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**AFFECTED PERSONS IN BUSINESS RESCUE  
PROCEEDINGS: HAS A BALANCE BEEN  
STRUCK?**

By

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## CHAPTER 1: INTRODUCTION

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### 1.1 HISTORICAL BACKGROUND

South African corporate law has provided a rescue procedure for financially distressed companies as far back as 1926 when judicial management was introduced by the Companies Act 24 of 1926. The judicial management system also provided for under the Act 61 of 1973<sup>1</sup>, remained relatively unchanged from its inception in the 1926 Act.

Prior to the enactment of the Companies Act 71 of 2008 (“the 2008 Act”) financially distressed companies were either liquidated or placed under judicial management, Judicial management was soon criticized as a dismissal failure. *Le Roux Hotel Management (Pty) Ltd v E Rand (Pty) Ltd*<sup>2</sup>, Josman J referred to judicial management as ‘a system which has barely worked since its initiation in 1926’.

As a result of judicial management’s failure, it become apparent that there was a need for a system of corporate rescue appropriate to the needs of a modern South African economy and one that is in alignment with those international jurisdictions such as the United States of America, the United Kingdom and Australia.

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<sup>1</sup> Companies Act 61 of 1973.

<sup>2</sup> *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).

## 1.2 GENERAL INTRODUCTION

The legislature introduced a new business rescue regime when the companies Act of 2008 (the 2008 act) came into effect in the South African law, this new act remarkably changed corporate law. The 2008 act was drafted with certain expressed objectives to ensure an efficient business rescue process that would facilitate the rescue and rehabilitation of a business entity in financial difficulty in a way that would secure and balance the opposing interests of creditors, shareholders and employees.<sup>3</sup>

The 2008 Act states ‘that one of the main objectives with regards to business rescue is ensuring that the procedure balances the competing interests involved. The purpose of this dissertation is to consider to what extent the 2008 Act has been able to achieve this’<sup>4</sup>; as far as the rights of employees, shareholders and creditors are concerned. This dissertation will contend that, although the provisions are commendable, the procedure has failed to strike a proper balance in empowering certain stakeholders more than the others. It will be argued that if the business rescue procedure goes too far in providing for the protection of the employees of a failed company, this may eventually be to the detriment of the employees. Joubert et al submit that

‘This is especially so if the protection granted corresponds with the over-burdening of the new owner (employer), or the excessive erosion of the rights of creditors, such as banks, that hold the key to the company's credit lifeline. If these important stakeholders are deterred from investing by an unbalanced procedure, the corporate rescue legislation could become counter-productive.’<sup>5</sup>

The overall conclusion reached is that even though the objectives of the 2008 Act are admirable in what they strive to achieve, leave a wide gap regarding their practicality, much work still needs to be done to rid this much-needed procedure of its flaws, to ensure that the objectives of the 2008 Act are achieved.

## 1.3 PROBLEM STATEMENT & RESEARCH OBJECTIVES

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<sup>3</sup> Companies Act 71 of 2008.

<sup>4</sup>M Zwane “Affected Persons in Business Rescue Proceedings: Has a Balance Been Struck?” (University of Cape Town) (2015).

<sup>5</sup> T Joubert, S Van Eck & D Burdette ‘The expected Impact of Labour Law on South Africa’s New Corporate Rescue Mechanism’ (2011) 27 (1) *Intl. J. Comp. Lab. L. & Indus. Rel.* 65.

The 2008 Act came with several amendments; one of its central features was the introduction of the topic of business rescue in chapter six. Having been implemented in 2008 business rescue remains a relatively new topic in South Africa, one to be explored and constructively criticized.

The purpose of this dissertation as mentioned above is to explore one of the stated objectives of the 2008 Act, namely the provision for the efficient rescue and recovery of financially distressed companies in a manner that balances the rights and interests of all relevant Stakeholders.<sup>6</sup>

“Affected persons” in relation to a company, means a shareholder or creditor of the company, any registered trade union representing the employees of the company and if any of the employees of the company are not represented by a registered trade union, each of those employees or their respective representatives. The question that I will consider in this dissertation is whether the legislature has succeeded in striking an appropriate balance between the protection of the rights of the employees on the one hand, and actually saving the company or its business on the other.

#### 1.4 DELINEATIONS & LIMITATIONS

The focus of this dissertation will be on the aspects which pertain to affected persons in business rescue proceedings. The general rights afforded to affected persons and the possible effect they have on other affected persons will be discussed extensively. As mentioned above business rescue is still a novelty in our law so there is not an abundance of judicial pronouncements on the procedure although recently the courts have been plagued by competing applications for business rescue on the one hand and liquidation on the other, with that said I will mostly rely on academic articles available online.

#### 1.5 RESEARCH METHOD & CHAPTER OVERVIEW

1.5.1 A general desk top research will be conducted; the current legislation will be used as a starting point, information will be gathered from available case law, literature in the form of academic journal articles will be used to gather a more overall perspective. The

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<sup>6</sup> Companies Act 71 of 2008 (section 7k).



online database will mostly be used to collect the information, and where necessary hard copy secondary sources will be consulted.

1.5.2 This thesis will take the form of five chapters; each chapter will have an introduction and sub-headings. The summary of the chapters will be as follows;

**Chapter 1- Introduction**, this chapter introduces the research questions and how it shall be answered. It gives a brief background and indicates the conclusion that will be reached;

**Chapter 2- Creditors**, this chapter discusses creditors, the rights afforded to them in the business rescue process and the extent of their participation in the process. It examines whether the new business rescue procedure still adequately provides and protects them considering the broader purposes of the 2008 act.

**Chapter 3 – The Role of Shareholders in Business Rescue Proceedings**, this chapter deals with the rights of shareholders as affected person's and will examine to what extent the new corporate rescue allows for their participation and involvement, and whether business rescue will significantly improve the position of shareholders in the corporate rescue regime.

**Chapter 4- Employees**, this chapter will deal with the rights afforded to employees as affected person's and will examine to what extent the new corporate rescue allows for their participation and involvement, and whether business rescue has in fact gone far and beyond in trying to protect the interests of employees at the expense of the other stakeholders.

**Chapter 5- Conclusion**, this chapter will discuss the conclusion reached on the balancing exercise and an overall conclusion on the topic at hand.

## CHAPTER 2: CREDITORS

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### 2.1 THE GENERAL MORATORIUM

The commencement of the business rescue process results in the immediate limitation of the rights of creditors because once the court grants the order for business rescue, automatically there comes into force a general moratorium which suspends all legal proceedings or enforcement actions against the company.

The 2008 Act<sup>7</sup> provides that during business rescue proceedings, no legal proceedings, including enforcement action, against the company, or in relation to any property belonging to the company, or lawfully in its possession, may be commenced or proceeded with in any forum, except;

- (a) with the written consent of the practitioner<sup>8</sup>;
- (b) with the leave of the court and in accordance with any terms the court considers suitable<sup>9</sup>;
- (c) as a set-off against any claim made by the company in any legal proceedings, irrespective of whether those proceedings commenced before or after the business rescue proceedings began<sup>10</sup>;
- (d) criminal proceedings against the company or any of its directors or officers<sup>11</sup>;
- (e) proceedings concerning any property or right over which the company exercises the powers of a trustee;<sup>12</sup> or
- (f) proceedings by a regulatory authority in the execution of its duties after written notification to the business rescue practitioner.<sup>13</sup>

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<sup>7</sup> Companies Act 71 of 2008 Section 133 (1).

<sup>8</sup> Section 133 (1) (a).

<sup>9</sup> Section 133 (1) (b).

<sup>10</sup> Section 133 (1) (c).

<sup>11</sup> Section 133 (1) (d).

<sup>12</sup> Section 133 (1) (e).

<sup>13</sup> Section 133 (2) (f).

During business rescue proceedings, a guarantee or surety by a company in favour of any other person may not be enforced by any person against the company except with leave of the court and in accordance with any terms the court considers just and equitable in the circumstances.<sup>14</sup>

If any right to commence proceedings or otherwise assert a claim against a company is subject to a time limit, the measurement of that time must be suspended during the company's business rescue proceedings.<sup>15</sup>

It is clear from the above that creditors are prohibited from pursuing their claims against the company, because of this limitation, the legislature granted creditor's rights which enable them to play an important role in the business rescue process.

The business rescue proceedings do not have an automatic termination or an allocated time period, alternative methods of termination include setting aside of the resolution or where in terms of section 131(2) (a), the proceedings have been converted into liquidation proceedings. Wassman alludes to the consequences or effects of an indefinite business rescue on affected persons and in particular, creditors. He submits that the moratorium has the effect of suspending and preventing any legal proceedings. He states further that while this may provide some breathing space for the company to re-arrange its debts and financial structures it provides no relief for any aggrieved party as the moratorium can potentially continue indefinitely.<sup>16</sup>

Although the moratorium is a blatant infringement on the rights of creditors, it is essential in order to achieve financial stability. If claims against a financially distressed company were allowed during the process, then the business rescue proceedings would be a fruitless effort. The Supreme Court of Appeal (SCA) in the recent judgment of *Cloete Murry*<sup>17</sup> acknowledged that 'a moratorium on legal proceedings against a company under business rescue, is of cardinal importance since it provides the crucial breathing space or a period of respite to enable a company to restructure its affairs and that, it was aptly described moratorium is a cornerstone of all business rescue procedures.' The court in this case was faced with the issue of determining the proper meaning of s 133(1), particularly the correct interpretation of the term '... no legal proceeding, including enforcement action, against a company under business rescue may be commenced.' It was argued that a cancellation of an agreement by the creditor constituted an 'enforcement action' as meant in s 133(1) by the liquidators and thus the absence

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<sup>14</sup> Companies Act 71 of 2008 Section 133 (2).

<sup>15</sup> Companies Act 71 of 2008 Section 133 (3).

<sup>16</sup> B Wassman 'Business rescue: getting it right.' De Rebus, Jan/Feb 2014:36 (2014).

<sup>17</sup> *Cloete Murray and Another NNO v FirstRand Bank Ltd t/a Wesbank* 2015 (3) SA 438 (SCA).

of the written consent by the business practitioner or leave of the court meant that the cancellation was of no force or effect. After considering the wording of the section Fourie AJA held that ‘the concepts of “enforcement” and “cancellation” are traditionally regarded as mutually exclusive. “Cancellation” means the termination of obligations between parties to an agreement and cannot be interpreted to mean enforcement action as envisaged under s133(1)’.<sup>18</sup>

This means a creditor of the company may cancel an agreement if such company is in breach of the contract, it will not according to s 133(1) be regarded as an enforcement action falling under the notion of moratorium.

In the judgement of *Chetty v Hart*<sup>19</sup> the court was faced with the question of whether an arbitration proceeding while a distressed company is under supervisor constituted ‘legal proceedings’ it was held that in terms of s133 (1) of the act the moratorium on a company did not affect the arbitrator’s jurisdiction to adjudicate a claim where one of the parties was in business rescue. Here the one party had applied to court in attempt to have an arbitration order set aside contending that it is invalid because the company had commenced business rescue proceedings when such arbitration award was made. This decision by the Supreme Court Appeal (SCA) gives creditors hope because it shows that courts are not prepared to apply s131 (1) loosely and they will not allow this section to be used as an escape goat of the company’s obligations during business rescue.

## 2.2 GENERAL PARTICIPATION RIGHTS GIVEN TO CREDITORS

The interests of affected persons are recognized and their participation in the development and approval of a business rescue plan is extensively provided for. The rights of creditors are similar in most respects to those of the employees, and include the right to participate in court proceedings and discussions on the business rescue plan and to vote on the plan.

Understandably the creditors of the company may see business rescue proceedings as a ploy and as a futile attempt to salvage a doomed company and they may take the view that the company should just be put into liquidation rather than waste time and money trying to save it.<sup>20</sup> To prevent potential for abuse of the process, an affected person may apply to court for an order setting aside the resolution, on the grounds that there is no reasonable basis for believing

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<sup>18</sup>*Cloete Murray and Another NNO v FirstRand Bank Ltd t/a Wesbank* 2015 (3) SA 438 (SCA). para 33.

<sup>19</sup> *Chetty v Hart* (SCA) (unreported case no 20323/2014, 4-9-2015) (Cachalia JA); “Beware the double-edged sword in litigation with a company in business rescue.” *De Rebus*, Jan/Feb 2016:36 [2016] DEREBUS 25.

<sup>20</sup> R C Williams, “chapter 6 Business Recue and Compromise with Creditors” 2013.

that the company is financially distressed or that there is a reasonable prospect for rescuing the company<sup>21</sup> or that the company has failed to satisfy the procedural requirement.

This means the creditors as “affected persons” have the right to apply to court to have the resolution which initiated the business rescue proceedings set aside on the grounds above-mentioned and if the creditors manage to persuade the court, then it can make an order placing the company in liquidation.

During business rescue proceedings, each creditor is entitled to notice of, and participation in, each court proceeding, decision or meeting. Participation may be formal or informal. They have the right to vote to amend, approve or reject a proposed business rescue plan. Creditors may form a creditor’s committee and are entitled to consult with the practitioner during the preparation of the business rescue plan, but may not instruct or direct the practitioner.<sup>22</sup>

*Southern Palace Investment*<sup>23</sup> is said to be one of the most important cases on business rescue. It was one of the first cases that dealt with business rescue, the case specifically dealt with the ‘reasonable prospect’ requirement. Eloff AJ stated the use of different language in the 2008 act is an indication that the requirement in business rescue is less stringent than the one required in terms of s247(1) of the 1973 act which was a ‘reasonable probability’. Eloff AJ emphasized that ‘something less’ is required in the case of business rescue, this is because of a different mind-set that is in alignment with the objectives of business rescue.<sup>24</sup>

After examining the facts before him, Eloff AJ stated that when looking at the information presented to the court there was, on the vague and undetailed information before him, no reason to believe that there was any prospect of the business of the respondent being restored to a successful one. There was not even a concrete plan available for consideration.<sup>25</sup>

It is submitted that the courts’ use of the phrase “successful one”, the court applied a burden of proof that was required in terms of judicial management and thus completely neglected to examine the alternative objective contained in s128 (b) (iii).<sup>26</sup>

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<sup>21</sup> Companies Act 71 of 2008.

<sup>22</sup> Companies Act 71 of 2008 Section 149 (1) (a).

<sup>23</sup> *Southern Palace Investment 265 (Pty) Ltd v Midnight Storm investments 386 Ltd 2012 (2) SA 423 (WCC) 49-50.*

<sup>24</sup> *Southern Palace Investment 265 (Pty) Ltd v Midnight Storm investments 386 Ltd 2012 (2) SA 423 (WCC) 21.*

<sup>25</sup> *Southern Palace Investment 265 (Pty) Ltd v Midnight Storm investments 386 Ltd 2012 (2) SA 423 (WCC) 23.*

<sup>26</sup> Joubert EP “‘Reasonable possibility’ Versus “Reasonable prospect”: Did business rescue succeed in creating a better test than judicial management?’ (2013) 76 *THRHR* 550-563.

In conclusion, the court remarked that when faced with the question of whether there is a ‘reasonable prospect’ one needs to look at various factors with each case examined on its own merits. These factors must go beyond looking at a mere possibility of success and the information provided must also go beyond mere speculation.

This judgment has been criticized for putting the “benchmark too high” rightfully so however this strict approach by the court is necessary for the prevention of abuse by certain stakeholders. The requirement of business rescue ought to be proven before the application for business rescue is granted because it has an effect on several stakeholders whose interests must be considered by the court to ensure that the objectives of the act are upheld.

### 2.3 THE CREDITORS’ COMMITTEE

The committee must act independently of the practitioner to ensure fair and unbiased representation of creditors’ or employees’ interests.<sup>27</sup> A person may be a member of a committee of creditors or employees, respectively, only if the person is; an independent creditor, or an employee, of the company; an agent, proxy or attorney of an independent creditor or employee, or other persons acting under a general power of attorney; or authorized in writing by an independent creditor or employee to be a member.<sup>28</sup>

The formation of this committee is a considerate way to ensure that all the interests of the affected persons are represented and are seen through the process to ensure that a proper balance is struck. One can argue that the practitioner predominately serves the best interest of the company which directly impacts the shareholders of the company.

### 2.4 PROTECTION OF PROPERTY INTERESTS

‘The company is precluded from disposing of its property unless it is in the ordinary course of its business; in a bona fide transaction at arm’s length for a fair value approved in advance or in writing by the practitioner; or in a transaction contemplated within, and undertaken as part of the implementation of, a business rescue plan that has been approved in terms of section 152.’<sup>29</sup>

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<sup>27</sup> Companies Act 71 of 2008 Section 149 (1) (b) and (c).

<sup>28</sup> Companies Act 71 of 2008 Section 149 (2) (a) (b) and (c).

<sup>29</sup> Companies Act 71 of 2008 Section 134 (1) (a).

Any person who, as a result of an agreement made in the ordinary course of the company's business before the business rescue proceedings began, is in lawful possession of any property owned by the company may continue to exercise any right in respect of that property as contemplated in that agreement, subject to section 136; and despite any provision of an agreement to the contrary, no person may exercise any right in respect of any property in the lawful possession of the company, irrespective of whether the property is owned by the company, except to the extent that the practitioner consents in writing.<sup>30</sup>

The practitioner may not unreasonably withhold consent.<sup>31</sup>

This section serves to protect creditors and shareholders by ensuring that the company does not dissipate any of its assets during business rescue proceedings. This provision is especially essential because of the moratorium discussed above.

## 2.5 A BETTER RETURN FOR CREDITORS (OAKDENE CASE)

The key to business rescue will be the successful implementation, if approved by creditors, of a business rescue plan to rescue the company by restructuring its affairs, business, property, debt, other liabilities and equity in a manner that maximizes the likelihood of the company continuing in existence on a solvent basis or, if this is not possible, the implementation should result in a better return for the company's creditors or shareholders than would result from an immediate liquidation.<sup>32</sup>

This alternative objective contained in section 128 (1) (b) (iii) was dealt with by the Supreme Court of Appeal (SCA) in *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd*.<sup>33</sup>

## 2.6 FACTS

The facts of this case are quite complicated. Essentially, *Farm Bothasfontein (Kyalami) (Pty) Ltd* ('the company') was in default on payments to certain creditors, facing imminent

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<sup>30</sup> Companies Act 71 of 2008 Section 134 (1) (b) and (c).

<sup>31</sup> Companies Act 71 of 2008 Section 134 (2).

<sup>32</sup> Companies Act 71 of 2008 Section 128 (1) (b).

<sup>33</sup> *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd* (609/2012) [2013] ZASCA 68 (27 May 2013).

liquidation, the company launched a business rescue application. This application was opposed by Imperial Holdings Ltd and Nedbank Ltd whom were also majority shareholders in the company as a result of past financing transactions.

Nedbank and Imperial Holdings Limited each held 30 percent of shares of the company and were therefore affected persons by virtue of their shareholdings as well as being creditors of the company. ‘Nedbank and Imperial opposed the business rescue application on the simple basis that any proposal put forward by the practitioner will be rejected as, having sixty percent of the vote, they will vote against it’<sup>34</sup>

It is common cause between the parties that Kyalami Pty Ltd derived no income from its assets, thus it was apparent from the facts before the court that a successful rescue would not have been possible. It should be noted that the rights of employees as affected persons did not come into consideration in this matter because the company did not have any employees. The court was thus faced with the question whether to allow access to business rescue proceedings for the purpose of ensuring a better return for the company’s creditors than might be provided by liquidation proceedings.<sup>35</sup>

## 2.7 HIGH COURT

The issue before the court was whether the best results would be obtained by a liquidator selling the immovable property as the only major asset of the company or whether a business rescue practitioner would be able to do better. The applicant’s case was based on the assumption that business rescue proceedings would be able to realise a higher price, whereas a liquidation at a sale in execution would realize a lesser price. The difficulty was that no factual basis had been laid by the applicant’s for justifying such assumptions.<sup>36</sup>

Claassen J<sup>37</sup> laid down 12 distinct reasons for concluding that an order for business rescue was inappropriate in this case however these do not need to be repeated. It sufficient to say that the main amongst those reasons was the expressed intention of the creditors and majority shareholders to vote against any proposed business plan as well as the court’s view that a

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<sup>34</sup> Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others 2012 (3) SA 237 (GSJ) 47.

<sup>35</sup> Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others 2012 (3) SA 237 (GSJ) 15 and 45.

<sup>36</sup> Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others 2012 (3) SA 237 (GSJ) 48.

<sup>37</sup> Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others 2012 (3) SA 237 (GSJ) 49.



liquidator would be best equipped to deal with the litany of issues and complexity of this case, further the court could see no reason why a liquidator would be less successful in realizing a proper market value for the relevant property. Another important factor was what the courts call the balancing exercise, here the court decided that the interests of creditors ought to carry more weight when weighed against those of the company.<sup>38</sup>

## 2.8 SUPREME COURT OF APPEAL (SCA)

The SCA was faced with three issues which it had to consider and decide on. these were;

1. whether the court's decision amounts to exercise of discretion in terms of s131 (4);
2. what the applicant must show to satisfy requirements of 'reasonable prospect' under s131 (4) (a) (iii) and
3. The meaning of 'rescuing the company' under s 131 (4) (a).

For the purposes of this dissertation only the third issue will be considered.

The debate surrounding the third issue arises out of the definition provided for in terms of the 2008 Act under s 128 (1) (h), read with s 128 (1) (b) (iii). According to s 128 (1) (h)<sup>39</sup>, 'rescuing the company' means 'achieving the goals set out in the definition of "business rescue" in paragraph (b)'.

In this light the debate arose whether the fulfillment of the said alternative object of business rescue was sufficient to constitute a successful rescue where the proposed rescue plan provides for the secondary goal only.

The court in its interpretation of s128 (1) (b) stated that 'business rescue' means to facilitate 'rehabilitation', which in turn meant the achievement of one of two goals: (a) to return the company to solvency, or (b) to provide a better deal for creditors and shareholders than what they would receive through liquidation. Further the court stated that this construction coincides with the reference in s 128 (1) (h) to the achievement of the goals set out in s128 (1) (b). The judge placed emphasis on the term 'goals' being a plural term, to drive his point home.<sup>40</sup>

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<sup>38</sup> *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* 2012 (3) SA 237 (GSJ) 49.

<sup>39</sup> Companies Act 71 of 2008 Section 128 (h).

<sup>40</sup> *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd* (609/2012) [2013] ZASCA 68 (27 May 2013) 26.

Accordingly, the court accepted that the achievement of any one of the two goals referred to in s 128 (1) (b) would qualify as 'business rescue' in terms of s131 (4).

After settling the above issue the question quickly turned on whether there was a 'reasonable prospect' present. The court after considering the facts and circumstances of the matter was not convinced that there was a reasonable prospect present. The court explained the difficulty which was also faced by the court *a quo* in that it could see no reason why a business practitioner would be able to obtain a better price for the property than a liquidator. The court stated that the contention appeared to rest on nothing more than speculation.<sup>41</sup>

The court seemed to condone some of the reasons laid down by the high court in its dismissal of the application and added some of its own reasons for dismissing the appellant's arguments. The court in conclusion was of the view that there was a real possibility that liquidation would in fact be more advantageous to creditors and shareholder.

## 2.9 THE BALANCING EXERCISE

Returning to the high court judgment of Oakdene, the court here was faced with the task of juxtaposing the interests of the company and the interests of creditors in order to decide whether to allow access to the procedure.

In light of the circumstances of the case, particularly that there was no "business" of the company to be rescued, the court took the view that the interests of the company should carry more weight. The applicants had emphasized its reliance on the second goal of the act which was accepted as correct by the court after adopting the Australian decision in *Dallinger v Halcha Holdings*<sup>42</sup> however no facts were placed before the court by the applicant in support of its argument in this case. It accordingly failed to show that business rescue would yield a better return for the company's creditors.

The court noted that the goals set out in s128 (1) are 'primarily directed at the prevention of unnecessary liquidations of companies and the consequent loss of its employees' employment', and also remarked that 'employees stand to gain substantial benefits from business rescue proceedings which precede a liquidation'<sup>43</sup>. The court noted further that the new procedure

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<sup>41</sup> *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd* (609/2012) [2013] ZASCA 68 (27 May 2013) 34.

<sup>42</sup> *Dallinger v Halcha Holdings* (1996) 14 ACLC 263, 268.

<sup>43</sup> *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd* (609/2012) [2013] ZASCA 68 (27 May 2013) 15.

'encapsulates a shift from creditors' interests to a broader range of interests' on the rationale that preserving the business as a whole may 'in the end prove to be a better option for creditors'<sup>44</sup>

Claassen J's approach is more favorable because it exhibits the sort of balance envisaged by the 2008 Act. Bradstreet<sup>45</sup> in his analysis of the judgment submits that 'Although employees were not a factor to take into consideration in this case, the court appears to have recognised this principle in relation to stakeholders more broadly, and expressly recognised the interests of creditors in the use of the procedure'.

## 2.10 POST COMMENCEMENT FINANCE

To successfully implement a proposed business rescue plan, the company would most definitely need financial support, in business rescue this support is called post commencement finance which allows the company to carry on business in its time of financial distress.

The 2008 act provides for the elevation of employees claims in that if 'any remuneration, reimbursement for expenses or other amount of money relating to employment becomes due and payable by a company to an employee during the company's business rescue proceedings, but is not paid to the employee will be regarded as post commencement financing'<sup>46</sup> and will have preference over other claims.

Bradstreet correctly points out that 'the prioritisation of the claims of employee creditors is important in ensuring that a struggling business is not faced with the extra burden of potential resignations and desperate employees who have no motivation to work. A guarantee of preference in payment will provide such motivation to employees who may otherwise feel financially pressed to cut their losses and find alternative employment.'<sup>47</sup>

'Where post commencement finance is obtained from creditors other than employee creditors, such 'traditional' post-commencement creditors also obtain priority in repayment by virtue of

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<sup>44</sup> *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd (609/2012) [2013] ZASCA 68 (27 May 2013) 12.*

<sup>45</sup> R 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 *SALJ* 44.

<sup>46</sup> Companies Act 71 of 2008 Section 135 (1).

<sup>47</sup> R Bradstreet, "The new business rescue: will creditors sink or swim?" 2011 *SALJ* 352.

their finance being provided during the business rescue and have preference amongst themselves in the order in which they incurred their claim against the company.<sup>48</sup>

After payment of the practitioner's remuneration and expenses referred to in s143, and other claims arising out of the costs of the business rescue proceedings, all the employees' claims will be treated equally, but will have preference over all claims contemplated in sub-section two of section 135 (3) (a), irrespective of whether or not they are secured; and all unsecured claims against the company.<sup>49</sup>

It is not clear from the section whether or not secured post -commencement claims will rank ahead of unsecured post-commencement claims and further whether creditors who are secured prior to the commencement of business rescue, will rank in the order of preference as determined by section 135 of the 2008 act.

The ranking of claims in a business rescue was clarified and decided in the cases of *Merchant West Capital Solutions (Pty) Ltd*<sup>50</sup> and *Redpath Mining South Africa (Pty) Ltd*<sup>51</sup> as follows:

1. The business rescue practitioner, other professionals for remuneration and costs or expenses of the proceedings;
2. Employees for any remuneration which became due and payable after business rescue proceedings began (post commencement finance);
3. Secured lenders or other creditors for any loan made after business rescue proceedings began (post commencement finance);
4. Unsecured lenders or other creditors for any loan or supply made after business rescue began (post commencement finance);
5. Secured lenders or other creditors for any loan or supply made before business rescue proceedings began;
6. Employees for any remuneration which became due and payable before business rescue proceedings began; and

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<sup>48</sup> R Bradstreet, "The new business rescue: will creditors sink or swim?" 2011 *SALJ* 352.

<sup>49</sup> Companies Act 71 of 2008 Section 135 (3).

<sup>50</sup> *Merchant West Working Capital Solutions (Pty) Ltd v Advanced Technologies & Engineering Company (Pty) Ltd & Another* (2013) ZAGPJHC 109 (10 MAY 2014).

<sup>51</sup> *Redpath Mining South Africa (Pty) Ltd v Marsden N.O & Others* (2013) ZAGPJHC 148.

7. Unsecured lenders or other creditors for any loan or supply made before business rescue proceedings began.

According to these judgements above, both decided upon by Kgomo J, it seems that the claims of secured creditors prior to the commencement of business rescue rank below the claims of both secured and unsecured creditors post the commencement of business rescue. Law practitioners Jones and Wellcome submit that following these judgements ‘would lead to an absurd result that post-commencement financiers who hold no security would be paid out first from the proceeds of the security held by pre-business rescue creditors’<sup>52</sup>

Jones and Wellcome further submit that ‘the above raking cannot be justified in section 135 and that it is irreconcilable with the provisions of section 134 (3) which provide secured pre-commencement creditors with the necessary certainty in respect of their security during business rescue proceedings. They assert that the true position is that secured creditors are entitled to the treatment set out in s134 (3) of the Act. This means that post commencement financing ranks only in priority to all unsecured creditors and that pre-business rescue creditors rights to their security must be respected in terms of section 134 (3) of the act.’<sup>53</sup>

It is important to note that if business rescue proceedings are suspended by a liquidation order, the preference conferred in terms of this section will remain in force, except to the extent that any claims arising out of costs of liquidation.<sup>54</sup>

## 2.11 CONCLUSION

Creditors are granted extensive rights in the business rescue process as affected persons. The proceedings have the effect of limiting the rights of creditors and have a general impact throughout. It is for this reason that their interests are recognized and their participation is extensively provided for. Amongst others creditors have a right to form a creditors committee and the 2008 act also provides for the property interests of the company.

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<sup>52</sup> J Jones and R Wellcome “Business Rescue, Restructuring and Insolvency: The Elephant in The Room-Post-Commencement Financing and Whether Pre-Business Rescue Creditors’ Rights to Their Security are Compromised” 2016.

<sup>53</sup> J Jones and R Wellcome “Business Rescue, Restructuring and Insolvency: The Elephant in The Room-Post-Commencement Financing and Whether Pre-Business Rescue Creditors’ Rights to Their Security are Compromised” 2016.

<sup>54</sup> Companies Act 71 of 2008 Section 135(4).

It is important to keep in mind that while it is fair and acceptable that the interests of creditors are provided for and are given weight in the process, as seen above in court proceedings, particularly by the SCA; one of the reasons why the previous system of judicial management was a dismissal failure was because it was seen as too creditor-centric. It is then crucial that the same mistake is not repeated.

The striking of a balance in the context of this dissertation does not mean the attainment of equal rights, instead it is whether the rights that the stakeholders have been granted adequately reflect their interest in the outcome.

Furthermore, it is to assess whether these rights facilitate a smooth process in the sense that they do not empower certain stakeholders to the extent that they can be unduly obstructive. It is noted that this exact concern was tested in the case of Oakdene regarding two major creditors and shareholders of a company where the two declared they intention to oppose any business rescue plan proposed and the high court dismissed the application for business rescue for this reason. In argument before the SCA the appellants criticized the high court for dismissing the application merely because the major shareholder and creditor expressed their intention to oppose any business plan, with authority sought from a statement made in *Nedbank Ltd v Bestvest*<sup>55</sup> at the paragraph 55 of the judgement.<sup>56</sup> The SCA in Oakdene took the time to correctly state its view on the matter as follows:

If the statement is intended to convey that the declared intent to oppose by the majority creditors should in principle be ignored in considering business rescue, I do not agree. As I see it, the applicant for business rescue is bound to establish reasonable grounds for the prospect of rescuing the company. If the majority creditors declare that they will oppose any business rescue scheme based on those grounds, I see no reason why that proclaimed opposition should be ignored. Unless, of course, that attitude can be said to be unreasonable or mala fide.<sup>57</sup>

This above statement confirms that the courts are fair and reasonable when faced with a business rescue application and that they will prevent any undue obstruction or mala fide intentions.

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<sup>55</sup> *Nedbank Ltd v Bestvest 153 (Pty) Ltd; Essa v bestvest 153 (Pty) Ltd* 2012 (5) SA 497 (WCC) 55.

<sup>56</sup> *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd* (609/2012) [2013] ZASCA 68 (27 May 2013) para 37.

<sup>57</sup> *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd* (609/2012) [2013] ZASCA 68 (27 May 2013) 38.

Chapter six seems to have the interest of creditors provided for adequately and has proven to be creditor-friendly. However, there is still potential for concern with regards to post commencement financing which severely infringes the rights of pre-commencement creditors, particularly that authorization by the older creditors is not required for the company to make new creditors even though ultimately it affects the pre-commencement creditors. This preference for repayment may be of significant deterrence to post commencement creditors because they come third to employee creditors and the business rescue practitioner.

Creditors in the new business rescue still have much influence in the process, one can safely say that one of the keys to a successful business rescue is the sufficient protection of the interests of creditors.

## **CHAPTER 3: THE ROLE OF SHAREHOLDERS IN BUSINESS RESCUE PROCEEDINGS**

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Shareholders as affected persons, as defined, are afforded rights in the business rescue process. Shareholders' participation in the process is limited unlike the participation allowed to creditors and employees. It is submitted that shareholders' have a real reason to be involved in the corporate rescue procedure because they have a financial interest in the outcome. A successful rescue will revive their shares, with these shares regaining at least some of their previous value.<sup>58</sup>

This chapter will discuss the rights afforded to shareholders in the business rescue process, participation and the possible influence they have in the outcome of the procedure. It will examine to what extent the new corporate rescue allows for their participation and involvement, and whether the business rescue procedure will meaningfully improve shareholders position in the corporate rescue regime. Previously shareholder's rights have always been put before the rights of creditors in the corporate rescue proceedings.

### **3.1 GENERAL PARTICIPATION RIGHTS**

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<sup>58</sup> A Loubser 'The Role of Shareholders during Corporate Rescue Proceedings: Always on the Outside Looking In?' (2008) 20 SA Merc LJ372. Page 372.

During a company's business rescue proceedings, each holder of any issued security of the company has the following rights;

- a. to receive notice of each court proceeding, decision, meeting or other relevant event concerning the business rescue proceedings<sup>59</sup>;
- b. participate in any court proceedings arising during the business rescue proceedings<sup>60</sup>;
- c. formally participate in a company's business rescue proceedings to the extent provided for in this Chapter<sup>61</sup>;
- d. vote to approve or reject a proposed business rescue plan in the manner contemplated in section 152, if the plan would alter the rights associated with the class of securities held by that person<sup>62</sup>; and
- e. if the business rescue plan is rejected, to;
  - (i) propose the development of an alternative plan, in the manner contemplated in section 153; or
  - (ii) present an offer to acquire the interests of any or all the creditors or other holders of the company's securities in the manner contemplated in section 153.<sup>63</sup>

On the face of it shareholders are afforded the same rights as the other affected persons. Loubser<sup>64</sup> argues that although shareholders of the company are given formal recognition as affected persons in the business rescue procedure and have the right to be notified of important events, and to participate in court procedures, their position has not improved very much in real terms.

The reference in the definition of business rescue to a better return for the company's creditors and shareholder implies that the interests of shareholders are equal to those of creditors. I submit that this isn't the case but should be the case considering that shareholders have just as much of a financial interest in the outcome as creditors do. In *Swart v Beagles*<sup>65</sup> the court was faced with the first application for business rescue, where an application was brought to court by the sole director and shareholder of the company to place the company in business rescue. In interpreting the phrase "reasonable prospect" contained in s131 (4) Makgoba J looked to the

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<sup>59</sup> Companies Act 71 of 2008 Section 146 (a).

<sup>60</sup> Companies Act 71 of 2008 Section 146 (b).

<sup>61</sup> Companies Act 71 of 2008 Section 146 (c).

<sup>62</sup> Companies Act 71 of 2008 Section 146 (d).

<sup>63</sup> Companies Act 71 of 2008 Section 146 (e) (i) (ii).

<sup>64</sup> A Loubser 'The Role of Shareholders during Corporate Rescue Proceedings: Always on the Outside Looking In?' (2008) 20 SA Merc LJ372.

<sup>65</sup> *Swart v Beagles Run Investments 25 (Pty) Ltd* (2011) 5 SA 422 (GNP).



old companies act to determine whether the company in question had a “reasonable prospect” of becoming a ‘successful concern’<sup>66</sup> after the proposed business rescue proceedings. This approach by the court was criticized because the new business rescue procedure does not contain the words ‘successful concern’ as part of the recovery requirement.<sup>67</sup> In the 2008 act “rescuing the company” is defined in section 128(i)(h) and this section explains the objectives of the act. In terms s 128(i)(h) a successful business rescue is not limited to the company becoming a successful concern as contained in the 1973 act. ‘According to section 128 (b) (iii) the company’s continued existence to a solvent basis in not the only requirement of business rescue. The section provides for an alternative’.<sup>68</sup> Where business rescue procedure can yield a better return for creditors and shareholders of the company than what they would receive under liquidation proceedings, this will be regarded as a successful rescue.<sup>69</sup> Bradstreet submits that in terms of business rescue procedure ‘rescuing’ the company does not mean saving the distressed company at all cost, but rather making an appropriate use of the procedure to facilitate an outcome that is in the interests of all stakeholders.<sup>70</sup>

The court in this case only dealt with the first objective of the act, it is a pity that the second or alternative objective was not argued before the court because it would have been interesting to see the court’s interpretation of section 128 (b) (iii). The court ultimately refused the application stating that there was ‘no basis for contending that the company would be able to carry on business on a solvent basis or that there was any prospect thereof.’<sup>71</sup>

The court took a narrow approach in interpreting the provisions of business rescue. It could be that Makgoba J decided to adopt a cautionary approach because at the beginning of the judgement he acknowledged the fact that business rescue was a novelty in our law, be that as it may, what it seems like is that the court applied an old mind set placing the creditor’s interest above those of other stakeholders.

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<sup>66</sup> Companies Act 61 of 1973 section 427.

<sup>67</sup> Joubert EP “‘Reasonable possibility’ Versus “Reasonable prospect”: Did business rescue succeed in creating a better test than judicial management?’ (2013) 76 *THRHR* 550-563.

<sup>68</sup> Joubert EP “‘Reasonable possibility’ Versus “Reasonable prospect”: Did business rescue succeed in creating a better test than judicial management?’ (2013) 76 *THRHR* 550-563

<sup>69</sup> Companies Act 71 of 2008 Section 128 (b) (iii).

<sup>70</sup> R 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) *SALJ* 44-52.

<sup>71</sup> *Swart v Beagles Run Investments 25 (Pty) Ltd* 2011 5 SA 422 (GNP).

In the case of *Oakdene*<sup>72</sup> which is discussed extensively in the previous chapter, here the court was faced with the task of juxtaposing the interests of creditors and the interests of the company. The court found after weighing the circumstances of the case that the interests of creditors should carry more weight than that of the companies. I submit that the interest of the company is also the interest of the shareholders, this is because shareholders have a capital investment in the company and that their interests is based largely on the companies continued existence on a solvent basis.

In view of the reliance placed on the dictum of the Australian case of *Dallinger v Halcha Holdings*<sup>73</sup> mentioned in chapter two above, which refer to creditors and the decision in *Oakdene*, the implication is that the second goal emphasizes the interest of the company's creditors above its shareholders.

As an affected person, a single shareholder is authorised to bring an application to begin business rescue proceedings as seen in the case of *Beagles Run* discussed above, however Loubser<sup>74</sup> states that

‘it is doubtful whether a shareholder will find it possible to prove any of these grounds without the co-operation of the directors: proving financial distress requires information not immediately at the disposal of a member, even if he suspects that the company is in trouble, and given our existing case law on the just and equitable requirement for judicial management, it seems unlikely that any court will find it just and equitable to commence rescue proceedings on the application of a shareholder, particularly if opposed by a creditor.’

It is doubtful whether anyone will argue with this statement considering the approach taken by courts in business rescue applications thus far, affected persons that have been successful in bringing such applications so far have been the creditors and employees or trade unions respectively.

In the case of *Francis Edward Gormely*<sup>75</sup>, Gormley, a major shareholder of the company, applied for the company's business rescue. ‘The court made it clear that in the event where the objective of the application comes down to the benefit derived from the moratorium under

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<sup>72</sup> *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd*. (609/2012) [2013] ZASCA 68 (27 May 2013).

<sup>73</sup> *Dallinger v Halcha Holdings* (1994) 14 ACLC 236.

<sup>74</sup> A Loubser ‘The Role of Shareholders during Corporate Rescue Proceedings: Always on the Outside Looking In?’ (2008) 20 SA Merc LJ372.

<sup>75</sup> *Francis Edward Gormely v West City Precinct Properties (Pty) Ltd* 19076/11 (WCC) 18 April 2012.

section 128(a)(ii) and the realisation of assets over a three to five-year period, it cannot be within the object contained in section 128(a)(iii)<sup>76</sup>. Further the court indicated that not a single fact was put forward to prove that there was a reasonable prospect that the company will be able to carry on business on a solvent basis or that the business rescue plan will yield a better result for creditors and shareholders than liquidation, only generalisations were put forward. This judgement is consistent with the submissions made above that it may be difficult for shareholders to prove that there is a reasonable prospect that exist, without the support of the company's management and or creditors. The necessary information, such as financial records of the company in most cases will not be easily available to shareholders.

Shareholders have the right to vote to approve or reject a proposed business rescue plan, only if, the plan would alter the rights associated with the class of securities held by that person. This means if the business rescue plan does not propose to alter these rights, then the right to vote falls away even though any business rescue plan will ultimately affect the interests of shareholders. Loubser<sup>77</sup> asserts that

‘the supervisor is unlikely to consult the shareholders because the general body of members do not have the power to accept or reject the plan or even influence the outcome. Employees however have been granted the rights to address and make submissions to the meeting of creditors convened to consider the rescue plan, and can therefore exert a substantial influence on the way the creditors vote. Shareholders whose rights will not be directly affected are basically ignored.’

Williams<sup>78</sup> in his commentary states that ‘this provision creates a valuable short cut’ respectfully I must disagree with this point, yes it creates a shortcut, but this is done so at the expense of the general shareholders, who have just as much right to be included as the other stakeholders.

It has been submitted that the key to a successful business rescue is the implementation of an efficient business rescue plan, if approved by creditors. considering the provisions of business rescue pertaining to the development of a business rescue plan I wonder if shareholders have any meaningful influence in the development of the plan. The act provides that if the proposed plan is rejected than there is an opportunity for shareholders to propose the development of an

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<sup>76</sup> Joubert EP ‘“Reasonable possibility” Versus “Reasonable prospect”: Did business rescue succeed in creating a better test than judicial management?’ (2013) 76 *THRHR* 550-563.

<sup>77</sup> A Loubser ‘The Role of Shareholders during Corporate Rescue Proceedings: Always on the Outside Looking In?’ (2008) 20 *SA Merc LJ*372.

<sup>78</sup> RC Williams ‘chapter 6 Business rescue and compromise with creditors’ 2013.

alternative plan or to acquire the interest of any or all the creditors or other holders of the company's securities in the manner contemplated in section.<sup>79</sup> Again here the chance to propose an alternative plan would accrue only if the rejected plan had proposed to alter the rights associated with the class of securities of those shareholders, at least this seems to be the logical interpretation of the section.

The above-mentioned provision which allows affected persons to make an offer to purchase the votes of any person who has opposed the adoption of the business rescue plan, at a value determined by an independent expert and based on the fair and reasonable estimate of the return that such person would receive on liquidation of the company, is one provision that will be of use to shareholders.

### 3.2 RIGHTS OF SHAREHOLDERS IN RELATION TO THE BUSINESS RESCUE PLAN

Section 137(1) prohibits an alteration in the classification or status of any issued securities of a company during business rescue proceedings, other than by way of a transfer of securities in the ordinary course of business unless the court directs otherwise or it is contemplated in an approved business rescue plan.<sup>80</sup> If the business rescue plan purports to have such an effect, shareholders must approve the plan before it is adopted. In preparing the plan, the practitioner is compelled to consult with all affected persons<sup>81</sup>

Shareholders do not have the right to form a shareholders meeting but creditors and employees do. Some have argued that there is no need for such a committee as shareholders partake in general meetings of the company but I would submit that a committee meeting during business rescue is very much different to the company's usual meetings. What is important about the committee meetings is that stakeholders get the opportunity to discuss and voice their opinions to the practitioner about concerns they may have about the business rescue plan and the procedure. Most importantly stakeholders are present to ensure that their interests are protected. Without the opportunity to consult with the business rescue practitioner the general body of shareholders will mostly be left in the dark.

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<sup>79</sup> Companies Act 71 of 2008 Section 146 (e) (i) (ii).

<sup>80</sup> Companies Act 71 of 2008 Section 137.

<sup>81</sup> Companies Act 71 of 2008 Section 150(1).

### 3.3 ADOPTION OF THE BUSINESS RESCUE PLAN

In the event that a proposed business rescue plan purports to alter any class of holders of the company's securities then the practitioner must immediately hold a meeting of holders of the class, or classes of securities whose rights would be altered by the plan, and call for a vote by them to approve the adoption of the proposed business rescue plan.<sup>82</sup> if, in a vote contemplated, a majority of the voting rights that were exercised support adoption of the plan, it will have been finally adopted, subject only to satisfaction of any conditions on which it is contingent; but if the adoption of the plan is opposed, the plan is rejected, and may be considered further only in terms of section 153.<sup>83</sup>

A business rescue plan that has been adopted is binding on the company, and on each of the creditors of the company and every holder of the company's securities, whether or not such a person was present at the meeting or voted in favour of adoption of the plan.<sup>84</sup>

if the business rescue plan was approved by the shareholders of the company the practitioner may amend the company's Memorandum of Incorporation to authorise, and determine the preferences, rights, limitations and other terms of, any securities that are not otherwise authorised, but are contemplated to be issued in terms of the business rescue plan.<sup>85</sup>

A pre-emptive right of any shareholder of the company will not apply with respect to an issue of shares by the company in terms of the business rescue plan unless an approved business rescue plan provides otherwise.<sup>86</sup>

Binns-Ward J correctly point out that

'it is the task of a business rescue practitioner, after he is appointed to draft a business plan, to indicate whether there is a reasonable prospect that the company will be able to carry on business on a solvent basis after the business rescue plan was implemented or that the business rescue plan will enable creditors and shareholders to receive a better result from the rescue proceedings than would be the case in liquidation.'<sup>87</sup> In light of this passage one would argue

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<sup>82</sup> Companies Act 71 of 2008 Section 152(3)(c)(i).

<sup>83</sup> Companies Act 71 of 2008 Section 152(3)(c)(ii) (aa)(bb).

<sup>84</sup> Companies Act 71 of 2008 Section 152 (4).

<sup>85</sup> Companies Act 71 of 2008 Section 152 (6)(b).

<sup>86</sup> Companies Act 71 of 2008 Section 152 (7).

<sup>87</sup> *Koen & another v Wedgewood Village Golf & Country Estate (Pty) Ltd* 2012 (2) SA 378 (WCC); Joubert EP "Reasonable possibility" Versus "Reasonable prospect": Did business rescue succeed in creating a better test than judicial management? (2013) 76 *THRHR* 550-563.

that it imperative that shareholders are given a seat at the table, to consider and vote on the adoption of the business rescue plan regardless of whether or not the proposed plan purports to alter their class of shares.

### 3.4 CONCLUSION

What is certain from the reference in the definition of “business rescue” is that the main goal of the proceedings is for the company to survive. So therefore, there can be no doubt that shareholders have a very real and continued interest that deserves protection during the process.<sup>88</sup>

Shareholders are entitled to notices and to participate in court proceedings regarding business rescue to the extent provided, they are entitled to vote on a business rescue plan only if the proposed plan purports to alter the rights associated with the class of securities held by that person. Shareholders are also entitled to bring an application to commence business rescue proceedings in terms of section 131. These rights ensure participation in the business rescue process but it is doubtful whether shareholder’s participation can be construed as meaningful.

Unlike creditors and employees, shareholders are not empowered to form a shareholder’s committee, this is a factor which is unfairly prejudicial to shareholders. No explanation or substantial reason has been put forward by the legislators of the 2008 Act for this blatant exclusion of shareholders. The fact that shareholders are entitled to vote on a business rescue plan only if the proposed plan purports to alter the rights associated with the class of securities held by that shareholder, makes one understand why Loubser<sup>89</sup> opines that once the process has started it will leave shareholders on the side-lines and with very little influence. She convincingly argues that the prevailing view and policy remaining is that the role of shareholders in a company’s business rescue will mainly be that of “onlookers”, although they may be the only ones that stand to lose everything should the attempt to rescue the company fail.

The courts in their interpretation of the provisions of business rescue seem to have placed much weight on the interests of creditors and employees as opposed to the interests of shareholders. When faced with the issue of weighing the interests of creditors and the interest of company

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<sup>88</sup> A Loubser ‘The Role of Shareholders during Corporate Rescue Proceedings: Always on the Outside Looking In?’ (2008) 20 SA Merc LJ372.

<sup>89</sup> A Loubser ‘The Role of Shareholders during Corporate Rescue Proceedings: Always on the Outside Looking In?’ (2008) 20 SA Merc LJ372.

the court in the of cases *Oakdene*<sup>90</sup> and *Beagles Run*<sup>91</sup> decided that the interests of the creditors should carry the day. In the Australian decision of *Dallinger v Halcha Holdings*<sup>92</sup> the implication was that the second goal emphasizes the interest of the company's creditors above its shareholders.

## CHAPTER 4: EMPLOYEES

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### 4.1 EFFECTS OF BUSINESS RESCUE ON EMPLOYEES AND CONTRACTS

One cannot discuss the rights of employees without first mentioning the Constitution of the Republic of South Africa Act 108 of 1996 (1996 Constitution), employees have distinctive advantages in that the constitution enshrines several workers' rights as fundamental human rights. The 1996 Constitution provides protection to every employee's right to fair labour practices<sup>93</sup>. The Labour Relations Act<sup>94</sup> (LRA) and the Basic Conditions of Employment Act (BCEA)<sup>95</sup> give effect to the constitutional right of fair labour practices. One of the 2008 Act's clearly stated purpose is to ensure compliance with the bill of rights of the constitution which give effect to fair labour practices.

The rights of employees have received limited protection in the past, whereas in the liquidation proceedings employees are immediately put off work after a company is ordered by the court to be liquidated, the new companies act offers a solution to end the unfairness and prejudice previously suffered by employees in the insolvency regime. In the 2008 Act provision is made to prevent immediate loss of employment.

'Employees of the company immediately before the beginning of the business rescue proceedings, continue to be so employed on the same terms and conditions , except to the extent that; changes occur in the ordinary course of attrition; or the employees and the company, in accordance with applicable labour laws, agree to different terms and conditions; and any

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<sup>90</sup> *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd*. (609/2012) [2013] ZASCA 68 (27 May 2013).

<sup>91</sup> *Swart v Beagles Run Investments 25 (Pty) Ltd* 2011 5 SA 422 (GNP).

<sup>92</sup> *Dallinger v Halcha Holdings* (1994) 14 ACLC 236.

<sup>93</sup> Constitution of the Republic of South Africa Act 108 of 1996 Section 23 (1) - (5).

<sup>94</sup> Labour Relations Act 66 of 1995.

<sup>95</sup> Basic Conditions of Employment Act 75 of 1997.

retrenchment of any such employees contemplated in the company's business rescue plan is subject to the provisions of the LRA and other applicable related legislation.<sup>96</sup>

This provision above will still apply despite any provision of an agreement to the contrary, during a company's business rescue proceedings.<sup>97</sup>

‘Subject to subsection (2A), and despite any provision of an agreement to the contrary, during business rescue proceedings, the practitioner may suspend, for the duration of the business rescue proceedings, any obligation of the company that arises under an agreement to which the company was a party at the commencement of the business rescue proceedings; and would otherwise become due during those proceedings; or apply urgently to a court to entirely, partially or conditionally cancel, on any terms that are just and reasonable in the circumstances, any obligation of the company contemplated in paragraph (a)’<sup>98</sup>. The purpose of section 136 (2A) is to avoid the unnecessary suspension of any provision of an employment contract or an agreement where section 35A or 35B of the Insolvency Act applies.

#### 4.2 REMUNERATION

Employees continue to receive financial consideration for services rendered, business rescue affords protection to employees. To the extent that any remuneration, reimbursement for expenses or other amounts of money relating to employment became due and payable by a company to an employee at any time before the beginning of the company's business rescue proceedings, and had not been paid to that employee immediately before the beginning of those proceedings, the employee is regarded a preferred creditor of the company<sup>99</sup>. The implications of this preference over pre-commencement creditors has already been discussed above in chapter two and need not be repeated. A medical scheme, or a pension scheme including a provident scheme, for the benefit of the past or present employees of the company is an unsecured creditor of the company to the extent of; any amount that was due and payable by the company to the trustees of the scheme at any time before the beginning of the company's business rescue proceedings, and that had not been paid immediately before the beginning of those proceedings; and

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<sup>96</sup> Companies Act 71 of 2008 Section 136 (1) (a).

<sup>97</sup> Companies Act 71 of 2008 Section 136 (1) (b).

<sup>98</sup> Companies Act 71 Section 136 (2) (a) and (b).

<sup>99</sup> Companies Act 71 Section 144 (2).



In the case of a defined pension scheme, the present value at the commencement of the business rescue proceedings of any unfunded liability under that scheme.<sup>100</sup>

#### 4.3 GENERAL PARTICIPATION RIGHTS OF EMPLOYEES

The rights of employees are similar in most respects to those of creditors discussed above in chapter two, these rights include the entitlement of a notice, of each court proceeding, decision, meeting or other relevant event concerning the business rescue proceedings. They have the rights to form a committee of employees' representatives; to be consulted by the practitioner during the development of the business rescue plan and afforded sufficient opportunity to review any such plan, they have the rights to vote with creditors on a motion to approve a proposed business plan, to the extent that the employee is a creditor. Employees may be represented by a registered trade union representing any employee of the company, which is usually the case in these matters.<sup>101</sup> It's clear that employees are extensively involved and may actively participate with the business rescue practitioner to make sure their interests are protected during the proceedings.

As affected person's individual employees and trade unions, are also entitled to make an application to court for an order commencing business rescue proceedings. Bradstreet<sup>102</sup> asserts, agreeably so, that 'this application may become subject to abuse as bargaining tool for salary and wage negotiations by employees and trade unions, and such parties would also have a right to appoint their own practitioner'. In this lights he further states that what is essential to any effective business rescue regime is the striking a balance between the various goals involved.

In interpreting the goals of business rescue in s128 (1) (b) the courts have found the interests of employees to be paramount, in *Employees Solar Spectrum Trading 83 (Pty) Ltd v Afgri Operations Ltd*<sup>103</sup> the very first case since the inception of the new business rescue where employees approached the court as affected persons to apply for a company's compulsory business rescue. The question before the court was whether there was a reasonable prospect to rescue the company.

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<sup>100</sup> Companies Act 71 Section 144 (4) (a) and (b).

<sup>101</sup> Companies Act 71 of 2008 Section 144.

<sup>102</sup> R Bradstreet, 'The new business rescue: Will creditors sink or swim?' (2011) 128 SALJ 352. At 49 to 53.

<sup>103</sup> *Employees Solar Spectrum Trading 83 (Pty) Ltd v Afgri Operations Ltd and Solar Spectrum Trading 83 (Pty) Ltd* unreported case no 6418/2011, 18624/2011 and 66226/2011 (NGC).

The judge found that the type of information that is brought before the court by an affected party will depend on the position the specific affected party has towards the company this was referred to by the court as a “balancing exercise”.<sup>104</sup> The court concluded that what is required is the determination that the future prospect of rescuing the business appear to be reasonable.<sup>105</sup> The court after evaluating all the merits and circumstances of the case decided that the employees had indeed made out a reasonable prospect that the business may be rescued and accordingly granted the application.

It is submitted that over-employment may also be a cause of a business’s financial distress, too high a wage bill and salary costs etc. in acceptance of this contention it is then essential that the provisions of business rescue allow for the cutting down off employees in a company where it is obviously needed, appropriate and in line with labour law practices. This approach is welcome in the sense that it may save the employment of some employees rather than the retrenchment of all.

*Solidarity Obo BD Fourie & Others v Vanchem Products (Pty) Ltd and Others (Vanchem)*<sup>106</sup> is the first known reported decision on retrenchment of employees by a business rescue practitioner, here the trade union challenged the lawfulness of the retrenchment of employees by the practitioner.

The National Union of Metalworkers (NUMSA) argued that unless the retrenchment of any employees employed at the time business rescue proceedings commence occurs in terms of an approved business rescue plan, then the termination of their services is unlawful because it is in breach of section 136 (1) (a), note that the specific provisions of this section are outlined in the beginning of this Chapter.

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<sup>104</sup> Employees Solar Spectrum Trading 83 (Pty) Ltd v Afgri Operations Ltd and Solar Spectrum Trading 83 (Pty) Ltd unreported case no 6418/2011, 18624/2011 and 66226/2011 (NGC).

<sup>105</sup> Employees Solar Spectrum Trading 83 (Pty) Ltd v Afgri Operations Ltd and Solar Spectrum Trading 83 (Pty) Ltd unreported case no 6418/2011, 18624/2011 and 66226/2011 (NGC).

<sup>106</sup> *Solidarity Obo BD Fourie & Others v Vanchem Products (Pty) Ltd and Others; In re: National Union of Metalworkers (NUMSA) Obo Members v Vanchem Vanadium Products (Pty) Ltd and Another* (J385/16 & J393/16 [2016] ZALCJHB 106, 22 March 2016).

Vanadium argued that nothing in the section suspends the operation of section 189A and that section 136(1) (b) merely means that retrenchments are contemplated as part of the process, but are subject to section 189 and 189A.<sup>107</sup>

The question that the court had to answer was whether ‘the wording of section 136(1) of the Companies Act mean that where an employer is in business rescue, employees cannot be retrenched except as provided for in the business rescue plan, which must first be approved by creditors? In other words, can the employer (or the business rescue practitioner) embark on a section 189 process based on the employer’s immediate (and often pressing) operational needs before the business rescue plan has been approved?’<sup>108</sup>

In its interpretation of section 136 (1) the court stated that the section consists of two distinct parts:

- (i) Subsection (1)(a) affirms the continuity of existing employees’ terms and conditions of employment and;
- (ii) Subsection (1)(b) obliges the business rescue practitioner to conduct any retrenchment in the business rescue plan in compliance with the relevant provisions of the LRA pertaining to retrenchments.

The court continued to rule as follows:

It is the reference to changes occurring in the “ordinary course of attrition” that might be seen as a basis for interpreting the section to provide a guarantee of continuity of employment and not merely the preservation of conditions of employment. If this interpretation is correct, what is anomalous is why subsection (1)(b) was not worded in the form of an exception to subsection (1)(a) rather than simply an additional self-standing provision preserving the rights of employees retrenched under a business rescue plan, to be retrenched only in accordance with the applicable provisions of the LRA. Alternatively, subsection (1) (a) ought to have stated that the prohibitions it contains are subject to subsection (1) (b). In the absence of such qualifications to either sub clause, the two provisions are

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<sup>107</sup> *Solidarity Obo BD Fourie & Others v Vanchem Products (Pty) Ltd and Others; In re: National Union of Metalworkers (NUMSA) Obo Members v Vanchem Vanadium Products (Pty) Ltd and Another* (J385/16 & J393/16 [2016] ZALCJHB 106, 22 March 2016).

<sup>108</sup> A Johnson & M Bux, “can a retrenchment process start before a business rescue plan has been approved?” <https://www.ensafrica.com/news/can-a-retrenchment-process-start-before-a-business-rescue-plan-has-been-approved?Id=2181&STitle=employment%20ENSight>.

irreconcilable unless the phrase “ordinary course of attrition” is interpreted to include all forms of lawful termination, including retrenchment.<sup>109</sup>

Further “Section 136(2) permits a BRP to suspend obligations owed by the company at that time business rescue proceedings commenced. Section 136(2A) exempts employment contracts from this power of suspension. Once again, the provisions deal with the suspension of obligations, but are silent on the question of the lawful termination of obligations. Considering the section as a whole it seems the primary object of the section was to prevent the unilateral variation of company obligations by a BRP, but to permit the BRP to suspend the performance of certain contractual obligations except those relating to employees. It does not seem to be directed at preventing the lawful termination of obligations including employment contracts. Consequently, I am not persuaded that the provisions of section 136 effectively outlaw any retrenchments taking place except in terms of an approved business plan.<sup>110</sup>”

As per this judgment of *Vanchem* it seems that the business rescue practitioner is entitled to retrench employees of a company, provided there is compliance with section 189 of the LRA, the business rescue practitioner would have to show that the proposed retrenchments are based on the employer’s proper and justifiable operational needs and requirements as was the case in this matter.

#### 4.4 ANALYSIS

Employees are afforded extensive rights in the business rescue process, if not excessive. The controversial right afforded in section 131 (4) (iii) where an employee or trade union as an affected person can apply to court to place the company under business rescue proceedings has been of concern. The wording of the section seems to suggest that creditors’ interests may be threatened by the application by trade unions being brought merely to extract value of the company<sup>111</sup>. Schoeman<sup>112</sup> also asserts that what is of greater concern is the fact that an individual employee may also make an application to court to commence business rescue proceeding. She presents an example where a disgruntled employee may abuse their right to

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<sup>109</sup> *Solidarity Obo BD Fourie & Others v Vanchem Products (Pty) Ltd and Others; In re: National Union of Metalworkers (NUMSA) Obo Members v Vanchem Vanadium Products (Pty) Ltd and Another* (J385/16 & J393/16 [2016] ZALCJHB 106, 22 March 2016). Para 35.

<sup>110</sup> *Solidarity Obo BD Fourie & Others v Vanchem Products (Pty) Ltd and Others; In re: National Union of Metalworkers (NUMSA) Obo Members v Vanchem Vanadium Products (Pty) Ltd and Another* (J385/16 & J393/16 [2016] ZALCJHB 106, 22 March 2016).para 36.

<sup>111</sup> R 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) *SALJ* 44-52.

<sup>112</sup>HC Schoeman, ‘The Rights Granted to Trade Unions under the Companies ACT 71 of 2008’ *PER/PELJ* (2013) 16 237.

force a company into accepting their demands in a situation which the company may have a good reason for a dismissal of the employee in accordance with the relevant legislation. She concludes by suggesting that legislation needs to revisit the provisions of chapter 6 and recommends that only majority registered trade unions or, at the least, sufficiently represented trade unions in the workplace be given the right to apply to court. Further that the rights afforded to trade unions are afforded only to trade unions that are a creditor of the company.

Bradstreet correctly observes that from an employment perspective where liquidation and wide- scale retrenchment will be inevitable, it is obvious and understandable that employees of a distressed company would lean towards the confines of the business rescue proceedings than that of liquidation, because the former clearly afford better protection than the latter, as far as the interests of employees are concerned.<sup>113</sup>

Bradstreet highlights that there is a clear economic benefit in using chapter 6 as means to extract value from a financially distressed company and in case where employment is extended, a social benefit also results.

Joubert et al have argued that ‘if corporate rescue goes too far in providing for the protection of the employees of the failed entity, this may ultimately be to the detriment of the employees. This is especially so if the protection granted corresponds with the over-burdening of the new owner (employer), or the excessive erosion of the rights of creditors, such as banks, that hold the key to the company's credit lifeline. If these important stakeholders are deterred from investing by an unbalanced procedure, the corporate rescue legislation could become counter-productive.’<sup>114</sup>

The above contention begs the question of whether legislation has indeed gone too far in protecting employees’ interests.

The prevailing view is simply that legislation has gone too far. Lousber<sup>115</sup> argues that in giving individual employees the right in section 131 (4) (iii), legislation has not only gone too far but have exposed the process and companies to potential abuse. She submits that the rights afforded to employees during business rescue far outweigh those that accrue to employees in liquidation.

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<sup>113</sup> R 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) *SALJ* 44-52.

<sup>114</sup>T Joubert, S Van Eck & D Burdette ‘The expected Impact of Labour Law on South Africa’s New Corporate Rescue Mechanism’ (2011) 27 (1) *Intl. J. Comp. Lab. L. & Indus. Rel.* 65.

<sup>115</sup> Loubser op cit (n79) 510.

Supporting Bradstreet's view mentioned above, she also states that there is real incentive for the employees in seeking that the company goes into business rescue thus increasing the potential for abuse.

The business rescue practitioner must consult with creditors, registered trade unions and employees and the management of the company when developing a business rescue plan for consideration and adoption. Affected persons must be provided with information reasonably required to facilitate affected persons in deciding whether or not to accept or reject the plan. Employees play a role when the claim is being finalized. Joubert et al highlights the fact that only employees have the right to propose the development of an alternative plan if the proposed plan is not accepted and that this puts them in a stronger negotiating position than shareholders and / or creditors of the company.<sup>116</sup>

Section 144 (2) provides for the preferential payments of moneys owed to "creditor employees" of a company under business rescue proceedings. The intentions behind this provision have been dealt with above. The provision is essential for the effectiveness of the procedure, however there are still some concerns which exist. The section does not place any limitation on the claims of employees for arrear salaries, this make the provisions of business rescue far more favourable than the provisions of the insolvency act which provide for a limitation in time and amount claimable if the company goes into liquidation.<sup>117</sup> These preferential provisions may act as a deterrence to financial institutions that are still willing to provide finance to a company under business rescue due to the reality that the money will first be used to pay the arrear salaries of employees and the business rescue practitioner's remuneration.

In her research Loubser<sup>118</sup> found that there is no equivalent comparable jurisdiction as regards to the rights given to employees in corporate rescue procedure and that these rights may be 'excessive'.

#### 4.5 CONCLUSION

While it is commendable that legislators of the new business rescue procedure have gone out of the way to make sure that the interests of employees are protected during insolvency times

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<sup>116</sup> T Joubert, S Van Eck & D Burdette 'The expected Impact of Labour Law on South Africa's New Corporate Rescue Mechanism' (2011) 27 (1) Intl. J. Comp. Lab. L. & Indus. Rel. 65.

<sup>117</sup> Note 111 above, 65.

<sup>118</sup> Loubser LLD thesis *op cit* note 55 at 53.

of a company, there are some troubling provisions which imply that maybe they have gone too far in trying to protect these interests.

It is submitted that ‘the provisions could be more balanced between the rights of all the stakeholders. A more balanced approach would allow for some flexibility in what appears to be a very rigid approach in the protection of employees. A flexible approach, especially regarding the business rescue practitioner’s right to downsize the workforce without having to comply with too many rigid and time-consuming formalities, would go a long way to making the resuscitation of companies more viable for the other stakeholder groups involved in the financial collapse of a company.’<sup>119</sup>

It’s been mentioned above that the provision for employees is essential in the business rescue process because they continue to work for the company during the process and so need an incentive to carry on working efficiently. The protection of continued remuneration or if not the promise of preferred payment in future has been provided in the provisions of business rescue, my submission is that any rights afforded which go beyond the relations of unpaid salaries are unnecessary and are a potential cause for concern.

## CHAPTER 5: CONCLUSION

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### 5.1 HAS A BALANCE BEEN STRUCK?

It has been accepted that the underlying objective of business rescue is to maintain the life of the distressed company. It is without exception that the continued existence of the company on a solvent basis is in the best interest of employees, this is the case for shareholders as well who hope to maintain their capital investments in the company and may still have hope of future dividends.<sup>120</sup> it is submitted that there is also an economic advantage to saving a corporate entity because of tax implications, a company going into liquidation signifies the loss of taxpayer’s jobs and subsequently a reduction in the tax base. Employees out of work and a

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<sup>119</sup> T Joubert, S Van Eck & D Burdette ‘The expected Impact of Labour Law on South Africa’s New Corporate Rescue Mechanism’ (2011) 27 (1) *Intl. J. Comp. Lab. L. & Indus. Rel.* 65.

<sup>120</sup> T Joubert, S Van Eck & D Burdette. ‘The expected Impact of Labour Law on South Africa’s New Corporate Rescue Mechanism’. (2011) 27 (1) *Intl. J. Comp. Lab. L. & Indus. Rel.* 65.

closed down entity means that these employees and the failed business entity will no longer be able to contribute to the countries tax system.<sup>121</sup>

On some different perspective creditors, may have lost hope in the business entity and may not share the same positive views expressed by the other stakeholders. Because of these competing interests, the 2008 act, specifically chapter 6 of business rescue was drafted with the specific purpose of providing for efficient rescue and recovery of financially distressed companies, in a manner that balances the rights and interests of all relevant stakeholders.<sup>122</sup>

the question that follows is whether this balance has been achieved. The preponderant view is that the legislature has failed to struck a proper balance between the relevant stakeholders. It is submitted that ‘the provisions could be more balanced between the rights of all stakeholders. A more balanced approach would allow for some flexibility in what appears to be a very rigid approach to the protection of employees.’<sup>123</sup>

The rights of employees in the business rescue procedure have been extensively provided for; Unlike in liquidation proceedings employees continue to be employed and receive financial consideration, employees are empowered to bring an application to court in terms of section 131 (3) (iii) to commence business rescue proceedings for a financially distressed company, an individual employee or a trade union representing employees of the company also have this right.

It is submitted that these applications may become subject to abuse by disgruntled employees and trade unions looking to extract money from the distressed company, the provisions also allows for the appointment of one’s own chosen practitioner.<sup>124</sup> Employees are further empowered to form an employee’s committee and may consult with the business rescue practitioner in the development of the business rescue plan, they can vote or reject a proposed plan, and may also propose an alternative plan if the one proposed is rejected. One of the most contentious provision of business rescue relating to employees is that if employees are owed any unpaid salaries or outstanding employment related amounts, they claim in the process will

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<sup>121</sup> R 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) *SALJ* 44-52.

<sup>122</sup> Companies Act 71 of 2008 Section 7 (k).

<sup>123</sup> Note 117 above.

<sup>124</sup> R Bradstreet, “The new business rescue: will creditors sink or swim?” 2011 *SALJ* 352.



be elevated to those of co-creditors and these claims will be preferred over the claims of pre-commencement creditors.

The interests of employees should be provided for and protected and it clear that this was the legislature's noble intentions when the act was drafted however the over-empowerment of employees may come at the expense of other stakeholders more specifically shareholders.

Bradstreet remarks that 'one category of stakeholders that will probably in most cases not stand to benefit is the company's shareholders, although already being at the back of the queue.'<sup>125</sup> This is true when one compares the rights afforded to employees compared to the rights afforded to shareholders in the business rescue process.

Shareholders have all the rights afforded to employees and creditors, they are given formal recognition as 'affected persons'. However, the extent to which they can participate and be involved in the process is questionable. Whether shareholders play a meaningful role in the process is a question that has been examined above and answered in the negative.

The courts in the judgements discussed in this dissertation, *Oakdene*, *Swart v Beagles* and the Australian decision of *Dallinger*, took an approach that seems to favour the interests of creditors over those of the company or its shareholders, when faced with weighing of the interests of creditors against the interests of the company the courts decided that the interests of creditors should carry the day. The reference in the definition of business rescue to a better return for the company's creditors and shareholders implies that the interests of shareholders are equal to those of creditors however the courts have emphasised the creditors interest's in this regard.

In theory shareholders have the right to bring a business rescue application to court but it doubtful whether they will find it possible to prove any of the grounds they are required to prove in court before such an application can be granted. Without the co-operation of creditors or the company's management is unlikely that shareholder will be able to prove that there is a 'reasonable prospect' without the relevant information needed, this especially so if the application is opposed by the creditors.<sup>126</sup> These observations are consistent with the case of

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<sup>125</sup> R 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 *SALJ* 44.

<sup>126</sup> A Loubser 'The Role of Shareholders during Corporate Rescue Proceedings: Always on the Outside Looking In?' (2008) 20 *SA Merc LJ* 372.

*Francis Edward Gormely*<sup>127</sup>, discussed above, where a major shareholder had applied to court to have a company placed under supervision. The application was refused by the court because it lacked the factual foundation and information needed to prove a 'reasonable prospect'. There also hasn't been a reported case where a general shareholder has successfully brought an application except where the shareholders were also the creditors of the company as seen in the case of Oakdene.

Shareholders do not have the right to vote to approve or reject a proposed rescue plan unless the plan would alter the rights associated with the class of securities held by that person. Shareholders are not empowered to have a shareholder's committee but creditors and employees are empowered to have their own committees. This prejudice is unjustified, shareholders have just as much interests in the process as the other stakeholders. The committee meetings are important because it allows the stakeholders to consult with the practitioner about the business rescue plan and therefore influence the outcome of the process.

One of the primary reasons why judicial management failed was because too much emphasis was placed on the interests of creditors. The new rescue procedure attempts to address this problem without unduly prejudicing creditors.

There is not much left to be said about creditors except that the creditors have been granted extensive rights in the business rescue process and that the provisions adequately provide for and protect their interests in the process. There are a few provisions which are a cause for concern but not big enough that they can't be amended.

I submit that protection of creditor's interests is highly essential because the provision for their repayment encourages their further participation in the commercial enterprise. It is also important when it comes to financing the rescue process considering that the reason for the company initiating these proceedings is because of financial difficulty in the first place. A creditor is unlikely to lend a helping hand to a financially distressed company if the rescue procedure does not show promise in protecting his financial interest.

The main two contentious provisions that seem to prejudice or curtail the right of creditors are; firstly, the provision for post-commencement creditors which are preferred over pre-commencement creditors and more interestingly is that employee's claims are also elevated to the status of post-commencement creditors. This means that the claims of pre-commencement

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<sup>127</sup> *Francis Edward Gormely v West City Precinct Properties (Pty) Ltd* 19076/11 (WCC) 18 April 2012.

secured creditors will come after the claims of employees. Secondly is the legal moratorium which comes into force at the commencement of the business rescue proceedings, this moratorium has the effect of suspending all legal proceedings, including enforcement action against the company during the business rescue process. It accepted that these two provisions are necessary because they are designed to ensure a successful business rescue which will hopefully result in the creditors ultimately being repaid in full or at the very least, getting a better return than what they would get in liquidation proceedings.

## 5.2 OVERALL CONCLUSION

South African corporate law has done a commendable job in providing a rescue procedure for financially distressed companies that is in line with the needs of a modern South African economy. The legislature introduced the new business rescue procedure in the 2008 act, although it is a remarkable improvement from the old judicial management system, there is room for improvement. I submit that legislature needs to revisit the provisions contained in chapter 6 business rescue.

A limitation of the rights afforded to employees in the business rescue process is the first solution that comes to mind. It is suggested above that only majority registered trade unions or, at the least, sufficiently represented trade unions in the workplace be given the right to apply to court and the rights afforded to trade unions be allowed only to trade unions that are a creditor of the company.<sup>128</sup> for example, an individual employee or the registered trade union should be allowed to apply to court for a company to be placed under supervision only in the event were employees have not been paid salaries for two to three months owing to the company's financial difficulty.

Business rescue provides for the preferential payments of moneys owed to 'creditor employees' of a company under business rescue proceedings. The 2008 act should have limitations on the claims of employees for arrear salaries and other amounts that may exist at the time the company goes into business rescue. This is especially, because employees claim in the process are preferred over the pre-commencement creditor's claims and this preference

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<sup>128</sup> H C Schoeman, 'The Rights Granted to Trade Unions Under the Companies ACT 71 of 2008' *PER/PELJ* (2013) 16 237.

will continue to apply if business rescue proceedings are terminated and the company is placed in liquidation.<sup>129</sup>

As far as the attainment of a balance between all stakeholders is concerned, I submit that the empowerment of shareholders in the process will go a long way, provision must be made for a shareholder's committee that will represent the general shareholders of the company; this will ensure that the interests of shareholder are protected and provided for extensively, it will give shareholders the chance to consult with the business rescue practitioner about the plans and future of the distressed company. Shareholders should also have the right to vote to reject or approve the business rescue plan regardless of whether the proposed plan purports to alter the rights of the holders of any class of the company's securities, because the adopted business rescue plan will apply to all stakeholders even though they did not vote or had voted against the plan. Voting for the adoption of a business rescue plan is a very important step because it could mean the beginning or the end of the business rescue process.

The approach taken by courts in corporate rescue proceedings has for a long time leaned towards the protection of the creditor's interests, with the coming into force of the 2008 act the need for a balanced system was introduced this meant a shift in the mind set was necessary in the judicial system. the provisions of business rescue need to be applied in a manner which considers all the stakeholder's interests. Courts must take into consideration the specific purpose or intentions of the act when interpreting the provisions of business rescue, when courts are faced with competing interest of creditors and the company's, the rules of just and equitable should be applied to avoid any biases. In the case of *Oakdene* the court remarked that the new procedure 'encapsulates a shift from creditors' interests to a broader range of interests' on the rationale that preserving the business as a whole may 'in the end prove to be a better option for creditors.'<sup>130</sup>

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<sup>129</sup> T Joubert, S Van Eck & D Burdette. 'The expected Impact of Labour Law on South Africa's New Corporate Rescue Mechanism'. (2011) 27 (1) *Intl. J. Comp. Lab. L. & Indus. Rel.* 65.

<sup>130</sup> *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd* (609/2012) [2013] ZASCA 68 (27 May 2013) para 37.

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