creditor. The court found that the wording was clear and unambiguous. SARS did not enjoy the preferent status.

The new procedure confirms the focus-shift from the creditors to the preservation of the business as a whole, which may in turn, ultimately provide better returns for the creditors.[105]

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99 Ibid para 49.
100 Ibid at 25.
101 Oakdene SCA supra note 46 at 29.
102 M Seligson 'The impact of business rescue on tax claims: does SARS enjoy a preference under s 135 of the Companies Act against a company in business-rescue proceedings?' (2014) 5 *Business Tax and Company Law Quarterly* 1–20 at 5.
103 2013 (1) SA 307 (C) ('*Beginsel*').
104 Act 24 of 1936.
105 Bradstreet op cit note 1 at 52.

Creditors also have the right to form a creditors' committee that represents the interests of the creditors, acting independently and in an unbiased manner.[106]

## II THE BUSINESS RESCUE PLAN IN RELATION TO CREDITORS

The business rescue plan is a crucial part as it contains vital information in respect of the affected parties. The business rescue practitioner is tasked with drawing up a business rescue plan that necessitates the successful rescue of the business. The business rescue plan includes, *inter alia*, a list of the assets of all the assets and which assets are held as security by creditors.[107] A complete list of creditors must also be provided, including which creditors qualify as secured, preferent, and concurrent, as well as which creditors have proved their claim.[108]

The amount in terms of dividends must also be disclosed, should the company be liquidated,[109] the duration of the moratorium in the plan;[110] property available to pay creditors claims;[111] preference of the creditors (with regards to how the proceeds will be applied to creditors);[112] and the benefits to the creditors (if the company were to go into liquidation or if the plan was to be adopted).[113] The practitioner must call a meeting with those who have voting interests in order to consider the proposed plan within ten days of the plan's publication.[114]

The business rescue plan must be supported by more than seventy-five percent of the creditors with voting interests, and supported by fifty percent of the independent creditors. Independent creditors are protected as they are also required to approve the plan by a majority vote, and, accordingly there is a double majority requirement.[115]

The Chapter 6 approach has been branded 'non-interventionist' as the courts are less involved in the development of the rescue plan.[116] Involving the courts in the developing-, and implementing stages of the business rescue plan may be regarded as an unnecessary, taxing, and unjustifiable expense.

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106 S 149(1)(c) of the Companies Act.
107 See s 150(2)(*a*)(i).
108 See s 150(2)(*a*)(ii).
109 See s 150(2)(*a*)(iii).
110 See s 150(2)(*b*)(i).
111 See s 150(2)(*b*)(iv).
112 See s 150(2)(*b*)(v).
113 See s 150(2)(*b*)(vi).
114 See s 151(1).
115 Rushworth op cit note 76 at 405.
116 Bradstreet op cit note 77 at 362.

The purpose and aim of restructuring is to enable a company to return to a solvent basis and it would be burdensome if creditors do not vote to approve the business rescue plan without a valid reason. In terms of section 153(1)(*a*) the practitioner may:

> '(i) [S]eek a vote of approval from the holders of voting interests to prepare and publish a revised plan; or
>
> (ii) [A]dvise the meeting that the company will apply to a court to set aside the result of the vote by the holders of voting interests or shareholders, as the case may be, on the grounds that it was inappropriate.'[117]

Section 153 makes provision for steps to be taken in the event where the business rescue plan has been rejected in terms of section 152. The provisions of section 153 should be of last resort[118] and does not apply if no vote was taken.[119] The courts will not set aside a vote just because it is 'inappropriate' but rather because it is reasonable or just to do so in terms of section 153(7) of the Companies Act.

The effect of section 153 was considered in the case of *African Bank Corporation of Botswana v Kariba Furniture Manufacturers*[120] the bank voted against the plan and the shareholders advised the business rescue practitioner that they wanted to use section 153 in order to make an offer for the banks voting interest. Kathree-Setiloane J was of the view that a 'cram-down' process was an important aspect.[121] The process of 'cram-down' meant that a business rescue plan that was adopted, is binding on every creditor, whether that person was present or not, voted in favour of the plan, and whether creditors had proven their claims.[122]

The process of cram-down originated in the US Bankruptcy Code, Bankruptcy reform Act 1978. This forced creditors to accept the business rescue plan even if it is against their wishes.[123] This is to discourage creditors from voting against the business rescue plan hoping that they would get a better return.[124] The 'offeror' must forward a binding offer to buy the

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117 See also ss 152(3)(a); 152(3)(*c*)(ii); 152(3)(*c*)(bb).
118 See P Delport (ed) *Henochsberg on the Companies Act 71 of 2008* at 550.
119 *South African Bank of Athens Ltd v Zennies Fresh Fruit CC* 2018 (3) SA 278 (WCC) para 26.
120 2015 (5) SA 192 (SCA) ('Kariba SCA').
121 Ibid para 6.
122 *Kariba* supra note 70 para 28. See also E Levenstein 'The *Kariba* case – the watering down of the binding offer in South African business rescue proceedings' (2017) 50(2) *De Jure* 241–262 at 248.
123 *Kariba* supra note 70.
124 Ibid.

dissenting creditors shares at the liquidation value and the 'offeree' must be forced to sell at that price.[125]

On appeal, the court held that the offer only creates obligations when it is accepted, meaning that an offer made to a creditor who opposes the business rescue plan would not constitute a binding offer, as in order for the offer to be binding, the offer would need to be accepted.[126] It has been suggested that the court relied too much on the US method of the cram-down approach when interpreting section 153(1)(*b*)(ii).[127]

An offer must comply with the minimum requirements outlined in the law of contract. The bank, in this case, was entitled to know who was making the offer, the details, and the price (or determined value) and how payment would be effected.[128] The words 'binding offer' should be binding on the offeror.[129] The concurring judgment handed down by Leach J stated that if the offer did equate to a contract (as per the court in *African Bank Corporation of Botswana Ltd v Kariba Furniture Manufacturers (Pty) Ltd*)[130] there is no valid contract because at the time of the offer there was no ascertainable price.[131]

However, the court in *D H Brothers Industries (Pty) Ltd and Karl Johannes v Gribnitz*[132] disagreed with the findings in *African Bank Corporation of Botswana Ltd v Kariba Furniture Manufacturers (Pty) Ltd*.[133] In this case, Govern J found that an offer could not be regarded as something that creates a binding obligation. The court remarked that if legislation intended on creating a statutory obligation it would have. Instead, the legislature mentions 'offer', which is made by one party and may be accepted by another. This would amount to a transaction of purchase and sale. If the plan is rejected then the business rescue practitioner is provided with mechanisms to deal with that particular situation and may approach the court to set aside the vote on the basis that it was inappropriate, or vote to amend the plan.

Creditors who vote against the plan cannot approach the court to set aside those who voted in favour of the plan and to acquire their voting interest. The purpose of section 7(k) does

125 Ibid para 32.
126 *Kariba* SCA supra note 120 para 18.
127 Levenstein op cit note 122 at 248.
128 *Kariba* supra note 70 para 20. See also *Absa Bank Limited v Caine, In Re; Absa Bank Limited v Caine* 2014 (ZAFSHC) 46 ('*Caine*') para 35.
129 *Caine* supra note 128 para 37.
130 *Kariba* SCA supra note 120.
131 Ibid para 52.
132 2014 (1) SA 103 (KZP) ('*Gribnitz*').
133 *Kariba* supra note 70.

not support that a business rescue plan should be implemented at all costs. This is why the legislature has included the majority vote of seventy-five percent. The decision in this case means that secured creditors are protected and cannot be deprived of their rights because of a 'binding offer.' Section 153(7) prevents abusive or arbitrary obstruction of the plan.[134]

The 'binding offer' principle is an important aspect for the restructuring of a company and ensures that plans are 'pushed through' by the provisions of section 153(1)(*b*)(ii).[135] Forcing dissenting creditors to sell their voting interests at liquidation value is aligned with section 7(k) of the Companies Act.[136] It is unclear from the wording of section 153(1)(*d*)(ii) whether it is intended to be a forced sale or not.[137] The uncertainty regarding the interpretation is most certainly not favourable to creditors and this uncertainty may also fall victim to abuse of the creditors and open to abuse.[138] Our courts are tasked with interpreting the wording of section 153, which promotes the provisions under section 7(k) of the Act. This provides for the efficient rescue and recovery of a company while balancing the interests of the affected parties.

The words 'binding offer' and section 154(1), read together, create the ability for a plan to become binding on all the creditors.[139] Where creditors who disapprove of the plan and would rather have the company placed in liquidation should be forced to give up their voting interests at liquidation value.[140] Creditors should not be allowed to hold out on creditors who are in favour of the plan and allow the company to collapse into liquidation. Instead, the dissenting creditors must be forced to sell their voting interests to the creditors who support the plan.[141]

## III CONCLUSION

There seems to be a significant shift from the traditional rescue mechanisms to the modern mechanism, which tries to look at the affected parties as a whole. Business rescue does not consider the rights of creditors as a major consideration and liquidate a company rather than enter business rescue proceedings. Creditors are afforded protection under Chapter 6. This

134 *Gribnitz* supra note 132 para 58.
135 Levenstein op cit note 122 at 259.
136 S 7(k) states that one of the purposes of the 2008 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.
137 See Delport op cit note 118.
138 Loubser op cit note _? (38? 26? 3?)
139 Levenstein op cit note 122 at 260.
140 Ibid.
141 Ibid at 261.

protection is clearly visible by ensuring that creditors are notified in the event that directors chose not to commence rescue proceedings if the company is financially distressed.

Creditors can therefore make a decision regarding the rescue of the company and can commence rescue proceedings, provided that they wish to obtain better a better return and not commence rescue proceedings with an ulterior motive in mind.[142] Creditors still play a significant role in the business rescue proceedings and are involved in decisions. While there are benefits to this, it could also pose challenges, as highlighted in the earlier cases.

The business rescue plan is a vital aspect of the actual business rescue procedure and creditors who would rather have the company liquidated than enter business rescue proceedings for reasons such as: 'If I am going down then so must the company', or wanting to be paid out immediately.[143] This would defeat the purposes as outlined in section 7(k) of the Companies Act and would undermine the objectives of business rescue, which is to ultimately enable a company to return to a solvent state. That objective should not be compromised due to creditors not voting in favour of plan without a valid reason.

142 Bradstreet op cit note 77 at 367.
143 Ibid.

CHAPTER 4

# THE ROLE OF SHAREHOLDERS IN BUSINESS RESCUE PROCEEDINGS

## I INTRODUCTION

A 'shareholder' is defined in terms of section 1 of the Act as the holder of a share issued by a company and who is entered as such in the certificated or uncertificated securities register.[144] Shareholders should be aware of their roles and rights during business rescue proceedings because once business rescue is successful, their shares (or the value thereof) will be revived.[145]

Each shareholder is entitled to receive notice of any meetings and is entitled to participate in the meetings, decisions, and court proceedings.[146] A shareholder is one who is a holder of any issued security. If the business rescue plan alters the rights of any holders, the holder is entitled (at the meeting held for this specific class of affected persons), to vote on the business rescue plan (approve or reject).[147]

If the plan is rejected, the holders may propose an alternative plan or offer to acquire the interests of any or all of the creditors, or others who hold securities and who voted against the business rescue plan.[148] Where the business rescue plan has no effect on the shareholders rights, they would be precluded from voting to adopt the business rescue plan.

When consulting the various affected persons, the business rescue practitioner should have the best interest of the company in mind and should not be dictated to by the various stakeholders.[149] This also means that the shareholder does not have any legal control over the business and the interests of creditors and employees are placed higher than that of the shareholders.[150]

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144 See s 1 of the Companies Act.
145 See Loubser op cit note 38 at 372.
146 See s 146 of the Companies Act.
147 Ibid.
148 Ibid.
149 M F Cassim 'South Africa in unfamiliar terrain as national carrier goes into business rescue' available at https://theconversation.com/south-africa-in-unfamiliar-terrain-as-national-carrier-goes-into-business-rescue-128868, accessed on 27 September 2020.
150 Ibid.

## II THE RIGHTS OF THE SHAREHOLDER

The traditional view is that creditors have the most to lose, which is why they play a more active role in the business rescue proceedings, while shareholders have limited liability and the risk they bear is losing their investment if the company becomes insolvent.[151] The purpose of the business rescue plan is to either rescue the business, or provide better returns for the creditors, including the shareholders.[152]

The definition in section 128(1)(*b*) equates the interests of the shareholders to that of the creditors, but in actual fact the shareholders do not play a vital role in business rescue proceedings.[153] The benefits of business rescue as opposed to liquidation is not set out in the rescue plan. The business rescue plan must set out the returns for creditors if the company were placed under liquidation, the returns upon liquidation of the company and a probable dividend.[154] While the Act may equate the creditor and shareholder, it is evident that creditors are given more protection.[155]

A resolution to commence business rescue proceedings can be taken by a BOD and they should notify all the affected persons.[156] The board must notify all affected persons within five days and the failure to do so will result in the resolution being void, and the company will be prevented from filing another business rescue resolution within three months of adopting the previous resolution which has lapsed unless the court grants consent.[157]

The directors must then deliver written notices to the affected persons, stating on which ground they believe the company to be in financial distress and its reasons for not adopting the resolution.[158] The shareholders' role can be seen as limited when compared to the role that creditors play insofar as the business rescue resolution, as the provisions do not require consultation with members.[159]

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151 Loubser op cit note 38 at 373.
152 See s 128(1)(*b*) of the Companies Act.
153 Loubser op cit note 38 at 379.
154 Ibid at 380.
155 Ibid.
156 See s 129(1) of the Companies Act.
157 See s 129(3)(*a)* of the Companies Act.
158 See s 129(7) of the Companies Act.
159 Loubser op cit note 38 at 381.

Shareholders are therefore dependant on the directors.[160] However, although they have no influence, they (like other affected persons) can apply to court to have the resolution set aside on the basis that the company is financially distressed, a reasonable prospect exists that the company can be rescued, or that the company has failed to comply with the provisions set out under section 129.[161] The affected persons must be notified business rescue proceedings and have the right to participate in the meeting.[162]

The shareholder can apply to court to commence business rescue proceedings if no resolution has been adopted by the board.[163] It is suggested that proving the requirement of financial distress would be difficult without the assistance of the directors, as the financial information is not necessarily accessible to members.

Therefore, our courts are not willing to grant an order of business rescue if the 'just and equitable' requirement is not met, and if the application to commence business rescue proceedings is opposed by a creditor.[164] In *Francis Edward Gormley v West City Precinct Properties (Pty) Ltd*[165] Traverso DJP held that a shareholder who brings an application to commence business rescue proceedings must prove a reasonable prospect and not merely put forward generalisations.[166]

In this case, the application is based on the basis that the loan to the bank be suspended for 3-5 years, which would enable the company to pay its creditors with the exception of the bank. The Court found that there needs to be certainty in the commercial world and that rescue proceedings are meant to be a short process. The company can either repay its debt within six months or it cannot. The company in this case cannot pay its debts unless the 3–5 year moratorium is lifted, which fails the 'financially distressed' test.[167]

If the business rescue plan alters the rights of the shareholders, then the business rescue practitioner is required to put the plan to the shareholders.[168] Section 152 read with section 153

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160 See *Automatic Self-Cleansing Filter Syndicate Co Ltd v Cuninghame* 1906 (2) CH 34 (CA). According to this case the members in a general meeting cannot force the BOD to make a business rescue resolution.
161 See s 131 of the Companies Act.
162 See s 131(3) of the Companies Act.
163 Ibid.
164 Loubser op cit note 38 at 383.
165 2012 (ZAWCHC) 33.
166 Ibid para 12.
167 Ibid para 11.
168 See s 152(3)(*c*) of the Companies Act; see also Rushworth op cit note 76 at 388.

requires that the business rescue practitioner holds a meeting with those who hold company securities if the rescue plan alters the rights of the holders.

'Securities' is defined in section 1 of the Act as shares issued and authorised by a profit company. If the rescue plan is rejected by the majority who hold voting interest or holders whose rights may be affected by the rescue plan, the practitioner will seek a vote of approval to prepare and publish a revised plan. Alternatively, the business rescue practitioner can apply to court to set aside the result of the vote by the shareholders.

If the business rescue practitioner fails to take the above steps, the affected persons can: (a) call a vote for approval from the holders of voting interests (requiring the practitioner to prepare and publish a revised plan); (b) apply to court to set aside the result of the vote by those holders with voting interest or shareholders; or (c) make a binding offer to purchase the voting interests of one or more persons who opposed adoption of the business rescue plan (at a value independently and expertly determined, on the request of the practitioner, to be a fair and reasonable estimate of the return to that person, or those persons, if the company were to be liquidated).[169]

In *Moodley v On Digital Media (Pty) Ltd and Others*[170] a minority shareholder of a company under business rescue sought leave to continue with his application against the company and its business rescue practitioner. The shareholder claimed that certain transactions such as: a share buy-back; the issue of new shares; the adoption of a new memorandum of incorporation; and a draft subscription agreement, are not in accordance with the adopted business rescue plan and are in contravention of the Act, and therefore unlawful. The minority shareholder sought to obtain an interdict against the business rescue practitioner to prevent him from implementing the transaction and set aside those transactions that have been implemented.[171]

The rescue plan would be more favourable to as shareholders would receive more dividends than liquidation. The plan also provided for existing shareholders to remain with restructured equity interests in the company and for the preservation of jobs and the creation of job opportunities. Liquidation will be severely prejudicial to the company and its affected parties, as there would be two-hundred job losses and a loss of one-hundred-and-fifty

169 See s 153(1)(*a*)(ii) of the Companies Act.
170 *Moodley* supra note 71.
171 Ibid para 1.

employment opportunities. The only secured creditor was Development Bank of Southern Africa who will receive a dividend of R12.50.

No other creditor, nor any shareholder, will receive any benefit or dividend distribution on their rights or claims.[172] The court found that there was no contravention in terms of the cancellation (which is the buy-back) and re-issue of shares was incorrect.[173] The court did not grant the interdict based on the fact that the shareholders rights were not infringed and he (Moodley) had no right to more shares than were allocated to him.[174] It is evident that a shareholder will be involved in business rescue proceedings if they have suffered prejudice, and a shareholder will not take preference over the super-preferent creditors.

## III THE KING REPORT AND SHAREHOLDER PROTECTION

King I was formed in 1994 and its purpose was to create a standard of corporate governance and as a result the *Code of Corporate Practices and Conduct* which established a set of principles which was voluntary.[175] The King Code applied to all companies listed on the Johannesburg Stock Exchange ('JSE'), large public entities (as defined in the Public Entities Act 93 of 1992), as well as other large unlisted public companies. King II replaced King I and King II deals with principles of good governance, relating to directors and boards. The importance of King II is that directors should act in accordance with the law but also take into consideration their fiduciary duties.[176]

There seems to be a wider variety of factors that has been recognised and public opinion recognises the interests of stakeholders, such as the: employees; investors; consumers; general public; and the environment.[177] It has been argued that the King I and King II Reports are not clear when it comes to stakeholder protection and also fails to provide guidelines to directors on how to act in the best interests of the company by considering the various stakeholders while managing the company.[178]

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172 Ibid para 25.
173 Ibid para 50.
174 Ibid para 54.
175 I M Esser 'The Protection of Stakeholder Interests in Terms of the South African King III Report on Corporate Governance: An Improvement on King II' (2009) 21 *South African Mercantile Law Journal* 188–201 at 189.
176 I M Esser & J Coetzee 'Codification of Directors' Duties' (2004) 12(1) *Juta's Business Law* 26–31 at 27.
177 Esser op cit note 175 at 191.
178 Ibid.

King II follows the 'enlightened shareholder value approach' where the director's role is to promote the success of the company for the benefit of the company and to generate maximum value for the shareholders.[179]

The King III Report is more structured and states that the board must create value for its shareholders, taking into account the interest of other stakeholders.[180] The board is not only accountable to the company but also to the various stakeholders.[181] A principle exists stating that there should be a balance between the various stakeholders, and this principle is in line with section 76(3)(*b*) of the Companies Act. Specific stakeholders are mentioned, such as: suppliers; creditors; employees; Government; external auditors; consumers; industry; media; regulators; and potential investors.[182] This has provided a more inclusive approach.

Lastly, the King IV Report was published in 2016 and came into effect on 1 April 2017. There were no significant changes from the King III Report to the King IV Report, except that Principle 5[183] places more emphasis on stakeholder inclusion. The Report states that directors have a fiduciary duty to act in the best interests of the company.[184]

If a shareholder brings an application to liquidate the company to gain access to funds and the director opposes the application based on the fact that they are acting on behalf of the company (as mentioned previously, a shareholder holds equity and a stakeholder includes employees, customers, service providers and the environment) then both the shareholders and stakeholders interests must be considered. When the shareholders want a company to be liquidated, not just their interests but the impact of the liquidation on the economy, must also be taken into account.

The interests can be considered by an ethics committee, and while the Companies Act places no obligation on a company to establish one, the King IV Report recommends the establishment of an ethic committee to ensure that the relevant interests are taken into account,

## IV CONCLUSION

It has been established that the shareholders, although referred to as affected parties, are not actively involved in the business rescue procedure unless their rights have been adversely

179 Ibid at 193.
180 Ibid at 197.
181 Ibid.
182 The King Report on Corporate Governance for South Africa 2002.
183 The King Report on Good Governance for South Africa 2016.
184 The King Report on Good Governance for South Africa 2016 at 48.

affected. The shareholder is dependent on the director to approve a business resolution and also be consulted of the rescue proceedings. The shareholder has a right to be informed of business rescue proceedings however, that is where its role ends, unless the shareholders' rights are affected.

It is trite that when a company is under business rescue, the shareholders have the most to lose should a company be liquidated and like in the case of *Fidentia* (where the widows and orphans of mineworkers lost substantially while the curators benefitted). Currently, our national airline South African Airways ('SAA') is under business rescue and although the Government is a shareholder, it does not have the right to vote on the business rescue plan unless their rights are affected by plan. The approach in the King Report can provide guidance when it comes to shareholders and how their interest should be protected.

I submit that the interests should be weighed up like it should have been in the case of *Fidentia* so that the average classes do not suffer and are not prejudiced.

CHAPTER 5

# THE ROLE OF EMPLOYEES IN BUSINESS RESCUE PROCEEDINGS

## I INTRODUCTION

Business rescue provides a mechanism that enables a company to return to a solvent status instead of being liquidated and ceasing its operations. South Africa has shed 2.2 million jobs in the second quarter of 2020,[185] and there has been an increase in companies entering business rescue which inevitably results in an increase job loss.

The Companies and Intellectual Property Commission ('CIPC') has reported that two-hundred-and-four[186] businesses have entered business rescue and with an increase in business rescue, it would also mean that apart from creditors and shareholders being affected, employees have a significant amount to lose. Employees are considered 'the lost souls of insolvency law.'[187] Chapter 6 of the Companies Act embraces the interests of employees, creditors, and shareholders. With regard to employees:

> 'Employees are recognised as creditors of the company that have a voting right in respect of any part of unpaid remuneration due before commencement of the business rescue proceedings. Employees must be consulted in the development of the business rescue plan. Employees are given the opportunity to address creditors at their meeting before they vote on the business rescue plan. Employees have the right to buy out dissenting creditors or shareholders who have voted against the approval of the business rescue plan.'[188]

Employees' rights have become a discernible feature under the new rescue dispensation of judicial management. Although employees were not significant considerations in the past, employees are now actively involved in rescue proceedings. Employees' rights and the creditors' interests should be properly balanced[189] in the sense that one class of rights should

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185 Stats SA available at http://www.statssa.gov.za/?p=13633#:~:text=unemployment%20levels%20drop-,SA%20economy%20sheds%202%2C2%20million%20jobs%20in%20Q2%20but,Africa%20on%2029%20September%202020, accessed on 10 October 2020.

186 CIPC 'Business Rescue Proceedings Status Report as at 30 September 2020' available at http://www.cipc.co.za/files/7016/0227/4751/Status_of_Business_Rescue_Proceedings_in_South_Africa_-_as_at_30_September_2020_v1.0.pdf, accessed on 10 October 2020

187 V Finch *Corporate insolvency law: Perspectives and principles* 2 ed (2009) 778.

188 A Loubser & T Joubert 'The role of trade unions and employees in South Africa's business rescue proceedings' (2015) 36 *Industrial Law Journal* 21–39 at 22.

189 Cassim et al op cit note 35 at 885; S Van Eck, T Joubert & D A Burdette 'Impact of labour law on South Africa's new corporate rescue mechanism' (2011) *The International Journal of Comparative Labour Law and Industrial Relations* 65–84 at 67.

not outweigh the other. The employee's interests are pivotal as the Act provides for trade unions to be established to facilitate and influence the process.[190]

As previously discussed in Chapter 4, shareholders are not afforded the protection that creditors and employees have. This alludes to the fact that the Act does not achieve the balance as contemplated in section 7(k), which provides for the efficient rescue and recovery of financially distressed companies, in a manner that balances the rights and interests of all relevant stakeholders.[191]

It has been argued that this imbalance extends into the aspect of remuneration and that employees' claims become due and payable during business rescue and these claims rank higher than those of creditors who provided post-commencement finance.[192] The over protection of employees would have the effect 'eroding the rights of the creditors.'[193] Employees' rights are extensively protected during rescue proceedings as affected persons, employees who become creditors,[194] and lastly employees.[195]

Section 128(1) of the Companies Act allows an 'affected person' to bring an application to commence business rescue proceedings and the definition of an 'affected person' includes the trade unions representing employees. Employees can be represented by a trade union and must exercise their rights through a trade union[196] and have the right to form a committee of employee representatives.[197]

Section 136(1) of the Companies Act ensures protection by providing that employees are to remain employed during rescue proceedings on the same terms and conditions subject to the following:[198]

'(i) changes occur in the ordinary course of attrition; or

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190 Loubser & Joubert op cit note 188 at 23.
191 See s 7(k) of the Companies Act.
192 Loubser & Joubert op cit note 188 at.
193 W J C Swart 'Business rescue: Do employees have better (reasonable) prospects of success? Commentary on *Employees of Solar Spectrum Trading 83 (Pty) Limited v AFGRI Operations Limited* (North Gauteng High Court, Pretoria (unreported) 2012-05-16 Case no 6418/2011; 18624/2011; 66226/2011; 66226A/11): cases' (2014) 35 Obiter 406–420 at 408.
194 See s 12 of the Companies Act.
195 Loubser & Joubert op cit note 188 at 23.
196 See s 144(1) of the Companies Act.
197 Ibid.
198 See s 136(1)(*a)* of the Companies Act.

(ii) the employees and the company, in accordance with applicable labour laws, agree different terms and conditions[.]'

As previously mentioned, employees are extensively protected. Section 136(1) provides that employees who were employed before business rescue commenced must continue their employments on the same terms and conditions. Section 136(1) of the Companies Act is more concerned with the 'contract' than the 'employee' and deals with contracts in the context of business rescue. The responsibility of terminating managerial employees is vested in the business rescue practitioner. Employment contracts are also excluded from the business rescue practitioners' powers.

The exclusion of employment contracts is indicative of the fact that while the business rescue practitioner may be of the view that employees' salaries may be exorbitant (and contributing to the financial distress) the practitioner is precluded from altering any terms in the employment contract. The strict approach adopted by labour legislation makes it difficult for a successful business rescue.

Employee's rights are further protected in section 189 and section 189A of the LRA which regulate retrenchments. When the business rescue practitioner decides that the company needs to retrench its employees, the business rescue practitioner must commence consultations with the employees in line with the LRA. The business rescue practitioner should act in accordance with the LRA when exercising its power in relation to employees.

The business rescue practitioner must act in accordance with section 189A of the LRA which imposes a sixty-day consultation period should there be a large number of employees being retrenched. The consultation must be a process where the employee and employer can engage in meaningful manner.

The last category of employees are those employees who have acquired rights as creditors due to unpaid remuneration in respect of employment related matters that were due and not paid.[199] Money that has become due and payable to an employee during the course of business rescue proceedings, and is not paid, must be treated as post-commencement finance.[200] Employee remuneration is paid after the business rescue practitioners' fees, and employee

[199] See s 144(2) of the Companies Act.
[200] See s 131(8)(*b*) of the Companies Act.

claims are treated as super-preferent and will rank above the secured and post-commencement lenders.[201]

Employees, by virtue of affected persons, have a right to be notified of the business rescue proceedings when business rescue is initiated by way of a resolution. While informing employees of business rescue proceedings can be seen as a benefit, it could also be argued to play to the detriment of the proceedings. Employees could cause unnecessary delays or have the trade unions push their personal agenda without regard to the actual rescue proceedings.

## II THE ROLE OF TRADE UNIONS AND EMPLOYEES IN BUSINESS RESCUE PROCEEDINGS

The Act provides that trade unions representing employees fall under the category of affected persons and therefore, they can apply to commence business rescue proceedings. Based on the definition provided, employees should exercise their rights through the trade unions and members who are not members of the trade union should exercise their rights in their individual capacity.[202]

Section 144 states that trade unions representing employees and unrepresented employees are entitled to their detailed rights, which places importance on the role of trade unions that they should play an active role to ensure that the members' rights are protected. Employees who are not represented can be represented by a proxy through a company employee, or organisation, or directly.[203]

An employee can only be represented if they have been appointed as his or her proxy, and trade unions may not assume that it has the power to represent members who are not members of that trade union.[204] Allowing trade unions and employees to initiate rescue proceedings is an important feature as the new rescue regime aims to protect employees.[205] Section 152 provides an opportunity for the employees' representative to address the meeting.[206] The wording of this section arguably lacks certainty because this could be

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201 Loubser & Joubert op cit note 188; *Merchant West Working Capital Solutions (Pty) Ltd v Advanced Technologies and Engineering Company Ltd* 2013 (ZAGPJHC) 109 para 21.

202 Ibid at 25.

203 Ibid.

204 Ibid.

205 A Lousber 'The business rescue proceedings in the Companies Act of 2008: Concerns and questions (part 1)' (2010) 3 *Journal of South African Law* 501–514 at 509.

206 See s 152(1)(*c)* of the Companies Act.

interpreted to include the committee of employee representatives, trade unions, or employees who formed a committee that do not belong to trade union.[207]

Suspension of an employment contract would not affect the employee's status as an affected person and can therefore still apply to commence business rescue.[208] Employees have a right to participate in the proceedings and do not need an order to intervene because they have an automatic right to participate.[209] This principle was confirmed in *AG Petzetakis International Holdings Ltd v Petzetakis Africa (Pty) Ltd*.[210] The trade union (NUMSA) intervened to postpone proceedings to enable them to file supporting documents in favour of business rescue and the court held that NUMSA is a registered trade union who represents employees and therefore has an automatic right by virtue of being an affected person and therefore participate in proceedings without needing an order to do.[211]

Petzetakis Holdings is the shareholder of Petzetakis Africa. Petzetakis Africa is unable to pay its debts as their assets amount to the value of R60 million and their liabilities amount to R225 million. The company ceased trading in 2010 and stopped paying their employees in 2011. In September 2011 the company applied to be placed under business rescue.

NUMSA, the trade union representing employees, sough a postponement. However, Sasol Polymers was a creditor and opposed the postponement and moved for provisional liquidation orders. The court found that the affected parties have a right to participate in the proceedings and the legislature did not intend that the affected party would have to apply for leave to intervene. [212]

## III THE CONSIDERATION OF EMPLOYEES IN THE COMMENCEMENT OF BUSINESS RESCUE

The courts consider whether the employees would benefit from business rescue. The requirements to commence business rescue proceedings is the requirement of financial distress and 'reasonable prospect'. Under judicial management, the courts decided whether or not to grant an order of judicial management by considering the interests of the creditors. The new

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207 A Loubser op cit note 205 at 694.

208 *Richter v Bloempro CC* (GNP) unreported case no 69531/2012 of 14 March 2014.

209 *A G Petzetakis* supra note 44 para 4.

210 Ibid.

211 Ibid para 4.

212 Ibid; see also *Cape Point Vinyards (Pty) Ltd v Pinnacle Point Group Ltd* 2011 (5) SA 600 (WCC) para 21; *Engen Petroleum Ltd v Multi Waste (Pty) Ltd* 2012 (5) SA 596 (GSJ) para 30.

approach in the Companies Act is that business rescue is preferred to liquidation.[213] Chapter 6 of the Companies Act provides a more inclusive approach and the interests of employees are considered under the requirement of a 'just and equitable and that reasonable prospect exists'.[214] The legislature has made provision for the requirement of an employee or trade union proving financial distress an provided under section 31(3), that the trade union must submit a request to the commission to be granted access to financial statements to commence rescue proceedings. This remedy is not available to individual employees and creditors which can be seen as a protective measure to ensure company confidentiality. The applicant must prove that the company has failed to pay an amount in respect of an employment-related amount.

The second requirement is that an employee must prove is that a reasonable prospect exists and that it is just and equitable. Although the requirement of just and equitable is unclear, it does however allude to the point that, the requirement of financial distress may pose challenging for an employee to prove. Therefore, this requirement allows the employee to prove financial difficulties under this requirement. [215]

The case of *Employees of Solar Spectrum Trading 83 (Pty) Limited v AFGRI Operations Limited* supra marks the first case where an employee brought an application to commence rescue proceedings. In this case, the applicants were employees who represented seventy-six temporary and permanent employees. All the employees lived and worked on the farm. The company, Solar Spectrum, was financially distressed and the issue before the Court was whether a 'reasonable prospect' existed, in terms of rescuing the business.

The Court considered the definition of section 7(k) and remarked that the purpose of legislation was to bring about change in the liquidation culture. This does not mean a creditor is precluded from applying for a liquidation order, although business rescue is preferred over liquidation. The Court found that even though the employees may not have access to the financial aspects, they do have knowledge of the business history, performance, and solutions, as employees are regarded as the 'heart and soul' of the business.[216]

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213 *Southern Palace* supra note 51 para 21.

214 T Rabilall 'Business Rescue as opposed to liquidation' available at http://www.cipc.co.za/files/3515/2688/8915/Buisness_Rescue_vs_Liquidation_Article_March_2018.pdf, accessed on 25 October 2020.

215 A Loubser 'The Role of Trade Unions and Employees in South Africa's Business Rescue Proceedings' (2015) 36 Industrial Law Journal at 31.

216 Solar Spectrum supra note 42 para 18.

The right of the creditor(s) to liquidate is subsequently weighed against the interests of the other stakeholders. In addition hereto, the word 'prospect' does not necessarily refer to a certainty, but rather to something that is 'future looking.'[217] The Court considered the fact that the employees have been living and working on the farm for a number of years, they support their dependants, as well as the fact that are willing to use their skills and knowledge to assist with the rescue of the business.

In conclusion, liquidation will likely result in the employees losing their employment and accommodation, which ultimately affects the dependants. The Court remarked that the 'prospect must be future looking and is dependent on a number of factors.'[218] The significance of this case is rooted in the fact that it is the first case where the employees applied to commence business rescue proceedings.

Although preserving and protecting employment is not one of the purposes of business rescue, the courts do consider employees in line with the purposes of section 7(k). The *Oakdene* case supra illustrates the court's reluctance to grant an order of business rescue in the absence of employees to consider. On the other hand, *the case* of *Cardinet*,[219] illustrates the court's willingness to commence business rescue although there were no employees to consider. An As the primary purpose of the Act is is to promote the economic development, the court ruled that business rescue would contribute to the job creation which is in line with the primary purpose of the Act.[220]

In the *NUMSA* case,[221] the business rescue practitioners of SAA issued consultation notices as part of a retrenchment process in terms of section 189 of the LRA and due to operational requirements. NUMSA, representing the employees, applied to Johannesburg LC for an order declaring the issuing of the notices as procedurally unfair, based on the fact that there is made no provision for this in the business rescue plan. The LC held that section 136(1) provides that a business rescue practitioner may initiate a retrenchment process only once a business rescue plan, contemplating retrenchments, has been presented.

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217 *Southern Palace* supra note 51 para 34.

218 Ibid.

219 *(Pty) Ltd v Wedgewood Golf and Country Estate (Pty) Ltd* (WCC) unreported case no 19599/2012 of 25 February 2013 *('Cardinet').*

220 A Loubser op cit note at 38.

221 *NUMSA* supra note 21.

In the absence of a business rescue plan, the issuing of notices commencing a consultation process over proposed retrenchments is procedurally unfair. In the *Ziegler* case,[222] Ziegler (a global logistics solutions company, providing freight forwarding and custom clearing services) concluded an agreement with SA Express. Zeigler alleged that SA Express was financially distressed and that it was accordingly just and equitable to place Zeigler under business rescue (as opposed to liquidating them).[223]

By considering the requirement of a 'reasonable prospect' of success, the Court found that one-thousand job losses would likely occur, being very significant in nature, which would have detrimental effects on their families.[224] Liquidation would also result in South Africa losing its asset which contributes significantly to the economy.[225]

In light of the above it is evident that our courts are not willing to grant an order to commence business rescue if there are no employees.[226] It is apparent that a court will likely grant an order if it discovers that business rescue will create or save jobs, which is in pursuit of supporting the purposes of section 7 of the Act. Regardless of the fact that a company has no employees at the time, an order to commence business rescue may promote the objectives of the Act,[227] especially the objective to promote economic development.[228]

Whilst it is evident that employees are afforded extensive protection, this can be to the detriment of the business rescue proceedings. For this reason, the suggested approach should be to rescue the business. The successful rescue of the business will ultimately save and protect jobs. Job retention should be a secondary advantage to the granting of a business rescue order.

## IV CAN A DIRECTOR FALL INTO THE CATEGORY OF AN EMPLOYEE?

An executive director is one who is involved in the day-to-day management, and is a full-time salaried employee, while a non-executive director is one who is not involved in the day-to-day activities and is not a full-time salaried employee.[229] The Companies Act, does however not

222 *Ziegler* supra note 17.
223 Ibid para 10.
224 Ibid para 59.
225 Ibid.
226 Loubser & Joubert op cit note 188 at 32.
227 Ibid; see for example *Cardinet* supra note 219 para 53.
228 See s 7(k) of the Companies Act. Employees should also be remunerated for the work done and the idea of giving the employees preference is correct.
229 Ibid at 96. See also King Report on Corporate Governance (King 1) para 4, published in 1994 by the Institute of Directors which distinguished between executive and non-executive directors and was further developed in King Report on Corporate Governance for South Africa 2002 (King II).

use the words 'executive' and 'non-executive' director, however the Act does draw a distinction for example in section 94 of the Companies Act where it states the director who serves on the audit committee must not be involved in the day to day activities of the business or be employed full-time.

Under the LRA section 213 provides a wide definition of an employee and provides that an employee is 'any person excluding an independent contractor and any other person who in any manner assists in carrying on or conducting the business of an employer.'[230]

The definition in LRA would apply to most directors.[231] The Labour Court ('LC') in *Chilliebush Communications (Pty) Ltd v Johnston*[232] dealt with the issue of whether Mr Miyeni was an employee of the company. Mr Miyeni, who was the third respondent in the matter, was a managing creative director of Chilliebush Communications and claimed unfair dismissal at the Commission for Conciliation, Mediation and Arbitration ('CCMA') proceedings. The CCMA found that Mr Miyeni was in fact an employee of the company.

During arbitration proceedings, the commissioner found that Mr Miyeni was an employee of the company. The LC had to determine whether Mr Miyeni was an employee and whether he was unfairly dismissed. The court found that a director who is an employee will hold two positions and act in two capacities.[233]

The Companies Act and the LRA applied and the court found that he was an employee as defined in terms of section 213 of the LRA.[234] The court considered the decision in *PG Group (Pty) Ltd v Mbambo,*[235] and found that there was no reason that a director cannot fall under the definition of an employee. The third respondent (Philip Thomas) was a director and during restructuring was transferred to PG Glass as a financial director. The third respondent's services were terminated by the board (PGSI) who was the holding company and the sole shareholder.

The third respondent alleged unfair dismissal. PG Group argued that he had not been dismissed and his services were terminated by the board in terms of articles of association. The PG Group argued that he had not been dismissed and that he was not an employee of the

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230 See s 213 of the LRA.

231 *P G Group (Pty) Ltd v Mbambo NO and Other* 2004 (ZALC) 78 ('Mbambo') para 24.

232 2010 (ZALC) 3 ('*Chilliebush*') para 24.

233 Ibid.

234 Ibid para 25.

235 *Mbambo* supra note 231 para 29; *Whitcutt v Computer Diagnostics & Engineering (Pty) Ltd* 1987 (8) ILJ 356 (IC).

company. The LC found that section 213 of the LRA would apply to most if not all directors.[236] A director would perform duties that would exclude him from the definition of an employee but on the other hand, would perform duties as an employee.[237] The court accordingly held that Philip Thomas was an employee.[238]

The dual capacity was illustrated in *Amazwi Power Products (Pty) Ltd v Turnbul*[239] which dealt with a director who was a financial director. The respondent resigned and wished to remain an employee of the company. The managing director accepted her resignation and offered to pay her until the end of March. The respondent rejected and stated that she wished she resigned as a director and not as an employee. The court had to consider whether she was unfairly dismissed. The court found that a person could resign as a director but still be an employee of the company.[240]

The arbitrator initially found that she was unfairly dismissed and awarded compensation. On review, the court dismissed the application to set aside the award but the compensation was altered. On appeal, the LC agreed that protection is afforded in terms of the LRA[241] to a managing director.[242] The issue was whether the employee terminated her employment by means of her resignation. It was evident that she intended to resign from the BOD and remain an employee. The issue that arises is that, although she is not starting anew in the company, she is starting in a new position. The company would have to pay a severance package if they cannot offer alternative employment.[243]

*Protect A Partner (Pty) Ltd v Machaba-Abiodun*[244] had to, once again, consider if a director was an employee, and adopted a reality test, namely:

(a) The right of supervision and control of the employer over the employee;

(b) Whether or not the employee forms an integral part of the organisation; and

(c) The extent of financial dependence of the employee on the employer.[245]

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236 *Chilliebush* supra note 232 para 27.
237 Ibid para 26; *Hydraulic Engineering Repair Services v Ntshona & Others* 2008 29 ILJ 163 (LC).
238 *Chilliebush* supra note 232 para 33.
239 2008 29 ILJ 2554 (LAC) ('*Turnbul*').
240 Ibid para 20.
241 Ibid para 14.
242 Ibid para 15.
243 H Stoop 'The Company Director as Employee' (2011) 32 *Industrial Law Journal* 2367–2377 at 2371.
244 2013 34 ILJ 392 (LC) ('*Protect A Partner'*).
245 Ibid para 53.

The court considered the element of 'control' and that it must be determined whether the employee assists the employer in the conducting of the business in order to decide whether the employee formed part of that organisation or not.[246] The court found that a company is a juristic person and exercises its powers through its organs, and the court found that Machaba-Abiodun was an employee and an executive director.

Executive directors have therefore been accepted as employees and therefore will be regarded as affected parties and can therefore apply to commence business rescue proceedings.[247] Executive directors would have to exercise their rights directly and in their individual capacity, in their best interests, as executive directors would not be registered with a trade union and section 144(1) requires that employees be registered with a trade union.[248]

Employees do not have access to all the information to prove the requirements for a business rescue order like a director, which is why the courts adopted a sympathetic approach towards the employees in the *Solar Spectrum* case.[249] The courts will not treat directors who apply to commence business rescue with the same sympathy a director is held to high standards as he understands the dynamics and financial position when applying to place the company under business rescue. [250] The director unlike employees will have access to the financials and therefore would be able to satisfy the courts whether the company is financially distressed or not.

The problems that arise by virtue of a director being regarded as an affected person is that section 131(6) provides that a board cannot adopt a resolution to commence business rescue proceedings once liquidation proceedings have commenced, but an affected person can apply to court to commence business rescue proceedings even if liquidation proceedings have already commenced. The issue with this is that a director (as an affected person) could 'maliciously or fraudulently cause the suspension of liquidation proceedings for a substantial period.'[251]

The second complication is that if the director will be allowed to nominate the business rescue practitioner and this could result in the director having undue influence on the business

246 Ibid para 57; E Joubert & A Loubser 'Executive directors in business rescue: Employees or something else' (2016) 49(1) *PER* 95–104 at 98.
247 Joubert & Loubser op cit note 246 at 99.
248 Ibid.
249 *Solar Spectrum* supra note 42.
250 Joubert & Loubser op cit note 246 at 99.
251 Ibid at100.

rescue practitioner and the affected person can also apply to court to remove the practitioner who was appointed by the board.[252] Directors as affected persons would know the financial status of the business and could cast doubt whether the requirements have been met.[253]

Finally, directors as affected persons can apply to court to set aside a board resolution to commence business rescue proceedings. However, the legislature has made provision for this particular circumstance and section 130(2) provides that a director who voted in favour of the resolution may not apply to set aside the resolution or to set aside the appointment of the business rescue practitioner, unless the director can show that court that he supported the resolution in good faith, and based on information that turned out to be false or misleading.[254]

A practitioner may remove a director from office based on the grounds as set out in section 137(5), which states that a practitioner may remove the director on the grounds that he (the director) has:

> '(a) failed to comply with a requirement of this Chapter [6]; or
>
> (b) by act or omission, has impeded, or is impeding—
>
> (i) the practitioner in the performance of the powers and functions of practitioner;
> (ii) the management of the company by the practitioner; or
>
> (iii) the development or implementation of a business rescue plan in accordance with this Chapter [6].'

An executive may be removed as a director but would still be an employee of the company. The practitioner would not be allowed to amend the terms and conditions of the director's employment contract without his consent, and would have to comply with the LRA should the practitioner want to retrench or dismiss the director.[255]

Employees, including directors, enjoy super-preferent status with regard to unpaid remuneration. Directors' unpaid salaries, bonuses and other unpaid benefits (whether the amount due is unreasonably high or not) would also have the super-preferent status. I submit that is fair that employees enjoy super-preferent status in respect of unpaid remuneration, it is unfair that directors fall into the same category if the directors caused the financial distress.

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252 Ibid.
253 Ibid.
254 Ibid.
255 Joubert & Loubser op cit note 246 at 102.

# V CONCLUSION

Employees are protected in terms of the Companies Act, LRA and the Constitution. Employees have an active role in business rescue proceedings and are represented by trade unions who will engage with the business rescue practitioner on the employees' behalf. This position, in my view, will work to the advantage to the employee due to the fact that most often employees may have issues with language barriers or understanding the legal terminology or their rights as employees.

This can have an adverse effect on the employees' rights. However, on the other hand, it has been suggested that an over-protection of employees could be to the detriment of the rescue proceedings. Their over-protection and involvement could cause unnecessary delays, especially if the employees do not make decisions with the best interest of the company in mind.

CHAPTER 6

# THE EFFECT OF BUSINESS RESCUE PROCEEDINGS ON PROPERTY OWNERS

## I INTRODUCTION

Business rescue not only affects the 'affected parties' but also affects landlords and those who have had entered into other forms of agreements with the company. When a company is placed under, or initiates, business rescue proceedings, it means that the performance of either the company, or the other contracting party, is outstanding. This is known as an 'executory contract', which was described in *Nedcor Investment Bank v Pretoria Belgrave Hotel (Pty) Ltd*[256] as a contract under which 'one or the other, or all of the obligations remain unfulfilled.'[257]

The Act places restrictions on third parties against the property of the company or property in the company's possession.[258] As soon as business rescue has commenced, there is an automatic stay on legal proceedings which means that the creditors can enforce no legal action against the company, its assets or property.[259] Section 133 places a moratorium on legal proceedings, and therefore no legal proceedings may be taken against the company while under business rescue. Protection to property owners is envisaged under section 133(1) of the Act.

The moratorium has been argued to be an important feature in business rescue , without which it would not be possible to rescue a company.[260] The moratorium freezes both the secured- and unsecured creditors' rights.[261] The moratorium can be lifted under certain exceptions, such as with the business rescue practitioner's written consent, or with leave of the court.[262] Both the cases of *Kariba* SCA[263] and *Panamo Properties (Pty) Ltd v Nel*[264] criticised the drafting in the Act which has led to uncertainty, including the rights of creditors, and the business rescue practitioner in dealing with uncompleted or executory contracts.[265]

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256 2003 (5) SA 189 (SCA) ('*Nedcor*').
257 Ibid para 6.
258 Rushworth op cit note 76 at 375.
259 See s 133(1) of the Companies Act.
260 M F Cassim 'The Effect of the Moratorium on Property Owners during Business Rescue' (2017) 29 *South African Mercantile Law Journal* 419–449.
261 Ibid 422.
262 See ss 133(a)–(b).
263 *Kariba* SCA supra note 120 para 43.
264 2015 (5) SA 63 (SCA) ('*Panamo Properties*') para 1.
265 S Lawrenson 'Lease agreements and business rescue: In need of rescue?' (2018) 3 *TSAR* 657–670 at 658.

In the *Kariba* SCA case,[266] Kariba (furniture manufacturers) owed money to the bank (African Banking Corporation of Botswana). The bank's debt was secured by a suretyship by the shareholders.

Kariba could not pay its debts and the shareholders sought to place the company under business rescue. The bank voted against the business rescue plan. The shareholders wished to make a binding offer to purchase the bank's vote interest in terms of section 153(1)(*b*)(ii). The practitioner ruled that bank could not respond to the offer and that the offer was binding on the bank and the bank's voting interest must be transferred to the shareholders.

The practitioner amended the plan which reflected that the bank had zero percent interest, while the shareholders held ninety-five percent. A vote was then taken and the rescue plan was taken by the reconstituted creditors which excluded the bank.[267] Kathree-Setiloane J in the High Court ('HC') found that the term 'binding offer' did not anticipate an option or an agreement in the contractual sense, but was rather 'a set of statutory rights and obligations, from which neither party could resile.'[268]

This meant that once an offer is made, the parties are bound thereto.[269] Govern J, however, disagreed with Kathree-Setiloane J in *D H Brothers Industries (Pty) Ltd v Gribnitz* supra, and held that if it was the intention of the legislature to bind the 'offeror' and 'offeree', the legislature would have expressly mentioned it, however, a creditor cannot be deprived of their voting rights and claim without consent.[270] The words 'offer' does not give rise to set of rights and obligations.[271]

In *Panamo Properties*,[272] (dealing with the lapsing of a resolution passed by the board) Panamo Properties' sole shareholder was a trust. Mr and Mrs Nel were the trustees and also the directors. They sought to commence business rescue proceedings to avoid the company's property being sold, due to a judgement taken against the company by a financial institution. A business rescue plan was approved, but there were no funds, and the business rescue practitioner sold the property which was contained in the business rescue plan.

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266 *Kariba* SCA supra note 120.
267 Ibid para 6.
268 *Kariba* supra note 70 para 29.
269 Ibid para 8.
270 *Gribnitz* supra note 132 para 40.
271 Ibid.
272 *Panamo Properties* supra note 264.

Upon transfer, the trust (represented by the Nel's) alleged that the company did not comply with the procedural requirements in terms of section 129, which meant that the business recue proceedings were invalid. This was upheld by the HC. The SCA had to decide the meaning of section 129(5) and the manner of interpretation. The SCA held that there is no provision that provides for the automatic termination of rescue proceedings as a result of failing to comply with procedural requirements.[273]

## II THE MORATORIUM

It has been argued that the moratorium causes injustice to the creditors but it is necessary to assist the business rescue practitioner in assisting the company return to a financially viable state without having to entertain claims from creditors.[274] The Act does not define 'legal proceedings' and 'enforcement action'.[275] In the case of *Chetty t/a Nationwide Electrical v Hart*,[276] the court dealt with the exclusion of an arbitration award on the basis that the moratorium precluded it. The principle contractor was under business rescue when the award was granted. Chetty argued that the award constituted legal proceedings in terms of section 133 of the Companies Act.[277]

The court referred to section 142(3), which requires the company to provide details of all proceedings to the business rescue practitioner, including arbitration proceedings.[278] The court then considered why there would be a need for disclosure if it was excluded, and the court found that the purpose of the Act was to allow 'breathing space'. Arbitration would interfere with the effectiveness of business rescue and therefore the court found that arbitration does amount to 'legal proceedings' which are prohibited in terms of the Act.

The purpose of the moratorium is to give effect to section 7(k) and prevent the owner from claiming the return of the property during business rescue.[279]

## III THE EFFECT OF BUSINESS RESCUE ON LEASE AGREEMENTS

Section 133 prevents: the property owner (whose property is hired or leased) from removing the company from the leased premises; or in the case of an instalment-sale transaction, the

273 Ibid para 19.
274 Cassim op cit note 260 at 422.
275 A Potgieter 'The business rescue moratorium: Company law' (2016) 16(2) *Without Prejudice* 20.
276 2015 (6) SA 424 (SCA) ('*Chetty*').
277 Ibid at para 3.
278 Ibid at para 29.
279 Cassim op cit note 260 at 440.

property owners are prevented from recovering the property.[280] The property owners are prevented from claiming their property, as this would hamper the prospects of rescuing the company, and this extends to hired equipment, or motor vehicles, which are critical to the rescue of the business.[281]

A property owner, by virtue of section 133 of the Companies Act, cannot take any legal action against a company engaged in business rescue proceedings. Despite this, the wording of section 133 of the Companies Act does not prevent the cancellation of a lease agreement and this cancellation does not amount to an 'enforcement action' as contemplated in section 133. Therefore, a property owner or landlord may legally cancel a lease agreement (or other relevant agreement) with the company, without acquiring the permission of the court or the business rescue practitioner.[282]

The concept of cancellation-, and enforcement action are mutually exclusive, and this principle is applied in the case of Cloete Murray.283 In this case, Wesbank concluded an instalment sale agreement with Skyline Crane Hire ('Skyline'). Wesbank sold movable goods to Skyline but retained ownership until the full purchase price was paid. Skyline was placed under business rescue and due to Skyline's default payments to Wesbank, Wesbank sought to cancel the agreement with Skyline.[284]

The SCA found that Wesbank had a right to cancel the agreement, based on the fact that there is no moratorium preventing this cancellation. The basis for this judgment is that section 133 prevents a writ of execution (or attachment enforcement action), whilst 'cancellation' refers to the cancellation of obligations between the parties.[285]

In *Madodza (Pty) Ltd v Absa Bank Ltd*[286] Madodza (a company conducting a transport business) entered into finance agreements with Absa Bank. When Madodza defaulted on their payments to Absa, Absa cancelled the relevant agreements. Notably, the vehicles remained in the possession of Madodza. Madodza conducted a transport company which made the vehicles

280 See s 134(1)(*c*) of the Companies Act.
281 Cassim op cit note 260 at 423.
282 See ss 133(1)(*a*)–(*b*) of the Companies Act; see also *J V J Logistics v Standard Bank of South Africa* 2016 (6) SA 448 (KDZ) ('*J V J Logistics*').
283 *Cloete Murray* supra note 72.
284 Ibid para 5.
285 Ibid para 32.
286 and Others 2012 (ZAGPPHC) 165 ('Madodza').

essential to continue to conduct business. Absa Bank obtained various court orders to compel the return of the vehicles from Madodza.

Subsequently, Madodza entered into rescue proceedings and the removal of Madodza's possessions (vehicles) were prohibited by the moratorium. The Court found that the words 'legal action' and 'enforcement action' are not defined in the Act. Despite this, the Court noted that the intention of the legislation is to consider the widest scope possible, as to include 'any 'any conceivable type' of action which will enable a company to operate.[287]

Section 133 requires that the property be in the lawful possession of the company. The issue in the Madodza case is that the agreement was cancelled and therefore Madodza was not in lawful possession of the vehicles. It is for this reason that the application was unsuccessful.[288] The moratorium would not apply where an agreement is cancelled and the company is ordered by court to return the vehicle, before business rescue has commenced. The Court held that the applicant (Madodza) was not in lawful possession and could not rely on section 133(1). Therefore, vindicatory proceedings against a company under business rescue is valid. The Court in Madodza applied a wide interpretation of lawful possession to prevent the granting of the moratorium.[289]

The facts in *J V J Logistics*[290] are similar to that of the Madodza case. In *J V J Logistics* the applicant fell into arrears pertaining to an instalment-sale agreement with Standard Bank. The applicant (Standard Bank) took possession of the vehicle and retained ownership. However, when the company (J V J Logistics) defaulted, Standard Bank sought an order for the repossession of the vehicle before J V J Logistics went into voluntary business rescue.[291]

As mentioned above, a moratorium serves protection for those who are in lawful possession of the property. The Court in J V J Logistics found that there are two approaches, the first being the one as adopted in *Madodza* supra, and the second being to distinguishes between 'just' and 'unjust' possession, which translates to lawful- and unlawful possession.[292] It is essential to once again reiterate that the moratorium does not apply where cancellation of the agreement occurred before business rescue commenced. The applicant became the lawful

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287 Ibid para 12. In promoting the purpose of business rescue, it is suggested that our courts should not enforce existing court orders. The effect of s 133(1) is that legal proceedings are stayed, and that enforcement actions may not be initiated (and if they have commenced, they should be stopped).

288 Ibid para 17.

289 M F Cassim op cit 260 at 430.

290 *J V J Logistics* supra note 282.

291 M F Cassim op cit 260 at 430.

292 *J V J Logistics* supra note 282 para 26.

holder upon the lawful the conclusion of the instalment-sale agreement and was no longer the lawful holder when the contract was cancelled. [293]

The moratorium on enforcement-action is in line with the purpose of business rescue, granting the business rescue practitioner with ample time to reorganise its affairs. The Court in Kythera,294 once again, had to consider if the cancellation of a lease agreement was valid, and whether it fell within the ambit of section 133(1) of the Act, after business rescue proceedings have commenced. In this case, the landlord intended to evict the tenant (Le Rendez-Vouz Café CC trading as News Café, Bedfordview) who had defaulted on his rental and utilities for a period of three months. The landlord sent two notices of breach to the tenant, however, the landlord only cancelled three months after the company was placed under the business rescue.[295]

The Le Rendez-Vouz Café CC placed itself under voluntary business rescue when it fell behind with three monthly rental payments and municipal payments. The landlord cancelled the lease agreement on 7 March 2016.[296] The landlord argued that the lease agreement was validly cancelled after the tenant had been placed under business rescue. The landlord also argued that the tenant was misusing the business rescue process to occupy the premises and in order to avoid paying rent.[297]

The tenant (Le Rendez-Vouz Café CC) argued that the eviction constituted an action prohibited in terms of section 133(1) and the lease agreement was not validly cancelled.[298] The court consulted the reasoning of the *Cloete* case supra, which emphasised that the intention of the legislature was to allow 'breathing space' by placing a moratorium on legal proceedings and that cancellation does not amount to an 'enforcement action'.[299] Therefore, it is possible to cancel an agreement during business rescue proceedings.[300] The court held that the lease was validly cancelled and therefore the tenant was an unlawful occupier and section 133 does not preclude the legal process of ejectment.[301]

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293 M F Cassim op cit note 260 at 430.
294 *Kythera Court v Le Rendez-Vous Café CC* 2016 (6) SA 63 (GJ) ('*Kythera*').
295 Ibid para xx.
296 Ibid para 3.
297 Ibid.
298 Ibid para 13–14.
299 *Cloete Murray* supra note 72 para 40.
300 *Kythera* supra note 294 para 13; see also *Southern Value Consortium v Tresso Trading 102 (Pty) Ltd* 2016 (6) SA 501 (WCC) ('*Southern Value*').
301 *Kythera* supra note 294 para 16.

The rule that section 133 does limit juristic acts applies to creditors, meaning that under section 133 and that no 'enforcement action' may be taken against a company that is under business rescue. However, cancellation of a lease agreement does not fall within the ambit of enforcement action envisioned by section 133, so to can a creditor cancel agreements.

This principle was applied in the case of *LA Sport 4x4 Outdoor CC v Broadsword Trading 20 (Pty) Ltd*[302] where the court *a quo* held that cancellation does in fact amount to an enforcement action, but the SCA held that section 133 does not limit juristic acts and therefore the cancellation was valid.[303] The court found that the purpose of the moratorium was to limit legal proceedings, or an enforcement action (in relation to property owned by other entities other than the business, or in the unlawful possession thereof).[304]

It is trite in law that upon the termination of a lease agreement, the lessee has a duty to vacate the premises, otherwise he would be an unlawful occupier.[305] Section 134 of the Companies Act makes reference to property that is lawfully in possession of the company.[306] The intention behind this is that if legal proceedings applied to all legal disputes regarding property then it would interfere with the common-law rights of ownership when seeking to protect their own property.[307]

A business evicted by a property owner would set off a chain reaction if the business would have a franchise agreement. For example, company 'X' has entered into a legally binding franchise agreement with property owner 'Y'. Y evicts X based on breach of agreement as X failed to pay rent. This eviction leads to an inevitable sequence of events that may further complicate X's pursuit of obtaining solvency status as numerous expenses need to be accounted for such as relocation costs, point of sale system, and electricity *inter alia* that would complicate a business trying to return to a solvent state. Without the necessary infrastructure (i.e. place of business or premises) it would be nearly impossible to generate enough income in order to become solvent.

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302 2015 (ZAGPPHC) 78 ('LA Sport 4x4'); see also K Weyers 'Cancellation or suspension of agreements during business rescue: Company law' (2015) 15 *Without Prejudice* 16–17 at 17.

303 Ibid *LA Sport 4x4* para 44.

304 *Kythera* supra note 294 para 9.

305 Ibid para 12.

306 *J V J Logistics* supra note 282.

307 Lawrenson op cit note 265 at 660; *Energydrive Systems (Pty) Ltd v Tin Can Man (Pty) Ltd and Others* 2017 (3) SA 539 (GJ) ('*Energydrive*') para xx.

It is submitted that a provision prohibiting the landlord from cancelling the executory lease agreement be inserted into the Act, along with allowing a business rescue practitioner to cancel or continue an executory contract without having to apply to court.[308]

The landlord's claim for rent does not fall into 'financing' in terms of section 135(2) or 'costs of business rescue proceedings' in terms of section 135(3), and therefore does not have the preferred status.[309] The suggested approach when dealing with evictions, is that upon the interpretation of section 133(1), 'enforcement action' is precluded, regardless of whether the company is in lawful possession of the property, or not, except with the consent of the business rescue practitioner.[310]

A property owner is required, in terms of the common law, to apply for an eviction order as the Prevention of Illegal Eviction from and Unlawful Occupation of Land Act[311] does not apply to commercial leases and juristic persons.[312] The purpose of section 133 is to allow the court to balance the rights of the individual 'affected persons' and the general body of other persons. Therefore, a creditor landlord can apply to court for leave in terms of section 133(1)(*b*) and bring an application for order of eviction.[313]

## IV REMEDIES AVAILABLE TO PROPERTY OWNERS

A property owner that wishes to recover property in business rescue can seek the written consent of the business rescue practitioner.[314] The business rescue practitioner is required to act reasonably and consider the following three criteria:

(a) The purposes of business rescue;

(b) The company's circumstances; and

(c) The nature of the property and rights claimed in respect of it.[315]

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308 Ibid; C Marumoagae 'The law relating to executory contracts in South Africa During Business Rescue Proceedings' (2017) 3 *Journal Of Corporate and commercial Law and Practice* 31–51 at 35.

309 Ibid; Lawrenson op cit note 265.

310 Lawrenson op cit note 265 at 663–664.

311 Act 19 of 1998 ('PIE Act').

312 Lawrenson op cit note 265 at 664; *M C Denneboom Service Station CC v Phayane* 2015 (1) SA 54 (CC) ('*Denneboom*') para 17: The Court held commercial occupants and juristic persons do fall within the ambit of the PIE Act.

313 *LA Sport 4x4* supra note 302 para 39.

314 See s 134(1)(*c*) of the xx Act.

315 M F Cassim 'The safeguards and protective measures for property owners during business rescue' (2018) 30(1) *SA Merc LJ* 40–70 at 43.

If the business rescue practitioner unreasonably withholds consent, then the property owner can apply to court to lift the moratorium.[316] The creditor is allowed to seek the leave of the court, or proceed with the legal proceedings under section 133(1)(*b*), if the business rescue practitioner refuses to give his or her permission, or even without first seeking the permission of the business rescue practitioner under section 133(1)(*a*) of the Act.[317]

However, the preferred approach is to seek permission from the business rescue practitioner, whether it is to institute proceedings or to recover the property. Application to court should of the last resort, as it would save legal costs and would not burden the courts.[318]

## V THE LIFTING OF THE MORATORIUM

The courts have been granted wide discretion to lift the moratorium.[319] The court must take into account the purpose and object of section 133(1)(*b*) together with section 7(k), and section 128(1)(*b*). Each case must be determined on its own set facts and there is no closed list of factors. The court will, however, consider the following factors:

> '(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.'[320]

The lessor of the property should be able to repossess its property, or goods, if the asset is not needed for the 'effective business rescue', or where the asset is unlikely to obstruct the purpose of rescue.[321] If the business rescue practitioner notifies the creditors that there is no prospect of success, the business rescue practitioner should consent to the landlord repossessing his property.[322]

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316 See s 133(1)(*b*) of the xx Act.
317 *Chetty* supra note 276 para 41.
318 Cassim op cit note 315 at 45.
319 *Mabote and Others v Van Der Merwe NO and Another* 2016 (ZAGPJHC) 185 *('Mabote')* para 28.
320 Ibid.
321 Cassim op cit note 315 at 47.
322 Ibid at 48; see also *178 Stamfordhill CC v Velvet Star Entertainment CC* 2015 (ZAKZDHC) 34 ('*178 Stamfordhill CC'*).

In situations where the repossession would obstruct the purpose of the Companies Act, a balancing test is required. The courts are required to exercise discretion in determining whether to grant, or refuse, leave for the enforcement of proprietary rights.[323] The balancing act entails considering the loss the owner would face in applying the moratorium, and on the other hand, the benefit for the: company; employees; creditors; and other stakeholders in applying the moratorium. One would have to consider the effects to the company and its affected persons if it were forced to leave the premises and the property owner who against is will is forced to leave his property in possession of the company.[324]

The balancing act requires a flexible approach and is determined on a case by case basis based on the facts before the court.[325] The court could require that the business rescue practitioner make ongoing payments of rent to the property owner, and could also consist of periodic payments, or compensation of rent.[326] Preventing a company a place to operate could mean that the company would be prevented from trading, and therefore earning revenue.[327]

The owner should be allowed to recover rental payments from the business if the property owner is refused leave, or permission, to recover his property.[328] The general rule is that if the owner is refused to recover his property, then the refusal should be allowed on the basis of continued rental payments, or compensation.[329]

It would be unfair for property owners to allow a business (in business rescue) to occupy the property without rental payments, except where it is unavoidable. This would mean that the property owner is compelled to fund business rescue venture. This principle will also apply to property owners who entered an instalment-sale agreement, where goods are leased to the company, and where the company possess movable property.[330]

If the lessee remains in occupation of the property after the lease is cancelled by using section 133 of the Act, the property owner would be entitled to damages.[331] If the court finds that the business cannot make rental payments, or other forms of compensation, due to its lack

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323 Cassim op cit note 315 at 49.
324 Ibid.
325 Ibid.
326 Ibid at 55–56.
327 Cassim op cit note 315 at 50; see also Cassim op cit note 260 at 434.
328 Cassim op cit note 315 at 55; see also *Southern Value Consortium v Tresso Trading* 102 (Pty) Ltd 2016 (6) SA 501 (WCC) (‘*Southern Value*’) para 7.
329 Ibid; see also Cassim op cit note 315 at 55.
330 Ibid.
331 Ibid at 57.

of finances, the court may then limit the period in which the company may use the property.[332] The threshold period is three months.[333]

The contentious issue is whether our law allows the business rescue practitioner to suspend obligations in terms of section 136(2) of the Companies Act. This section is wide enough and allows the property owner to be deprived of their property rights to possession and rent.[334] The business rescue practitioner could choose which provisions to maintain, and those which are burdensome, could be rejected. This could mean that the property owners are only dealt with at the very end of the proceedings, which could cause severe loss to the property owner.

If the property owners' rights are suspended they would not obtain the right to cancel their contract due to non-payment of rent or compensation.[335] The courts would need to come to the assistance of property owners (whose rights have been unfairly prejudiced).[336] The owner would also not be able to validly cancel the agreement because when the business rescue practitioner suspends the obligations, the failure to pay rent in post-commencement finance becomes due during business rescue proceedings. Therefore, the property owner will not have a valid claim as there will be a breach.

Our current legal position is that unpaid rent is treated as an ordinary unsecured claim. Unpaid rental in terms of post-commencement finance will also depend on the court, as it seems that our legislator intended that there is no automatic right for a lessor to receive post-commencement finance.[337]

## VI CONCLUSION

The current position is that the property owner can cancel the lease agreement, instalment-sale agreement or any other agreement if the company has breached its obligations in terms of the contract. The one way this breach could occur is failure to pay rent. It has been established that the cancellation of the contract does not amount to an 'enforcement action',[338] prohibited by section 133(1) of the Companies Act.

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332 Ibid.
333 Ibid.
334 Cassim op cit note 315 at 59.
335 Ibid.
336 Ibid at 59.
337 Ibid at 63.
338 *Cloete Murray* supra note 72.

The exception, however, is where the business rescue practitioner suspends the company's obligations in terms of section 136(2)(*a*) of the Act. The 'suspension' means that a company is suspended from its obligation to pay rent, and the failure to make payments when it becomes due, means that the company will not be in breach, and therefore the property owner has no grounds to cancel the agreement.[339] Cancellation does not give the property owner the right to reclaim his property.[340] The recovery of the property is still subject to section 133(1) and the protection afforded in section 134(1)(*c*) of the Act.

Our courts have adopted a sympathetic approach towards property owners. It is argued that the courts are incorrectly applying the moratorium, instead of using the protection afforded in terms of the Act, the courts are ruling that the moratorium would not apply where a property owner cancels the agreement.[341] This may be construed as a disregarding of the intention of the legislature, by the courts.[342]

Business rescue is meant to be a short-lived process and the moratorium is aimed to give effect the purpose of business rescue.[343] If property owners deprive businesses of their rights to trade, then it in itself will not assist with the rescue of a distressed business. What should also be taken into consideration is that if a company has a client database, moving premises may cause an inconvenience to their clients which could also hamper the rescue proceedings, which in turn will not give effect to the purpose outlined in section 7(k) of the Act.

339 Cassim op cit note 260 at 447.
340 Ibid.
341 Cassim op cit note 260 at 429.
342 Ibid.
343 Ibid.

CHAPTER 7

# I CONCLUSION

Business rescue is a mechanism that is viewed as a more holistic approach, as compared to judicial management, as it takes into account a range of factors, such as: the interests of the creditors, employees, and shareholders; as well as the economic value the company will have if it were liquidated.[344] This holistic approach is observed by interpreting of the Companies Act, which states that the Act must be interpreted to give effect to the purpose,[345] set out in section 7(k).[346]

Section 7(k) provides for the efficient rescue of financially distressed companies in a manner that balances the rights, and interests, of the relevant stakeholders. This approach provides an alternate rescue mechanism to creditors, as opposed to liquidation proceedings which was seen as the traditional approach.[347]

Business rescue can commence by one of two ways, namely: by way of a resolution passed by the BOD;[348] or an application can be brought before a court by an 'affected person'.[349] An affected person is a creditor, shareholder, or an employee.[350]

The provisions set out in the Act show that the intention of the legislature is to return a company back to a solvent and operational state.[351] While the Act appears to be more inclusive, 'affected persons' such as shareholders are still given inadequate protection.[352] Shareholders are limited in their capacity as 'affected persons' and are not afforded the protection that creditors and employees enjoy. The Act seeks to balance the rights of affected parties but has incidentally failed to protect shareholders in a manner that is adequate and just.

The goal under business rescue is to ensure that a business has returned to a solvent status and that would be provide a better outcome for creditors than liquidation.[353] A company that ceases to exist would have a knock-on effect on the economy, as the company itself would

344 Loubser op cit note 3 at 137.
345 S 5(1) of the Companies Act.
346 S 7(k) of the Companies Act.
347 Bradstreet op cit note 77 at 376.
348 S 129 of the Companies Act.
349 S 131 of the Companies Act.
350 S 128(1) of the Companies Act.
351 Section 7(k) of the Companies Act; Bradstreet op cit note 77 at 353.
352 Loubser op cit note 38.
353 S 7(k) of the Companies Act: Rushworth op cit note 76 at 376.

not be contributing to the economy as well the employees, through tax and other forms of spending. Employees who are due any money in terms of services rendered will become super-preferent creditors and rank even higher than normal creditors.

While it appears that employees are well protected, it could also be to the detriment of the rescue mechanism. The case in point is the case of *Ziegler*[354] where the airline was factually insolvent.[355] The order to commence rescue proceedings was granted, based on the interests of the employees as being one of the considerations, as the application was not opposed by the government, employees, or creditors.[356] The court looked at the purpose in section 7(k) of the Act found that it was just and equitable to grant the order.[357]

The Act provides wide protection to creditors and employees, but fails to adequately protect shareholders.[358] They are mentioned as affected persons but shareholders do not play an active role in business rescue proceedings. Shareholders cannot vote with regard to the rescue unless their rights are affected.[359] This means that shareholders who have a significant holding-stand to lose. The current position would deter future shareholders from investing in companies as the risk of their loss is high without adequate protection from the Act.

I submit that the legislation provides more protection to shareholders by adopting the suggested approach in the King II Report, as shareholders are 'affected persons' but do not vote in respect to the business rescue plan. Shareholders are informed of the rescue proceedings but remain passive in proceedings, unless their rights are affected. King II follows the 'enlightened shareholder value approach' which means that the director must promote the success of the company for the benefit of the company and to generate maximum value for the shareholders.[360] The suggested approach would not deter shareholders from investing in companies because of their fear of losing when a company is under business rescue.

A business that is under business rescue has an effect on other parties, such as property owners. The legal position regarding property owners is that the property owner can cancel a

354 *Ziegler* supra note 17.
355 M F Cassim 'South African Airways makes an emergency landing into business rescue: Some burning issues' (2020) 137(2) *SALJ* 201–214 at 203.
356 *Ziegler* supra note 17 para 45.
357 Ibid para 46.
358 Loubser op cit note 38 at 373.
359 Ibid at 379.
360 Esser op cit note 175 at 193.

lease agreement where there has been a breach and that this will not amount to an 'enforcement action' as prohibited by section 133(1) of the Act.[361]

A business rescue practitioner also has the power to suspend obligations in terms of section 136(2) of the Act. This suspension has the effect of giving the company some 'breathing space' in terms of rental payments, and the company will not be breach of their agreement with the landlord.[362] Cancellation does not give the property owner a right to reclaim his property, and the rationale behind this is that if the property were repossessed, the business would have no place to operate.

The rationale behind the moratorium is to create protection for the company and to allow them to return to an operational state, but it is argued that the courts are applying the moratorium incorrectly. It is argued that the moratorium does not provide adequate protection to a company under business rescue. It is submitted that legislation should be amended to allow a business rescue practitioner to cancel a lease agreement without requiring a court order, and by including unpaid rent in the costs of business rescue.[363]

The Act has carefully placed mechanisms in place, in order to enable a company to return to a solvent and operational state as there is more value in rescuing a business rather than liquidating a company that has prospects of success.[364] The employees play a vital role in the rescue proceedings, and are also a consideration for the courts when granting the order to commence rescue proceedings. Notably, this protection and involvement becomes difficult when it comes to the actual rescuing of the company. It is argued that the primary goal of business rescue is not to save jobs, the primary goal should be to rehabilitate and rescue the business.

Retaining jobs should be a consequence of business rescue.[365] I submit that employees, like shareholders, also have a significant amount to lose as a result of liquidation. Employees have rights, as employees and as 'affected persons'. The purpose of business rescue is to find a balance between all the affected persons. However, employees enjoy protection in terms of the Companies Act, the LRA, and have rights as creditors. This indicates that employees have

361 *Cloete Murray* supra note 72 para 36.
362 Cassim op cit note 260 at 422; Cloete Murray supra note 72 para 34.
363 Lawrenson op cit note 265 at 670.
364 *Oakdene* supra note 43 para 12; A O Nwafor 'Exploring the Goal of Business Rescue through the Lens of the South African Companies Act 71 of 2008' (2017) 28 *Stell LR* 597–613 at 605.
365 E P Joubert *A Comparative study of the effects of liquidation or business rescue proceedings on the rights of the employees of a company* (unpublished LLD thesis, UNISA, 2018).

the ability to play a major role in business rescue proceedings, and without the best interest of the company, this could mean that the business rescue attempts could be in vain due to excessive rights given to a particular class of affected persons.

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