



UNIVERSITEIT VAN PRETORIA
UNIVERSITY OF PRETORIA
YUNIBESITHI YA PRETORIA

**BUSINESS RESCUE AFTER THE COMMENCEMENT OF LIQUIDATION
PROCEEDINGS: A LEGAL CONUNDRUM IN SOUTH AFRICA?**

by

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Submitted in partial fulfilment of the requirements for the degree

Master of Laws in Insolvency Law

(MAGISTER LEGUM)

in the

DEPARTMENT OF MERCANTILE LAW

FACULTY OF LAW

at the

UNIVERSITY OF PRETORIA

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October 2018

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DEDICATION

I dedicate this work to my grandparents, Mr Amos “Khofi” Nyoni and Mrs Catherine Nyoni (née Manyisa), posthumously. This study was commenced and completed in their loving memory.

Gogo naMkhulu, I recognise and truly appreciate that you pulled out all the stops to ensure that I at least received basic education despite your impecunious circumstances in the disadvantaged rural area where we were domiciled. I am sure you would have been proud of me today. Your commitment to the Christian faith was also inspiring. May your souls rest in peace and rise to everlasting joy. Amen.

To all my children and descendants, I have upped the ante on the academic front against all odds. Your challenge is not to lower the bar, but to strive to reach even greater heights. The same applies to all of you my nephews and nieces. Getting education should be your top priority, albeit it does not guarantee material wealth. It nevertheless makes you a better person on this planet and helps you not to get lost in “the maze called life”, as viewed by Forest Whitaker. It is not an easy journey, but it is never too late to start. *Imfundvo ayikhulelwa*.

ACKNOWLEDGMENTS

The thesis would not have been completed without the unwavering support, guidance and encouragement from a number of people, some of whom deserve special mention.

Dr T. Joubert for gladly taking on the task of being my supervisor for the thesis despite her own academic and professional commitments. Your invaluable guidance, support and advice throughout the writing of this manuscript has been helpful towards the completion of the work. I would not have asked for a better supervisor. The Dean of the Faculty of Law, University of Pretoria, Prof. A. Boraine for the great insights into the field of insolvency law. Prof. Marius Pretorius in the Faculty of Economic and Management Sciences, University of Pretoria, for inspiring me to do my research on this topic. Mr Sikhumbuzo Tsabedze, a consummate professional, who not only motivated me with his passion for education, but also nudged and persuaded me to study law. My friend, Mr Mphiwa Ngwenya, for his steadfast moral support. Mr Eugene Dlamini, an attorney, who has always encouraged me to further my studies in the field of law and has constantly engaged me on various legal doctrines. My fellow colleagues in the Faculty of Law, especially Mses Mulamuleli Ramabulana and Renette Leathern, who supported me and encouraged me to stay the course when the going was tough and I was slacking off.

Lastly, I would like to thank Brand South Africa for affording me time to pursue my studies in spite of the constant work pressure in the organisation. Special thanks go to the team in the Governance and Legal Department as they had to contend with an extra workload when I was occasionally away on study leave. Thank you Ms Kholiwe Mosiea for your enormous support, especially when I had to juggle more than enough balls at the office and still get my assignments typed. You deserve nothing but accolades.

Nothando, Telamene and Tivamile, thank you my awesome daughters for motivating me to be a good role model. Telamene, your late night calls and mobile phone text messages when you were still pursuing your honours degree at Rhodes University encouraged me when I also could not get a wink of sleep, burning the midnight oil. I thank you Lord for my good health and keeping me focused. May God the Almighty continue to bless us all!

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CHAPTER 1: INTRODUCTION

1.1 General Background of the Study

The new business rescue procedure which was introduced by Chapter 6 of the Companies Act¹ (the 2008 Act) has changed the commercial landscape in South Africa.² It has been welcomed as a long-overdue replacement of judicial management, especially in the wake of the Supreme Court of Appeal's landmark judgment in *Le Roux Hotel Management (Pty) Ltd and Another v E Rand (Pty) Ltd*.³ In respect of this judgment, Josman J was generally viewed as having administered a final "lethal injection" to judicial management as a corporate rescue procedure.⁴

One of the purposes of the 2008 Act is to provide for the efficient rescue and recovery of financially distressed companies in a manner that balances the rights and interests of all relevant stakeholders.⁵ Consequently, a business rescue culture, as opposed to the inherent liquidation culture, is being ingrained by the 2008 Act. This comes as a result of the realisation that if the penalties for corporate bankruptcy were to be lowered, companies would take more economic risks to succeed, more jobs would be created, more tax-paying entities would be preserved, and the South African society as a whole would benefit. The idea that company failure is simply a market mechanism to get rid of inefficiency, as viewed by economists, no longer receives unqualified acceptance.⁶

Historically, benefits for creditors have constituted the main objective of insolvency regimes in most countries, including South Africa.⁷ In *Ex parte Erasmus and Another*,⁸ the

¹ 71 of 2008.

² Rhodie and Mpahlwa "Business rescue – where will it end?" 13 August 2015 *Dispute Resolution Matters* Cliff Dekker Hofmeyr www.cliffedekkerhofmeyr.com/en/news/publications/2015/dispute-resolution/dispute-resolution-matters-13-august-business-rescuewhere-will-it-end (Accessed 21 April 2018).

³ 2001 2 SA 727 (CPD).

⁴ Joubert "Reasonable possibility" versus "Reasonable Prospect": Did business rescue succeed in creating a better test than judicial management?.' 2013 *THRHR* 76.

⁵ S 7(k).

⁶ Kloppers "Judicial management – a corporate rescue mechanism in need of reform". 1999 *Stell LR* 215.

⁷ International Association of Restructuring, Bankruptcy and Insolvency Professionals (hereafter "INSOL International") Consumer Debt Report: Report on Findings and Recommendations 2001 (hereafter "Debt Report").

⁸ 2015 1 SA 540 (GP).

Court held that in sequestration proceedings the applicant must prove that the sequestration will be to the advantage of all creditors as a group. The concept of *concursum creditorum* (“coming together of creditors”)⁹ further puts creditors’ rights at the forefront after the sequestration or liquidation order has been issued.

In this study, the researcher will be traversing cases involving liquidations occasioned by insolvency or inability to pay debts, notwithstanding that a solvent winding-up can be converted into an insolvent winding-up.¹⁰

The purpose of the liquidation proceedings is to dispose of the assets of the company and to pay available proceeds to its creditors according to the legal order of preference. Section 339 of the 1973 Act¹¹ makes the Insolvency Act applicable to the winding-up of Companies unable to pay their debts. Sections 6, 10 and 12 of the Insolvency Act¹² stipulate advantage to creditors as a peremptory requirement for sequestration applications. As a result, the South African insolvency system has hitherto been seen as creditor-oriented. This has inadvertently perpetuated the liquidation culture which can be traced back to the country’s English law roots.

Contrary to the liquidation culture entrenched by both the Insolvency Act and the 1973 Act, Chapter 6 of the 2008 Act has ushered in a new corporate rescue regime which is bringing about an evolution in the country’s insolvency system. The new business rescue procedure was mainly prompted by the apparent failure of judicial management as a corporate rescue procedure. Despite its teething problems, it has been found to be a worthy alternative to the statutory norm of liquidation, particularly for financially distressed companies.¹³ Nevertheless, the intention is not to feather-bed inefficient companies, but to infuse a rescue culture into the corporate insolvency system in keeping with section 7(k) of the 2008 Act and international trends.

⁹ Sharrock *et al* Hockly’s Insolvency Law (2012) 4.

¹⁰ See s 79(3) of the Companies Act 71 of 2008.

¹¹ Companies Act 61 of 1973.

¹² Act 24 of 1936.

¹³ Levenstein “Quo vadis — business rescue or liquidation?” 3 November 2016 *Werksmans Attorneys* www.werksmans.com/legal-briefs-view/business-rescue-or-liquidation/ (Accessed 14 January 2018).

Be that as it may, the new business rescue dispensation has also brought with it a number of legal challenges and conundrums which courts are tussling with — one of these being the interface between liquidation proceedings and business rescue proceedings. Employees, and sometimes creditors, intervene with business rescue applications after liquidation proceedings have already commenced.

In this study, an exposition of the application for business rescue after the commencement of liquidation proceedings will be done. The 2008 Act does not define the concept of “liquidation proceedings” and courts that have grappled with its meaning have often reached different conclusions. The ultimate aim is to ascertain whether business rescue proceedings can be launched after the commencement of liquidation proceedings. It is imperative to know whether this matter has now been settled or it is still a legal conundrum which remains unresolved in terms of South African insolvency law. This currently appears to be a legal minefield which has been created by the blurred lines that have been drawn between the two legal processes. It is unquestionable that there is an interplay between business rescue and liquidation despite the dichotomy between these two procedures. Ideally, there should be a seamless transition from business rescue to liquidation, and vice versa,¹⁴ while discouraging frivolous business rescue applications aimed at staving off legitimate liquidation proceedings and keeping creditors at bay.

Against this backdrop, it is hoped that by the end of the study the researcher will be able to establish whether there is still a legal dilemma, uncertainty or lacuna regarding the interaction between business rescue and liquidation, with special reference to cases where business rescue applications are filed after the commencement of liquidation proceedings. Some of the pitfalls and legal quandaries created by the commencement of business rescue after a liquidation order has been granted will be highlighted.

1.2 Research Questions and Objectives

The key research questions explored in this study are: (a) How does business rescue interact with liquidation in practice? (b) Does legal certainty exist with regard to the

¹⁴ International Monetary Fund *Orderly and Effective Insolvency Procedures: Key Issues* 1999 chapter 4.

application for business rescue after the commencement of liquidation proceedings? (c) Has countenancing business rescue after the commencement of liquidation proceedings created legal conundrums for key stakeholders in South Africa?

The broad objectives of the study were:

- To examine Chapter 6 of the 2008 Act, Chapter 14 of the 1973 Act, as well as court decisions insofar as they relate to the launching of business rescue proceedings after the final liquidation order has already been granted.
- To explore the interface between business rescue and liquidation proceedings.
- To ascertain if the application for business rescue after the commencement of liquidation proceedings is still a legal conundrum in South Africa and whether it has in fact given rise to new legal conundrums.

1.3 Significance of the Study

As demonstrated by the plethora of case law, filing for business rescue after liquidation proceedings have already been commenced by or against the company is an occurrence which courts currently have to deal with on a regular basis. However, there still appears to be conflicting court decisions and a lack of legal certainty regarding the suspension of liquidation proceedings with a business rescue application. The study will attempt to provide legal certainty in this regard as well as on other matters incidental thereto.

It is in the best interests of business owners, directors, creditors, employees, labour unions, liquidators and business rescue practitioners alike to have a clear understanding of the legal position as regards the application for business rescue after a final liquidation order has been granted against a company. Furthermore, it is of cardinal importance to clarify the legal position because business rescue and liquidation are inherently operating at cross-purposes. A critical appraisal of the problems created by the launching of business rescue proceedings after the commencement of business rescue proceedings is also imperative.

1.4 Limitations of the Study

Literature pertaining to the topic of this study is quite limited currently, mainly because business rescue is still a fairly new procedure in South Africa, having been introduced into the country's commercial landscape by the 2008 Act. Accordingly, there was a heavy reliance on legislation, case law, journal articles, theses and opinions of academics when this study was conducted. The focus of the study was mainly on companies and not close corporations. Furthermore, in this study, the researcher was concerned with liquidations occasioned by insolvency or inability to pay debts.

1.5 Literature Review

The methodology used during the study was desk research. We are standing on the shoulders of the giants that have preceded us, hence similar work has already been done with respect to liquidation and business rescue and the interaction between the two processes. It is worth noting though that the amount of research and literature relating to this particular topic was still quite limited.

1.6 Methodology

The bulk of the research was conducted through desktop research and was qualitative. Relevant legislation was studied. There is a wealth of literature available on corporate insolvency and business rescue. Books, journal articles, theses, reports and opinions of academics were also studied. Since May 2011 when the 2008 Act came into force, the courts have taken a myriad of decisions in respect of business rescue while the liquidation process was under way. The researcher had these decisions at his disposal and took them into consideration.

In a nutshell, the research method included the collection of data through the study of primary sources such as statutes and case law, as well as secondary documents, i.e. authoritative texts, books, theses, journals, internet and other electronic sources.

A brief comparative analysis was done with reference to the legal position in England and Australia. South African company law is not based on Roman-Dutch common law but was

largely taken from English law¹⁵. England shares a Commonwealth heritage with South Africa and its insolvency legislation includes a business rescue regime. In addition, England shares a long commercial relationship with South Africa and there is no doubt that English law has had an important influence on South African company law. Consequently, South Africa owes its company law and its corporate insolvency law developments largely to the reception of English common law. Needless to say, English law has influenced the South African law regarding the liquidation of companies.¹⁶ It therefore makes sense to look at a comparable legal system for guidance when trying to find some solutions to problems in South African company law.

Australian corporate rescue provisions have been largely influenced by English law. Consequently, the company law regimes of Australia and South Africa are similar. Australia does not have a separate statute and the provisions which regulate corporate insolvency and business rescue are almost similar to those of the South African rescue mechanism.¹⁷

1.7 Structure of the Dissertation

This dissertation is divided into six chapters, as summarised below:

Chapter 1: Introduction

This is the current chapter which introduces the topic and indicates how the question posed will be answered.

Chapter 2: Commencement and Termination of Liquidation Proceedings in respect of an Insolvent Company

This chapter will deal with the commencement and termination of liquidation proceedings, as well as the effects of liquidation on key stakeholders.

¹⁵ Loubser “Business Rescue in South Africa: A procedure in search of a home?” 2007 *The Comparative and International LJ of Southern Africa*Vo40(.1). 152–171.

¹⁶ Kloppers 1999 *Stell LR*. 417.

¹⁷ Magardie *Companies in Financial Distress During Business Rescue Proceedings* (LLM mini-dissertation 2016 UP) 36.

Chapter 3: Commencement and Termination of Business Rescue Proceedings

This chapter will deal with the commencement and termination of business rescue, as well as the effect of business rescue proceedings on key stakeholders.

Chapter 4: The Launching of Business Rescue after the Commencement of Liquidation Proceedings: A Concise Analysis

This chapter will attempt to proffer answers to the research questions.

Chapter 5: A Comparative Analysis: Australia and the United Kingdom

This chapter will consist of a brief comparative analysis with two foreign jurisdictions and international standards of best practice.

Chapter 6: Conclusion and Recommendations

This chapter will comprise the conclusions reached and recommendations made.

CHAPTER 2: COMMENCEMENT AND TERMINATION OF LIQUIDATION PROCEEDINGS IN RESPECT OF AN INSOLVENT COMPANY

2.1 Introduction and Overview of Liquidation

In this chapter the objectives of liquidation will be highlighted and the definition of “liquidation proceedings” as well as the commencement thereof will be traversed. The effects of a liquidation order on the key role-players in the liquidation process will be unveiled as some of these pose challenges when business rescue is launched after the liquidation order has already been granted. Lastly, the termination of liquidation proceedings will be covered.

Liquidation¹⁸ is the process of administering the affairs of a company prior to its dissolution by ascertaining and realising its assets and applying them, firstly in the payment of creditors of a company according to their order of preference, and then by distributing the residue, if any, amongst the shareholders of the company in accordance with their rights.¹⁹ It is an exhaustive process by which a company is brought to an end and its assets, if there are any, are redistributed.²⁰ It takes place under the control of the Master of the High Court and the process is subject to creditors’ instructions. Liquidation precedes dissolution,²¹ and it should not be confused with deregistration.

The liquidation of insolvent companies still continues to be regulated by the provisions of the Companies Act 61 of 1973²² until such time that it has been replaced by new

¹⁸ Also referred to as “winding-up” in common parlance. However, Legodi J in *Van Staden v Angel Ozone Products CC and Others (in liquidation)* 2013 4 SA 630 (GNP) held that there could be a distinction between

liquidation and winding-up proceedings, where the former denotes legal proceedings before a court of law and the latter, the process overseen by the Master of the High Court (hereafter “the Master”).

¹⁹ Motsai *The Richter judgment: An analysis of section 131(6) of the Companies Act*. (LLM Dissertation 2016 UJ). 20.

²⁰ *Richter v ABSA Bank Limited* (20181/2014) – [2015] ZASCA 100 (1 June 2015) 1.

²¹ See ss 82 and 83 of the Companies Act 71 of 2008; *Cronje NO v Hillcrest Village (Pty) Ltd* 2009 6 SA 12 (SCA) para 22; and *Motala v Master of the High Court North Gauteng* case 07419/2011.

²² Companies Act 61 of 1973 (hereafter “the 1973 Act”).

legislation. The Insolvency Act²³ applies *mutatis mutandis* to a company unable to pay its debts where the 1973 Act does not deal with the matter.²⁴ Section 345 of the 1973 Act enunciates the circumstances under which a company can be deemed to be unable to pay its debts and therefore be liable to be liquidated. A debt in this context refers to an amount of money due and owing.²⁵ The court has discretion whether or not to wind-up a company unable to pay its debts, even where the company is factually insolvent.²⁶ However, normally if this is the case it will not refuse a winding-up order.

2.2 Objectives of Liquidation

Liquidation plays an important role in the market economy as it facilitates the enforcement of contracts. It is definitely not antiquated. Without liquidation, shareholders and creditors would be exposed to greater risk with regard to counterparties. Furthermore, liquidation frees up capital assets and market space for more effective entrepreneurs and business managers to take over, thus encouraging efficient economic outcomes.²⁷ A creditor needs to be able to recoup some value if a borrower fails to repay a debt. Debtor companies are disciplined by the threat of bankruptcy and liquidation.²⁸

As stated in chapter 1, the purpose of liquidation proceedings is to realise the assets of the company and to pay the proceeds to its creditors *pari passu* in accordance with the statutory distribution rules. The intention is to pay off as much creditor debt as possible. A *concursum creditorium* is established once a liquidation order is granted, and the interests of creditors as a group enjoy preference over the interests of individual creditors.²⁹ The Insolvency Act requires the insolvent debtor to satisfy the court that the sequestration will

²³ 24 of 1936.

²⁴ S 339 of the Companies Act 61 of 1973.

²⁵ Cassim *et al* Contemporary Company Law. (2012) 919.

²⁶ See *AA Distributors (Pty) Ltd v Sport & Spel (Edms) Bpk* 1973 3 SA 371 (c); *Cooper v A & G Fashions (Pty) Ltd; Ex parte Millman* 1991 4 SA 2014 (c).

²⁷ Ross "What is the Purpose of Liquidation?" 2018 Investopedia <https://www.investopedia.com/ask/answers/050815/what-purpose-liquidation> (Accessed: 7 March 2018). Also see Burdette "Some initial thoughts on the development of a modern and effective business rescue model for South Africa (part 1)." 2004 SA Merc LJ 260.

²⁸ *Ibid.*

²⁹ Sharrock *et al* Hockly's Insolvency Law (2012) 4.

be to the advantage of his or her creditors.³⁰ However, unlike in the case of sequestration applications, the court need not be satisfied that winding-up will be to the advantage of the company's creditors. Be that as it may, the likelihood of a dividend or otherwise is an important factor for the court to consider.

2.3 Liquidation Proceedings

The 2008 Act does not define the term "liquidation proceedings" found in section 131 of the Act and courts have reached divergent conclusions in this regard. As a result, the term still remains rather nebulous and unclear.

Legodi J in *Van Staden v Angel Ozone Products CC and Others (in liquidation)*³¹ had to deal with the contention that liquidation proceedings should be distinguished from, and not be confused with, winding-up proceedings. He held that liquidation refers to legal proceedings before a court of law and winding-up proceedings refer to the process overseen by liquidators and the Master. In the learned judge's view, winding-up proceedings should be seen as a continuation of liquidation proceedings. Furthermore, he stated that you do not grant a final liquidation order and then execute on it. You execute on a confirmed liquidation and distribution account. Liquidation and winding-up proceedings are processes that are concluded once there is a final liquidation and distribution account which is confirmed by the Master. These processes are meant to ensure that there is no single stakeholder (or creditor) who gains advantage over other creditors.³² In *casu*, the liquidators did not intervene or indicate how far they had progressed with the winding-up process.

Other cases where courts have grappled with the definition of liquidation proceedings include the *First Rand Bank Ltd v Imperial Crown Trading (Pty) Ltd*.³³ In this case, the court interpreted the meaning of "initiated" and held that the word "initiated" in section

³⁰ Ss 6, 10 and 12 of Act 24 of 1936.

³¹ (54009/11) [2012] ZAGPPHC 328; 2013 (4) SA 630 (GNP) (12 October 2012) para 26.

³² *Ibid* para 31.

³³ 2012 4 SA 266 (KZD).

129(1) must have been intended to have the same meaning as the word “commenced” in section 131(6) of the 2008 Act.

In *ABSA Bank Ltd v Summer Lodge Pty Ltd*³⁴ the court granted the following declaratory order:

“the meaning of the words liquidation proceedings in s 131(6) of the Companies Act 71 of 2008 is confined to the actual process of winding-up having been issued by a court, and is the actual process followed in winding-up and overseen by the liquidators and the Master. The words liquidation proceedings do not include the legal proceedings taken by a creditor for purposes of obtaining an order that a company be wound-up”.

In *ABSA v Summer Lodge (Pty) Ltd*³⁵ Makgoba J held that:

“In terms of s 348 of the previous Act, a winding-up order by the court is, by way of a fiction (for purposes of the proper administration of the winding-up order), “*deemed to commence at the time of the presentation to the court of the application for the winding-up,*” but this deeming clause only comes into operation after it has been determined *ex post facto* that a winding-up order has been granted. If no such order has been granted, any liquidation proceedings cannot be deemed to have commenced.”

According to Levenstein,³⁶ the retrospective nature of section 348 of the 1973 Act would assist a liquidator (and creditors) in applying the disposition provisions set out in sections 29 to 31 of the Insolvency Act.

In *ABSA Bank Ltd v Makuna Farm CC*,³⁷ the court held that in terms of section 131(6), liquidation proceedings refer to the process after the liquidation order has been granted.

³⁴ 2013 5 SA 444 (GNP).

³⁵ (63188/2012, 63189/2012, 63190/2012) [2013] para 14.

³⁶ Levenstein *South African Business Rescue Procedure* 2017 (Lexis Nexis looseleaf edition). (hereafter “Levenstein 2017”) para 8.4.

³⁷ 2014 (3) SA 86 (GJ) para 7.

Accordingly, winding-up commences retrospectively upon the final order of liquidation as stated in section 348 of the 1973 Act. Boruchowitz J endorsed the reasoning of Makgoba J that liquidation proceedings as contemplated in section 131(6) of the 2008 Act refer to the proceedings that follow the granting of a winding-up order, and not to the application to obtain a winding-up order.

In *Richter v Bloempro CC and Others*³⁸ Bam J differed from the finding in *ABSA Bank Ltd v Summer Lodge*³⁹ that liquidation proceedings include the final liquidation process after the granting of the final liquidation order. The learned judge held that it was not the legislature's intention to make it possible to launch business rescue proceedings after a final liquidation order has been granted.

The Supreme Court of Appeal in *Richter v ABSA Bank Ltd*⁴⁰ clarified the issue in respect of section 131(6) of the 2008 Act. Dambuza AJA held that the term "liquidation proceedings" does not refer only to a pending application for a liquidation order but includes the process of winding-up of a company after a final liquidation order has been granted, and that liquidation refers to the entire process by which a company's existence is brought to an end by its deregistration after its assets have been redistributed. He further held that the court *a quo*⁴¹ erred in its reasoning that a company's existence is terminated by a final liquidation order since the correct position is that the company continues to exist, but the control of its affairs is transferred to the liquidator.

In terms of section 348 of the 1973 Act, the liquidation of a company is deemed to commence with the presentation to court of the application for liquidation and continues until the company has been finally wound-up and the Master's certificate is published in the Government Gazette, thus confirming the dissolution of the company.⁴² The 2008 Act provides for the existence of a company until deregistered by the Companies and

³⁸ (69531/2012) [2014] ZAGPPHC 120.

³⁹ 2013 (5) SA 444 (GNP).

⁴⁰ (20181)/2014) – [2015] ZASCA 100 (1 June 2015).

⁴¹ *Richter v Bloempro CC and Others* (69531/2012) [2014] ZAGPPHC 120.

⁴² *Richter v ABSA Bank Limited* 2015 para 10.

Intellectual Property Commission.⁴³ (hereafter referred as the Commission). Presentation to the court refers to the time when the application is filed with the Registrar of the court and not the time when it is heard by the judge.⁴⁴ Time refers to a specific point in time not the date of the presentation to the court.⁴⁵

Historically, the terms “liquidation” and “winding-up” have been used interchangeably in the context of dissolving a company.⁴⁶ Similarly, the terms are used interchangeably in sections 79, 80, 81 and 82 of the 2008 Act and in relation to the process of liquidation both before and after the final liquidation order has been granted, including the final stages of the winding-up of the company.⁴⁷ In terms of section 348 of the 1973 Act, the winding-up of a company by the court is deemed to commence at the time of presentation to the court of the application for winding-up.⁴⁸ The commencement of liquidation is determined with reference to the provisional order if a provisional order is set aside and a new final order is issued on the same day.⁴⁹

In *Diener NO v Minister of Justice and Others*⁵⁰ the Supreme Court of Appeal had to decide whether when business rescue proceedings are converted into liquidation proceedings, the date of liquidation is the date of commencement of business rescue proceedings or the date when the liquidation application is filed. It held that the effective date of liquidation is the date when the application for liquidation was filed.⁵¹

⁴³ Established by s 185 of the Companies Act 71 of 2008.

⁴⁴ See *Venter v Farley* 1991 (1) SA 316 (W) 319 H – 320 F.

⁴⁵ *Development Bank of Southern Africa Ltd v Van Rensburg* 2002 (5) SA 425 (SCA).

⁴⁶ *Richter v ABSA Bank Limited* 2015 para 11.

⁴⁷ *Ibid* para 11.

⁴⁸ Also see *Engen Petroleum Ltd v Goudis Carriers (Pty) Ltd (in liquidation)* 2013.

⁴⁹ *Nel and Others NNO v The Master* 2002 (3) SA 354 (SCA).

⁵⁰ (926/2016) [2017] ZASCA 180 (1 December 2017).

⁵¹ *Ibid* para 56.

2.4 Commencement of Liquidation Proceedings in Respect of Insolvent Companies

2.4.1 Commencement by Special Resolution

In terms of the 1973 Act, the voluntary winding-up of a company which is unable to pay its debts may be commenced by its members with a special resolution which provides for a creditors' winding-up of the company. All the powers of directors cease upon the liquidation of the company.⁵²

Voluntary winding-up may be the voluntary winding-up of a solvent company in terms of the 2008 Act.⁵³ However, the provisions for the voluntary winding-up by members in sections 343 and 350 of the 1973 Act which applied to solvent companies have been repealed.⁵⁴

The voluntary winding-up of an insolvent company may be commenced with by its creditors and the provisions of sections 343 and 351 of the 1973 Act should apply. In *Botha v Van den Heever NO*⁵⁵ the court held that despite the confusing wording of section 80 of the 2008 Act, a resolution for the voluntary winding-up of an insolvent company must comply with the provisions of the 1973 Act and not the 2008 Act.

2.4.2 Commencement by Court Application

An insolvent company may be wound-up by a high court following an application made by the company itself, a creditor, a member of the company or certain officials.⁵⁶ The application takes the form of a notice of motion coupled with an affidavit supporting the facts on which the applicant relies for relief.⁵⁷ Notice of the application must be served on the company, unless the application is brought by the company itself.⁵⁸ Section 344 of the 1973 Act sets out the circumstance under which a company may be wound up by the

⁵² Cronje *SARIPA Programme in Insolvency Law and Practice* (2016) 414.

⁵³ See s 80 of the Companies Act 71 of 2008.

⁵⁴ Cronje *SARIPA Programme in Insolvency Law and Practice* (2016) 392.

⁵⁵ [Unreported] Case No. 40406. 2012 High Court Pretoria (23 July 2012).

⁵⁶ S 346 of the Companies Act 61 of 1973.

⁵⁷ Cassim (2012) 920.

⁵⁸ *Ibid.*

court, inability to pay debts being the circumstance most often relied upon in practice. In a number of cases the other circumstance most often relied upon is when “it appears to the court just and equitable that the company should be wound up”.⁵⁹

Although there is no requirement to prove advantage for creditors in a liquidation application, if an applicant can prove an advantage this can influence the court’s discretion in the applicant’s favour.⁶⁰ Sometimes, the court will grant a provisional winding-up order so as to give creditors and other parties an opportunity to object on the return day of the *rule nisi*.⁶¹ If at the hearing of the *rule nisi*, a court is not so satisfied, it shall dismiss the application and set aside the provisional order, or require further proof of the matters set forth in the application and postpone the hearing for a reasonable period, but not *sine die*.⁶²

In *Standard Bank of South Africa Ltd v Midnight Feast Properties 4 (Pty) Ltd*⁶³ the court held that in terms of section 131(6) of the 2008 Act an application for liquidation is not suspended by an application for business rescue which has not been served as required by the Act.

The liquidation of solvent companies is regulated by the 2008 Act, which indicates that the structure of insolvency laws in South Africa is fragmented.

2.5 Effective Date of Liquidation

The effective date of liquidation depends on the method used to apply for liquidation. If the liquidation of an insolvent company was commenced with a special resolution of shareholders, the effective date will be the date of the registration in terms of section 200 of the special resolution authorising the winding-up.⁶⁴

⁵⁹ Cronje *SARIPA Programme in Insolvency Law and Practice* (2016) 401.

⁶⁰ Sharrock *et al* (2012).15. Magardie Companies in Financial Distress During Business Rescue Proceedings. (LLM mini-dissertation 2016 UP)

⁶¹ *Ibid.*

⁶² S 12(2) of the Insolvency Act 24 of 1936.

⁶³ (31795/2014) [2017] ZAGP JHC 15 (7 February 2017).

⁶⁴ S 340(2) of the Companies Act 61 of 1973.

Where the liquidation order has been granted pursuant to an application to the High Court, *the effective date of liquidation is dated retrospectively* back to the date of the presentation of the application for the winding-up to the Registrar of the High Court.⁶⁵ This enables the liquidator to set aside impeachable dispositions made in the intervening period.

2.6 Legal Effects of a Liquidation Order

It is of central importance to understand the consequences of a liquidation order for some of the key stakeholders in the liquidation process since some of these consequences give rise to problems when business rescue is countenanced when liquidation proceedings are already in progress. Some of these are briefly discussed below.

2.6.1 Effect on the Company's Legal Status

In *Richter v Bloempro CC and Others*,⁶⁶ Bam J held that upon liquidation a company is denuded of its original status. However, the Supreme Court of Appeal in *Richter v ABSA Bank Limited*⁶⁷ disagreed with this postulation and held that the company continues to exist even after a final liquidation order, and all that happens is change of control over the company – which is transferred to the liquidator.

The company's estate is effectively frozen and a *concursum creditorium* comes into being from the commencement date of liquidation. This prevents the preference of certain creditors above others. Legal proceedings against the company are held in abeyance until the appointment of a provisional liquidator by the Master of the High Court.⁶⁸ Control of all assets of the company vests in the Master and ultimately in the liquidator appointed by the Master. Any change of the legal status of the company or of its members without the approval of the liquidator is void.

⁶⁵ S 348 of the Companies Act 61 of 1973; also see *Vermeulen v CC Bauermeister (Edms) Bpk* 1982 (4) SA 159 (T) 162

⁶⁶ (69531/2012) [2014] ZAGPPHC 120; 2014 (6) SA 38 GP (14 March 2014).

⁶⁷ *Richter v ABSA Bank Limited* 2015 para 10.

⁶⁸ S 359 of the Companies Act 61 of 1973.

Upon the granting of the final liquidation order, directors are divested of all power and unauthorised dispositions can be impeached. Section 82 of the 2008 Act provides for the continuous existence of the company until deregistered by the Commission.

2.6.2 Effect on the Rights of Creditors

Once a provisional liquidation order is granted, a *concursum creditorium* is established and the interests of creditors as a group enjoy preference over the interests of individual creditors.⁶⁹ The debtor relinquishes control of his estate and cannot burden it with any further debts. A creditor's right to recover his claim in full by judicial proceedings falls away and is replaced by the right, on proving a claim against the insolvent estate, to share with all other proved creditors in the proceeds of the estate assets.⁷⁰ The provisions of section 52 of the Insolvency Act apply *mutatis mutandis* to the right of any creditor to vote at any meeting of creditors.⁷¹

The primary purpose of the existence of insolvency law is to benefit creditors, and a court will not sequester a debtor's estate unless it is shown that the sequestration will be to the advantage of creditors.⁷² Accordingly, liquidation will not be ordered if the assets in the debtor company's estate will be dissipated by placing the estate under liquidation and there will be nothing left over for creditors.

The lodging of an application for leave to appeal against a liquidation order does not suspend the operation and execution of the order as contemplated in section 18(1) of the Superior Courts Act No. 10 of 2013 since insolvency proceedings are inherently urgent.⁷³

2.6.3 Effect on the Rights of Directors

Directors lose control of the company upon the granting of a final liquidation order. Control of the assets of the company then vests in the Master and thereafter in the liquidator.⁷⁴

⁶⁹ *Richter NO v Riverside Estates (Pty) Ltd* 1946 OPD 209 223. Also see *Walker v Syfret NO* 1911 AD 141 66.

⁷⁰ Sharrock *et al* (2012). 4.

⁷¹ S 412(2) of Act 61 of 1973.

⁷² Sharrock *et al* (2012). 4.

⁷³ See *Ex Parte Nell and Others NO* 2014 (6) SA 545 (GP) (28 July 2014).

The company is not divested of its assets.⁷⁵ Furthermore, the directors retain the residual power to oppose the final liquidation order and to nominate an alternative director to do that.⁷⁶ Section 353 of the 1973 Act clarifies the effect of a voluntary winding-up on directors.

Section 415(1) of the 1973 Act provides that at any meeting creditors of the company that is being wound-up due to its insolvency, the Master, presiding officer, liquidator and any creditor who has a proved claim, may interrogate any director or subpoenaed person about the company, its business or affairs, and its property. The purpose of the interrogation is *inter alia* to determine liability in terms of section 423 and 424 of the 1973 Act, as well as sections 22, 163 and 218 of the 2008 Act.

2.6.4 Effect on the Rights of Shareholders

In a compulsory liquidation process, the appointed liquidator is not required to report to any shareholder or provide updates on proceedings.⁷⁷ Shareholders have no legal right to this information, and a liquidator is not required to convene a shareholders meeting.

The transfer of shares of the company being wound-up is void if effected after the commencement of the winding-up without the approval of the liquidator.⁷⁸ Every disposition of property by the company being wound-up is void unless the court orders otherwise.⁷⁹

Shareholders are entitled to a dividend in the (unlikely) event of a surplus after the payment in full of costs and claims of creditors, with interest up to the date of payment. Any surplus must be distributed amongst the members according to their rights and

⁷⁴ S 20(1)(a) of the Insolvency Act 24 of 1936.

⁷⁵ Cronje SARIPA Programme in Insolvency Law and Practice (2016) 414.

⁷⁶ *Ibid.*

⁷⁷ Global Forum on Law, Justice and Development: Rome Conference, 23 – 24 June 2016. “The Rights and Obligations of Shareholders under South African Insolvency Laws”. <http://www.globalforumljd.org/sites/default/files/docs/events/Presentation%20notes%20Rights%20and%20obligations%20of%20shareholders%20under%20South%20African%20insolvency%20laws.pdf> (Accessed 27 May 2018).

⁷⁸ S 341 of the Companies Act 61 of 1973.

⁷⁹ S 341(2) of the Companies Act 61 of 1973.

interests in the company.⁸⁰ Unless otherwise provided, shareholders share *pari passu* in proportion to the number of ordinary shares held by them.⁸¹

A court may at any time after the commencement of a winding-up, on the application of a liquidator, creditors or shareholders make an order staying or setting aside the proceedings or for the continuance of any voluntary winding-up on such terms and conditions as the court deems fit.⁸² Shareholders have the right to lodge objections to the liquidation and distribution account lodged with the Master by the liquidator prior to its confirmation.⁸³

2.6.5 Effect on the Rights of Employees

In terms of the Insolvency Act,⁸⁴ once the estate of the employer is sequestrated, all contracts of service are suspended and only terminated 45 days after the appointment of the final liquidator or trustee. The suspension is aimed at providing for the transfer of the contracts to a new buyer of the business in terms of section 197A of the Labour Relations Act⁸⁵ in the event that the business is sold as a going concern. Therefore, unlike in the past, insolvency now suspends contracts of service and no longer terminates them. The employees then have an unliquidated concurrent claim against the insolvent estate due to the breach of contract.

Pursuant to the suspension of their contracts, employees are not required to tender their services and are not entitled to remuneration or employment benefits in accordance with the suspended contracts or service,⁸⁶ but they are entitled to unemployment benefits in terms of the Unemployment Insurance Act 30 of 1966, subject to the provisions of that Act.

⁸⁰ S 342(1) of the Companies Act 61 of 1973.

⁸¹ Blackman *et al Commentary on the Companies Act*. Vol. 3 (Juta & Co Ltd: 2002) 14 – 66.

⁸² S 354(1) of the Companies Act 61 of 1973.

⁸³ S 407(1) of the Companies Act 61 of 1973.

⁸⁴ S 38 of Act No. 24 of 1936.

⁸⁵ Act No.66 of 1995.

⁸⁶ S 38(2) of the Insolvency Act 24 of 1936.

A liquidator of a company may terminate the contracts after the required consultations as regards possible measures to save or rescue the business or part of it.⁸⁷ As indicated above, if the liquidator and an employee have not reached agreement on continued employment, the suspended contract of service is terminated 45 days after the appointment of a final liquidator. An employee whose contract of service has been terminated has a preferent claim⁸⁸ for severance benefits in terms of section 41 of the Basic Conditions of Employment Act 75 of 1997 (s38 (10)–(11)).⁸⁹

2.6.6 Effect on the Rights of the Business Rescue Practitioner

Where business rescue proceedings are superseded by liquidation proceedings, the business rescue practitioner's claim for remuneration and expenses does not enjoy a 'super-preference'⁹⁰ upon the liquidation of the company.

In a Supreme Court of Appeal judgment in *Diener NO v Minister of Justice and Others* (926/2016) [2017] ZASCA [at paragraph 49], Plasket AJA held that section 135(4) and section 143(5) of the 2008 Act do not create a "super-preference" over all other creditors (whether secured or not) after the costs of the liquidation when business rescue proceedings are converted into liquidation proceedings. Accordingly, if the company in business rescue is liquidated, section 97⁹¹ costs must be paid first before the business rescue practitioner's fees are paid. Therefore, the business rescue practitioner is not automatically entitled to his costs — he needs to submit and prove his claim in accordance with section 44 of the Insolvency Act.

It is also noteworthy that, in terms of section 140(4) of the 2008 Act, if business rescue proceedings are converted to liquidation proceedings, the business rescue practitioner who oversaw the business rescue process is ineligible to be appointed as a liquidator of the company.

⁸⁷ S 38(5) and (6) of the Insolvency Act 24 of 1936.

⁸⁸ S 98(1)(a)(iv) of the Insolvency Act 24 of 1936.

⁸⁹ Sharrock *et al* (2012) 92.

⁹⁰ Delpont. *Henochsberg on the Companies Act 71 of 2008* (Vol 1) 500.

⁹¹ Insolvency Act. 24 of 1936.

2.7 Termination of Liquidation Proceedings

The liquidation procedure begins with the application and continues until the company has been finally wound-up and a Master's certificate is published in the Government Gazette, which confirms the dissolution of the company.⁹²

In terms of section 354 of the 1973 Act, the court may, at any time after the commencement of a winding-up on the application of any liquidator, creditor or member, and on proof to the satisfaction of the court that all proceedings in relation to the winding-up ought to be stayed or set aside, make an order staying or setting aside the proceedings, or for the continuance of any voluntary winding-up on such terms and conditions as the court may deem fit.

Liquidation proceedings can also be brought to a screeching halt by an application for business rescue. In terms of section 131(6) of the 2008 Act, liquidation proceedings already under way can be suspended and converted into business rescue proceedings.⁹³ The applicant must satisfy the court that all reasonable steps have been taken to notify all affected persons known to the applicant, by delivering a copy of the court application to them in accordance with Regulation 7.⁹⁴ The court held in *Standard Bank of South Africa Limited v Gas 2 Liquids (Pty) Ltd*⁹⁵ that there must be service and notification in terms of section 131 of the 2008 Act before it can be said that the business rescue application has been "made" and that the liquidation proceedings have been suspended.

In the case of *Van Staden v Angel Ozone Products CC and Others*,⁹⁶ Legodi J made a far-reaching decision that liquidation proceedings, in the context of section 131 of the 2008 Act, are concluded once there is a final liquidation and distribution account confirmed by

⁹² *Richter v ABSA Bank Limited* (20181/2014) [2015] ZASCA 100, (1 June 2015).

⁹³ See *Richter v ABSA Bank Limited* (20181/2014) – [2015] ZASCA 100 (1 June 2015). Also see *Van Zyl NO v Engelbrecht* 2014 5 SA 312 FP, as well as *PMG Kyalami (Pty) Ltd and Another v Firstrand Bank Ltd, Wesbank Division* [2015] 1 All SA 437 (SCA).

⁹⁴ *Engen Petroleum Limited v Multi Waste (Pty) Limited and Others* 2012 5 SA 596 (GSJ) paras 15 – 24.

⁹⁵ (45543/2012) [2016] ZAGPJHC 38; 2017 2 SA 56 (GJ) (10 March 2016). Also see *ABSA Bank Limited v Summer Lodge (Pty) Ltd* 2013 5 SA 444 GNP; and *Taboo Trading 232 (Pty) Ltd v Pro Wreck Scrap Metal CC and Others* 2013 6 SA 141 KZP.

⁹⁶ 2012 JDR 1945 (GNP).

the Master, and that winding-up proceedings are part and parcel of liquidation proceedings. This means that liquidation proceedings can be stayed by an application from an affected person applying for business rescue even after the final winding-up order has been granted at any time up until the deregistration of the company.

Dissolution and deregistration are not synonymous, albeit they both have the effect of terminating the legal existence of a company. A company is dissolved as of the date on which its name is removed from the Companies Register, unless its removal is by reason of the transfer of its registration to a foreign jurisdiction as contemplated in section 82(5) of the 2008 Act.⁹⁷

⁹⁷ Sharrock *et al* (2012) 268.

CHAPTER 3: COMMENCEMENT AND TERMINATION OF BUSINESS RESCUE PROCEEDINGS

3.1 Introduction and Overview of Business Rescue

In this chapter the objectives of business rescue will be highlighted, the commencement of business rescue explored, and the effects of business rescue proceedings on the rights of affected persons traversed, especially because some of these have spawned applications for business rescue when liquidation proceedings are already in progress. Finally, the termination of business rescue proceedings will be covered.

It is widely accepted that the trend towards business rescue started with the introduction of the Chapter 11 Procedure in the Bankruptcy Reform Act of 1978 in the United States of America.⁹⁸ The 2008 Act⁹⁹ introduced business rescue into the South African business landscape as a new corporate rescue procedure. The need for a new business rescue mechanism was prompted, *inter alia*, by the apparent failure of judicial management as a corporate rescue procedure. In terms of the 1973 Act,¹⁰⁰ a company experiencing financial difficulty to pay its debts but not wanting to be liquidated, had two options, namely: judicial management or compromises.¹⁰¹

Judicial management was introduced into South Africa by the Companies Act of 1926.¹⁰² The judicial management regime set out in Chapter 15 of the 1973 Act was an attempt to provide an alternative to that of liquidating companies which were on the brink of insolvency, even though it was generally never accepted as an effective corporate restructuring process.¹⁰³ Consequently, it never took off as an alternative to liquidation and was regarded as a “dismal failure”.¹⁰⁴ It is against this backdrop that business rescue can

⁹⁸ Kloppers (1999) *Stell LR* 215.

⁹⁹ Companies Act 71 of 2008.

¹⁰⁰ Companies Act 61 of 1973.

¹⁰¹ Ss 427 and 311 of Act 61 of 1973, respectively.

¹⁰² Act 46 of 1926.

¹⁰³ Levenstein *An Appraisal of the New South African Business Rescue Procedure* (unpublished LLD Thesis 2015 UP) (*hereafter* Levenstein LLD) 58.

¹⁰⁴ Burdette 2004 *SA Merc LJ*.

be viewed as another attempt to achieve the objectives of judicial management and to rehabilitate financially-distressed companies.

Section 427(1) of the 1973 Act stipulated the requirements for a judicial management order. It is submitted that these requirements have unwittingly resulted in the failure of judicial management as corporate rescue procedure. In fact, judicial management was generally viewed as a precursor to liquidation and courts, as well as academics, perpetuated the negative ambiance around the procedure. As indicated in chapter 1, in *Le Roux Hotel Management (Pty) Ltd and Another v E Rand (Pty) Ltd*,¹⁰⁵ the court reviewed the history of judicial management and by implication, the reasons for its limited success, including the restrictive approach which the courts had followed in its interpretation and application.

The definition of “business rescue” is set out in section 128(1)(b) of the 2008 Act which reads as follows:

“Business rescue” means proceedings to facilitate the rehabilitation of a company that is financially distressed by providing for:

- (i) the temporary supervision of the company, and of the management of its affairs, business and property;
- (ii) a temporary moratorium on the rights of claimants against the company or in respect of property in its possession; and
- (iii) the development and implementation, if approved, of a plan to rescue the company by restructuring its affairs, business, property, debt and other liabilities, and equity in a manner that maximises the likelihood of the company continuing in existence on a solvent basis or, if it is not possible for the company to continue in existence, results in a better return for the company’s creditors or shareholders than would result from the immediate liquidation of the company.”¹⁰⁶

¹⁰⁵ 2001 2 SA 727 (CPD) para 39.

¹⁰⁶ S 128(1)(b).

It should be noted that Chapter 6 of the 2008 Act has also been made applicable to the business rescue of close corporations facing financial difficulties by item 6 of Schedule 3 to the 2008 Act.¹⁰⁷

3.2 Objectives of Business Rescue

The objectives of business rescue are enunciated in the definition above, the overriding ones being:

- (a) the facilitation of the rehabilitation of a company that is in financial difficulty in order to achieve solvency; or
- (b) if that is not possible, the achievement of a better return for creditors or shareholders than would occur if the company were to be liquidated.¹⁰⁸ This has now become popularly known as BRIL.¹⁰⁹

In *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others*¹¹⁰ Brand JA, when delivering the unanimous decision of the full bench, confirmed [paragraph 26] that the objectives of business rescue are twofold — that is, either to return the company to solvency or to provide a better deal for creditors and shareholders than they would receive through liquidation.

Joubert, Van Eck and Burdette¹¹¹ succinctly state that the primary aim of business rescue is to resuscitate faltering companies. “Financial distress” is defined in the 2008 Act¹¹² and the definition of business rescue is in line with the international principles of corporate rescue culture.¹¹³

¹⁰⁷ See s 66(1A) of the Close Corporations Act 69 of 1984 as amended in 2011.

¹⁰⁸ S 128(1)(b)(iii).

¹⁰⁹ “A better return than in liquidation”.

¹¹⁰ (2013) 3 All SA 303 (SCA).

¹¹¹ Joubert, Van Eck and Burdette “Impact of labour law on South Africa’s new corporate rescue mechanism” 2011 *The International Journal of Comparative Labour Law and Industrial Relations* 65–84.

¹¹² The 2008 Act s 128(1)(f).

¹¹³ Levenstein LLD 286.

The court in *Koen and Another v Wedgewood Golf & Country Estate (Pty) Ltd and Others*¹¹⁴ made an important observation that the legislature has recognised that the liquidation of companies often occasions significant collateral damage, both economically and socially, with attendant destruction of wealth and livelihoods, hence it is in the public interest that the incidence of such adverse socio-economic consequences should be avoided where reasonably possible.¹¹⁵ This observation augers well with one of the purposes of the 2008 Act, which is to promote compliance with the Bill of Rights in the application of company law as provided for in the Constitution.¹¹⁶ The devastating effects of liquidations have been recognised by courts.¹¹⁷ Governments also abhor the demise of corporate taxpayers as the tax base gets eroded when companies go into liquidation.¹¹⁸

In *Maroos and Others v GCC Engineering (Pty) Ltd and Others*¹¹⁹ the court held that the purpose of business rescue orders is to provide for efficient rescue and recovery of financially distressed companies in a manner that balances the rights and interests of all relevant stakeholders. Accordingly, it makes sense to attempt to rescue ailing businesses suffering a temporary setback but which do have the potential to survive if they are given some assistance and time to overcome their financial difficulties.¹²⁰ Moreover, if the business rescue culture is inculcated, whilst balancing the rights and interests of all key stakeholders,¹²¹ the cost of capital will invariably be lowered.

Accordingly, the chief aim of business rescue is to rescue the business undertaken by the company as a going concern, as opposed to rescuing the company or juristic person.¹²² The company is not only given some respite by virtue of the moratorium,¹²³ but it is also

¹¹⁴ 2012 2 SA 378 (WCC).

¹¹⁵ Also see *Commissioner: South African Revenue Services v Beginsel & Others* 2013 1 SA 307 (WCC) para 62.

¹¹⁶ Subsection 7(a) of the Companies Act 71 of 2008.

¹¹⁷ See *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd* 609/2012 [2013] ZASCA 68 and *Others*; 2013 4 SA 539 (SCA); 2013 3 All SA 303 (SCA) (27 May 2013).

¹¹⁸ Joubert, Van Eck and Burdette 2011 *The International Journal of Comparative Labour Law and Industrial Relations* 65–84.

¹¹⁹ 2017 ZAGPPHC 297.

¹²⁰ Loubser “Judicial management as a business rescue procedure in South African corporate law” 2004 SA Merc LJ 137.

¹²¹ See subsection 7(k) of the 2008 Act.

¹²² See *Oakdene Square Properties and Others supra* para 12.

¹²³ See s 133 of the 2008 Act regarding the statutory moratorium.

afforded an opportunity to reorganise and restructure itself under the temporary supervision of an external practitioner within the parameters of Chapter 6 of the 2008 Act.

By law, a creditor of an ailing company had a right *ex debito justitiae* (as of right) to liquidate the company if he could establish the requirements set out in the 1973 Act.¹²⁴ This was consonant with the private law principle that "agreements must be honoured" (*pacta sunt servanda*). This legal position has now somewhat changed with the advent of the modern international wave of business rescue.¹²⁵ Of significance is the fact that, in respect of business rescue, the 2008 Act gives top priority to the interests of stakeholders in contradistinction to the interests of creditors and shareholders which take centre-stage in liquidation proceedings.¹²⁶

The Supreme Court of Appeal underscored in *Diener NO v Minister of Justice and Others*¹²⁷ that central to the provisions of Chapter 6 of the 2008 Act is the intention to create an efficient, regulated and effective mechanism to facilitate the rescue of companies in financial distress in a way that balances the rights and interests of stakeholders.

3.3 Commencement of Business Rescue Proceedings

In terms of Chapter 6 of the 2008 Act, there is a dual gateway to business rescue proceedings, namely: the voluntary commencement of business rescue by way of a resolution passed by the company's directors;¹²⁸ and the compulsory commencement of business rescue by way of a court application launched by an affected person.¹²⁹

¹²⁴ *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) 739 para 42 referring to *Bahnemann v Fritzmore Exploration (Pty) Ltd* 1963 (2) SA 249 (TPD) at 250 H – 251 A.

¹²⁵ See *ABSA Bank Ltd v New City Group (Pty) Ltd* (unreported case no. 45670/2011; *Cohen v New City Group (Pty) Ltd and Another* (unreported case no. 28615/2012) (21 August 2012) (GSJ).

¹²⁶ See s 7(k) of Act No. 71 of 2008.

¹²⁷ (926/2016) [2017] ZASCA 180 (1 December 2017) para 40.

¹²⁸ S 129(1) of Act 71 of 2008.

¹²⁹ S 131(1) of the 2008 Act. An "affected person" is defined in s 128(1)(a) of the Act. The definition proffers very broad *locus standi* in respect of applications for business rescue.

3.3.1 Voluntary Commencement by Way of a Board Resolution

The board of a company can voluntarily commence business rescue proceedings if it has reasonable grounds to believe that the company is financially distressed¹³⁰ and there appears to be a reasonable prospect of rescuing the company.¹³¹ A resolution to this effect may not be adopted if liquidation proceedings have been initiated by or against the company and the resolution is of no effect until it has been filed.¹³² An affected person is afforded a right to object to voluntary business rescue by applying to court to set aside a business rescue resolution on the grounds set out in section 130(1)(a) of the 2008 Act. The court in *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 (Pty) Ltd and Others*,¹³³ held that the phrase “reasonable prospect” indicates that “something less is required than that the recovery should be a reasonable probability”.

In *Propspec Investments v Pacific Coasts Investments 97 Ltd*,¹³⁴ Van der Merwe J held that vague averments and mere speculative suggestions will not suffice. The Supreme Court of Appeal in *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others*,¹³⁵ held that the requirement for business rescue is a lesser requirement than the “reasonable probability” which was the yardstick for placing a company under judicial management in terms of section 427(1) of the 1973 Act. However, it requires more than a mere *prima facie* case or an arguable possibility, and it must be a prospect based on reasonable grounds.¹³⁶ In turn, the court has to exercise discretion in the wide sense and make a value judgement.¹³⁷ In *Newcity Group (Pty) Ltd v Allan David Pellow NO and Others*,¹³⁸ the Supreme Court of Appeal had to consider whether a company had a reasonable prospect of rescue as contemplated in section 131(4)(a) of the 2008 Act, and confirmed that “‘reasonable prospect’ means a yardstick higher than a mere *prima facie* case or an ‘arguable possibility’ but lesser than a reasonable probability”.

¹³⁰ A financially distressed company is defined in s 128(1)(f) of the 2008 Act.

¹³¹ S 129(1)(a) and (b) of the Companies Act 71 of 2008.

¹³² S 129(2)(a) and (b) of the 2008 Act.

¹³³ 2012 2 SA 378 (WCC).

¹³⁴ 2013 1 SA 542 (FB) para 11.

¹³⁵ 2013 3 All SA 303 (SCA).

¹³⁶ *Ibid* para 29.

¹³⁷ *Ibid*.

¹³⁸ (577/2013) [2014] ZASCA 162 (1 October 2014).

In the case of the *African Banking Corporation of Botswana Ltd v Kariba Furniture Manufacturers and Others*,¹³⁹ the Supreme Court of Appeal held that the directors voting in favour of business rescue must truly believe that the prospects of rescue exist and this belief must be based on a concrete foundation.

In terms of section 132(1) of the 2008 Act, business rescue proceedings begin when a directors' resolution is filed to place the company under supervision in terms of section 129(3) of the Act; or directors apply to court for consent to file a resolution in terms of section 129(5)(b) of the Act. Therefore, voluntary business rescue commences on the date of the filing of the directors' resolution with the Companies and Intellectual Property Commission¹⁴⁰ (hereinafter referred to as the Commission).

3.3.2 Compulsory Commencement by Way of a Court Application

As stated above, section 131(1) of the 2008 Act governs the commencement of business rescue by means of a court order. The section provides that an affected person "may apply to court at any time for an order placing the company under supervision and commencing business rescue proceedings".¹⁴¹ The applicant in such proceedings is required to serve a copy of the application¹⁴² on the company and the Commission, and to notify every other affected person of the application in the prescribed manner.¹⁴³ The court may grant the relief sought if it is satisfied that the company is financially distressed, or it has "failed to pay over any amount in terms of an obligation under or in terms of a public regulation, or contract, with respect to employment-related matters", or it is otherwise just and equitable to do so for financial reasons, and there are reasonable prospects for rescuing the company.¹⁴⁴ It still remains unclear whether compulsory business rescue commences at

¹³⁹ (228/2014) [2015] ZASCA 69 (20 May 2015).

¹⁴⁰ Established by s 185 of Act 71 of 2008.

¹⁴¹ Also see *Employees of Solar Spectrum Trading 83 (Pty) Ltd v AFGRI Operations Limited and Another* [2012] ZAGPPHC 359 (16 May 2012), which attests to the broader *locus standi* provided for in respect of business rescue applications.

¹⁴² The court held in *Engen Petroleum Ltd v Multi Waste (Pty) Ltd and Others* 2012 (5) SA 596 (GSJ) para 14 that the application must be in the Long Form Notice of Motion (Form 2(a)) and not the *ex parte* Form 2.

¹⁴³ S 131(2) of the Companies Act 71 of 2008.

¹⁴⁴ S 131(4) of the Companies Act 71 of 2008.

the time an application is made to court in terms of section 131(1) or on the date of the order for business rescue.¹⁴⁵

If the aim is to procure a better return than would result from immediate liquidation, Kubushi J held in *Target Shelf 284 CC v The Commissioner of South African Revenue Service*¹⁴⁶ that the applicant, as the master of the suit (*dominus litis*), must convince the court that there are reasonable prospects of achieving a better return for creditors than would result from immediate liquidation.

Business rescue proceedings also begin when a court makes an order placing a company under supervision during the course of liquidation proceedings, or proceedings to enforce a security interest, as contemplated in section 131(7) of the 2008 Act. If at the time an application is made for compulsory commencement of business rescue, liquidation proceedings have already been commenced by or against the company, the application will suspend liquidation proceedings until the court has adjudicated upon the application, or the business rescue proceedings end, if the court makes the order applied for.¹⁴⁷

In *Richter v Bloempro CC and Others*,¹⁴⁸ Bam J held that the legislature intended that business rescue proceedings be initiated before the liquidation order and that in order to bring an application for business rescue, the final liquidation order would first have to be set aside. The application for the rescission of judgment was accordingly dismissed. However, this decision was overturned by the Supreme Court of Appeal in *Richter v ABSA Bank Ltd*¹⁴⁹ in the context of section 131(6) of the 2008 Act. Accordingly, the route of business rescue remains open in spite of a final winding-up order having been granted.

¹⁴⁵ Levenstein 2017 para 8.4.

¹⁴⁶ (34775/14) [2015] GP (13 October 2015) para 51.

¹⁴⁷ Section 131(6) of the Companies Act 71 of 2008.

¹⁴⁸ (69531/2012) [2014] ZAGPPHC 120; 2014 (6) SA 38 GP (14 March 2014).

¹⁴⁹ (20181/2014) [2015] ZASCA 100 (1 June 2015).

3.4 Legal Effects of Business Rescue proceedings on the Rights of Affected Persons

It is of cardinal importance to understand the effects of business rescue proceedings on the rights of affected persons because, in essence, some of these effects prompt applications for business rescue when liquidation proceedings are already under way. However, it is not the thrust of the study to explore every nook and crevice in respect of the effects business rescue on the rights of affected persons. Only a synopsis of some of the most salient effects is given below.

3.4.1 Effect of Proceedings on the Rights of Shareholders and Directors

Section 137 of the 2008 Act enunciates the effect of business rescue proceedings on shareholders and directors. An alteration in the classification or status of a company's issued securities is invalid, unless it takes place by way of a transfer of the securities in the ordinary course of business, or in terms of a court order, or pursuant to an approved business rescue plan.¹⁵⁰

Levenstein¹⁵¹ recounts some of the effects of business rescue on shareholders, including:

- a) Receiving some benefit by having their shares bought by an offer or buyer of the company;
- b) Sometimes shares purchased at a negligible value, with creditors receiving a sufficient dividend to enable them to vote in the plan at the required thresholds; and
- c) Getting a vote on a plan only when their rights are being affected.

According to Levenstein¹⁵², shareholders seem to recognise that the principle of a better return than would result from liquidation is acceptable and more preferable to liquidation.

¹⁵⁰ S 137(1) of the Companies Act 71 of 2008.

¹⁵¹ Levenstein 2017 para 10.3.1.3.

¹⁵² *Ibid.*

Throughout the business rescue proceedings, the business rescue practitioner is vested with full management control of the company in substitution for its board and management.¹⁵³ However, each director of the company must:

- a) Continue to exercise the functions of a director, subject to the authority of the business rescue practitioner;
- b) Continue to discharge the duty to exercise any management function within the company in accordance with the express instructions or direction of the business rescue practitioner, to the extent that it is reasonable to do so; and
- c) Attend to the requests of the business rescue practitioner at all times and provide him/her with any information about the company's affairs as may reasonably be required.¹⁵⁴

In terms of section 137(4), if the board of directors, or one or more directors, purport to take any action on behalf of the company that requires the approval of the business rescue practitioner, the action is void unless approved by the business rescue practitioner.

Directors remain bound to disclose conflicts of interest or those of related persons.¹⁵⁵ They are also obliged to co-operate with and assist the business rescue practitioner.¹⁵⁶ The business rescue practitioner may apply to court for an order removing a director from office.¹⁵⁷

Unlike in the case of liquidations, the business rescue practitioner does not have any prescribed formal procedure to investigate the affairs of the company and to interrogate directors and management in respect of their actions prior to filing for business rescue as provided for in sections 417 and 418 of the 1973 Act. According to Levenstein¹⁵⁸, this is a flaw which encourages directors to opt for business rescue as opposed to placing the

¹⁵³ S 140(1)(a) of the Companies Act 71 of 2008.

¹⁵⁴ S 137(2) – (3) of the Companies Act 71 of 2008.

¹⁵⁵ S 137(2)(c) of the Companies Act 71 of 2008.

¹⁵⁶ S 142(1) – (4) of the Companies Act 71 of 2008.

¹⁵⁷ S 137(5) of the Companies Act 71 of 2008.

¹⁵⁸ Levenstein 2017 para 10.3.1.12.

company into liquidation so as to circumvent the interrogations associated with liquidations.¹⁵⁹

3.4.2 Effect of Proceedings on the Rights of Creditors

In the case of *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others*,¹⁶⁰ the Supreme Court of Appeal confirmed an interpretation of the meaning of business rescue that embodies the protection of creditors. Although the business rescue regime is construed as a shift away from the traditional creditor-oriented insolvency procedures that may be traced back to South Africa's English law roots, Bradstreet¹⁶¹ opines that this case reassured creditors that their interests, even though they are no longer of paramount importance, are still afforded protection by the very definition of what business rescue seeks to achieve. Section 145 of the 2008 Act entrenches the participation of creditors during business rescue proceedings.

Section 133 of the 2008 Act provides for an *ex lege* automatic general moratorium on legal proceedings (including enforcement action) against the company after the commencement of liquidation proceedings. In *Cloete Murray NO and Another v First Rand Bank Limited*¹⁶² the Supreme Court of Appeal held that the cancellation of a contract concluded prior to the commencement of business rescue proceedings by a creditor does not constitute enforcement action as contemplated in section 133(1). The court reached this decision despite the liquidators' contention that if the moratorium does not prohibit the cancellation of contracts, an inevitable demise of business rescue would result. The court held [at paragraph 35] that sections 136(2)(a) and 154(2) of the 2008 Act offer sufficient safeguards to prevent the result envisaged by the liquidators.¹⁶³ However, this ruling has

¹⁵⁹ S 415(1) of the Companies Act No. 61 of 1973.

¹⁶⁰ (2013) 3 All SA 303 (SCA).

¹⁶¹ Bradstreet "Lending a Helping Hand — The Role of Creditors in Business Rescues?" 1 December 2013 *De Rebus* <http://www.derebus.org.za/lending-helping-hand-role-creditors-business-rescues/> (Accessed 21 August 2017).

¹⁶² (20104/2014) [2015] ZASCA 39 (26 March 2015).

¹⁶³ S 136(2)(a) enables the business rescue practitioner to prevent a creditor from instituting action and repossessing or attaching property which is in the company's possession. Section 154(2) states that once a business rescue plan has been approved and implemented, a creditor is not entitled to enforce any debt owed by the company prior to the commencement of business rescue process — except to the extent permitted in the business rescue plan.

been criticised by some lower courts and academics as having been wrongly decided. There is a view that the phrase, “enforcement action”, should be defined in Chapter 6 of the 2008 Act, as it is the case in Australian legislation.

The Supreme Court of Appeal in *Chetty v Hart*¹⁶⁴ held that there is no absolute bar against legal proceedings during the moratorium and a creditor may ask for the business rescue practitioner’s written permission and, if refused, may approach the court under section 133(1)(b). The court further held that the creditor may approach the court directly under this provision for leave to institute legal proceedings without having asked for the business rescue practitioner’s consent. In addition, the court further held that the exercise of a creditor’s rights is suspended during the moratorium but that this is balanced by the other protections afforded in the section itself.

In the case of *Sean Crowder Bastos Tuna v Pioneer Foods (Pty) Ltd*¹⁶⁵, the court held that if a company is under supervision for purposes of business rescue, the provisions of sections 133(1) of the 2008 Act allowing for a moratorium in respect of payment of debts by a principal debtor do not extend to a surety. Wepener J held that the moratorium is directed exclusively at protecting the interests of the company in business rescue. In *Investec Bank Ltd v Bruyns*,¹⁶⁶ Rodgers AJ held that the statutory moratorium in section 133(1) on claims against the company under business rescue was a defence purely personal to the principal debtor, namely the company, and could not be raised by the surety. Therefore, it is a defence *in personam* and is not available to a surety, which means that a creditor may sue a surety for the debts of a company in business rescue in spite of the moratorium on claims against the company. It is also noteworthy that in terms of section 155(9) any compromise or arrangement entered into pursuant to section 155 will not affect the position of a surety.¹⁶⁷

Section 135 of the 2008 Act deals with the ranking of creditors’ claims in terms of business rescue proceedings. In *Merchant West Capital Solutions (Pty) Ltd v Advance Technologies*

¹⁶⁴ (20323/14) [2015] (6) SA 424 para 45.

¹⁶⁵ (A5001/2015) [2016] ZAGP JHC 298 (18 November 2016).

¹⁶⁶ 2012 (5) SA 430 WCC (14 November 2011).

¹⁶⁷ Also see *Tuning Fork (Pty) Ltd t/a Balanced Audio v Greeff* 2014 4 SA 521 (WCC).

and *Engineering Company and Another*,¹⁶⁸ the court held that the ranking of claims in a business rescue is as follows:

- (i) The business rescue practitioner;
- (ii) Employees' remuneration after business rescue;
- (iii) Secured lenders in respect of post-commencement finance;
- (iv) Unsecured lenders in respect of post-commencement finance;
- (v) Secured lenders and other creditors before business rescue;
- (vi) Employees' remuneration due and payable before business rescue proceedings;
and
- (vii) Unsecured lenders and creditors before business rescue proceedings.

In terms of section 137(1) of the 2008 Act, during business rescue proceedings, the classification or status of any issued securities of a company cannot be altered, other than by way of a transfer of securities in the ordinary course of business, except to the extent that the court otherwise directs, or to the extent contemplated in an approved business rescue plan.

Section 133(1)(c) of the 2008 Act permits the setting-off of claims made by the company in any legal proceedings whether commenced before or after the business rescue proceedings began. However, Levenstein¹⁶⁹ submits that this provision might be in conflict with section 154(2) of the Act.

Secured creditors, especially banks, are usually not in favour of business rescue as they believe the process allows the company to continue to erode its capital. As a result, they "ride roughshod" over the interests of unsecured (concurrent) creditors.¹⁷⁰ Needless to say, unsecured creditors are likely to benefit from business rescue because of the inherent likelihood to receive a better return than in a liquidation scenario.

With the exception of employment contracts and contracts to which section 35A or section 35B of the insolvency Act would apply if the company was to be liquidated, the business rescue practitioner may suspend, entirely or partially, or liquidate conditionally,

¹⁶⁸ [2013] ZAGP JHC 109 para 21. Also see *Redpath Mining South Africa (Pty) Ltd v Marsden NO and Others* (18486/2013) [2013] ZAGP JHC 148.

¹⁶⁹ Levenstein 2017 para 10.3.1.4.

¹⁷⁰ *Ibid* para 10.3.1.7.

any agreement or provision of an agreement to which the company was a party at the commencement of the proceedings.¹⁷¹ Where the business rescue practitioner exercises the power, the other party to the agreement may only assert a claim for damages against the company.¹⁷² Where the business rescue practitioner suspends a provision relating to security granted by the company, the creditor is entitled to be regarded as a secured creditor when the company wants to dispose of the property given as security.¹⁷³

Section 155 of the 2008 Act provides for a compromise or arrangement akin to the compromise or arrangement set out in terms of section 311 of the 1973 Act. It is submitted that this provision cannot be deemed to be a cram-down on dissenting creditors because of the manner in which section 155(7)(a) is couched, which provides that “the company may apply to court for an order approving the proposal”.¹⁷⁴

The Supreme Court of Appeal in *African Banking Corporation of Botswana Ltd v Kariba Furniture Manufacturers and Others*,¹⁷⁵ held that a binding offer made in terms of section 153(1)(b)(ii) to a creditor who opposes a business rescue plan is not automatically binding on the offeree unless there is acceptance, and once made it cannot be retracted or amended. This ruling was made based on the law of contract. In an earlier case of *KJ Foods CC v First National Bank*¹⁷⁶, the court held that the court has to do a purposive interpretation as enjoined by section 39(2) of the Constitution and a balancing act has to be done between the rights of role players when dealing with section 153. It further stated that the court must be slow to countenance liquidation where the interests of creditors are not affected by business rescue.¹⁷⁷

¹⁷¹ S 136(2)(a) of the Companies Act 71 of 2008.

¹⁷² S 136(3) of the Companies Act 71 of 2008.

¹⁷³ S 136(2A)(c) of the Companies Act 71 of 2008.

¹⁷⁴ Klopper and Bradstreet “Averting liquidations with business rescue: Does a section 155 compromise place the bar too high?” 2014 *Stell LR* 25

¹⁷⁵ (228/2014) [2015] ZASCA 69 (20 May 2015).

¹⁷⁶ (75627/2013) [2015] ZAGPPHC 221 (23 April 2015) para 10.

¹⁷⁷ *Ibid.*

3.4.3 Effect of Proceedings on the Rights of Employees

The rights of employees are of prime concern in the 2008 Act as articulated in section 136, read with sections 144 and 5(4). Joubert and Loubser¹⁷⁸ observe that the rights of employees are not only extensive but are also entrenched throughout the entire business rescue proceedings, and these rights emanate from three sources: the inclusion of employees in the definition of “affected persons” who enjoy a wide array of powers and rights; their recognition as creditors in cases where the company owes them any remuneration that was due before the commencement of business rescue; and based on the mere fact that they are employees of the company.

Section 144 of the 2008 Act deals extensively with the rights of employees during business rescue proceedings. The underlying philosophy is to try and prevent the negative results stemming from companies in distress having to lay-off or retrench employees.¹⁷⁹ The court held in *Lidino Trading 580 CC v Cross Point Trading (Pty) Ltd in Re: Mabe v Cross Point Trading 215 (Pty) Ltd*¹⁸⁰ that the interests of employees feature prominently as the object of business rescue proceedings.

Section 136(1)(a) of the 2008 Act provides that, during business rescue proceedings, employees of the company continue to be employed on the same terms and conditions as immediately before the proceedings except to the extent that changes occur in the ordinary course of attrition or the employees and the company agree upon different laws. Any employee retrenchments contemplated in a business rescue plan are subject to sections 189 and 189A of the Labour Relations Act 66 of 1995 and other applicable labour legislation.¹⁸¹ While the company is under business rescue, the power to terminate the services of managerial employees vests in the business rescue practitioner.¹⁸²

¹⁷⁸ Joubert and Loubser “Executive directors in business rescue: Employees or something else?” 2016 *De Jure* 95–104.

¹⁷⁹ *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others* (2013) 3 All SA 303 (SCA).

¹⁸⁰ [2012] JOL 2905 (FNB) para 19.

¹⁸¹ S 136(1)(b) of the Companies Act 71 of 2008.

¹⁸² S 140(1)(c)(i) of the Companies Act 71 of 2008.

In business rescue proceedings which precede a liquidation, the company is obliged to retain the employees' services, and their salaries are regarded as post-commencement expenses and thus they have a "super-preferential" status.¹⁸³ Section 144(2) of the 2008 Act does not place a limit on the claims of employees for arrear salaries and other outstanding amounts, which is more favourable than the provisions of the Insolvency Act¹⁸⁴ which stipulate a three-months arrear salary and a maximum of R12 000 if the company goes in to liquidation.

3.4.4 Effect of proceedings on the Rights of Liquidators

Although liquidators are not included in the definition of "affected person,"¹⁸⁵ liquidators' rights do get affected when liquidations are suspended by business rescue applications.¹⁸⁶ This scenario is dealt with in slightly more detail in the next chapter from the vantage point of the effects of permitting business rescue after the commencement of liquidation proceedings.

3.5 Termination of Business Rescue Proceedings

In terms of the 2008 Act, business rescue proceedings end when the court sets aside a resolution¹⁸⁷ or order to commence business rescue, or converts the proceedings to liquidation proceedings;¹⁸⁸ the business rescue practitioner files a notice of termination of the proceedings with the Commission;¹⁸⁹ or a business rescue plan has been proposed and rejected without action being taken to extend the proceedings;¹⁹⁰ or the plan has been

¹⁸³ Cronje *SARIPA Programme in Insolvency Law and Practice* (2016).

¹⁸⁴ S 98A of the Insolvency Act 24 of 1936.

¹⁸⁵ S 128(1)(a) of the Companies Act 71 of 2008.

¹⁸⁶ See ss 131(6) and 131(7) of the Companies Act 71 of 2008; and *Richter v ABSA Bank Limited* (20181/2014) – [2015] ZASCA 100 (1 June 2015).

¹⁸⁷ S 130(1)(a) of the Companies Act 71 of 2008.

¹⁸⁸ S 132(2)(a) of the Companies Act 71 of 2008. Also see *Sibakhulu Construction (Pty) Ltd v Wedgewood Village Golf Country Estate (Pty) Ltd* (27956/2010) [2011] ZAWCHC 439. The SCA in *Panamo Properties (Pty) Ltd and Another v Nel NO* (35/2014) [2015] ZASCA 76, 2015 5 SA 63 (SCA) confirmed that the termination of business rescue proceedings is specifically dealt with in s 132(2) of the 2008 Act, and that business rescue is also terminated when the court sets the initiating resolution aside.

¹⁸⁹ S 132(2)(b) of the Companies Act 71 of 2008.

¹⁹⁰ S 132(2)(c)(i) of the Companies Act 71 of 2008.

adopted and notice of substantial implementation of the plan has been filed by the business rescue practitioner.¹⁹¹

Regarding the conversion of business rescue proceedings into liquidation proceedings, in the case of the *Commissioner of South African Revenue Service v Primrose Gold Mines (Pty) Ltd*,¹⁹² the court held that the business rescue practitioner was the person suited to apply to court for the discontinuance of business rescue proceedings. However, in *Target Shelf 284 CC v The Commissioner South African Revenue Service*,¹⁹³ Kubushi J concluded that, on a proper reading of section 132(2)(a), it is not specifically stated who should apply to set aside the business rescue proceedings or to convert them into liquidation proceedings. The learned judge held that it was not the intention of the legislature to hold creditors to ransom and to prevent them from exercising their contractual rights for an inordinate length of time. In the circumstances of the case, the creditors were entitled to apply for the conversion of the business rescue proceedings and reverting to the business rescue practitioners would have been highly prejudicial to creditors.

The duration of business rescue proceedings is subject to a prescribed length of time. If they have not ended within three months (or longer if the court permitted this on the application of the business rescue practitioner), the business rescue practitioner must prepare a report on the progress of the proceedings, with updates at the end of each subsequent month until the end of the proceedings.¹⁹⁴ In *South African Bank of Athens Ltd v Zennies Fresh Fruit CC, Business Partners Limited v Zennies Fruit CC and Another*,¹⁹⁵ the court held that the mechanisms of business rescue were not designed to protect the company endlessly to the detriment of the rights of its creditors.

¹⁹¹ S 132(2)(c)(ii) of the Companies Act 71 of 2008.

¹⁹² (56581/2014) [2014] 26 ZAG PPHC (2 September 2014).

¹⁹³ (34775/14) [2015] GP (13 October 2015) para 74.

¹⁹⁴ S 132(3)(a) of the Companies Act 71 of 2008.

¹⁹⁵ (7681/17) [2018] ZAWCHC 11; [2018] 2 All SA 276 (WCC); 2018 3 SA 278 (WCC) para 43.

CHAPTER 4: THE LAUNCHING OF BUSINESS RESCUE AFTER THE COMMENCEMENT OF LIQUIDATION PROCEEDINGS: A CONCISE ANALYSIS

4.1 Introduction and Overview of the Launching of Business Rescue After the Commencement of Liquidation Proceedings

This chapter will attempt to answer the question whether business rescue proceedings can be launched when liquidation proceedings are already in progress and whether this is still a legal conundrum. This is the crux of the study. Some of the benefits and drawbacks of allowing business rescue proceedings after a final liquidation order has been granted will also be briefly explored.

Sections 131(1);¹⁹⁶ 131(6), 131(7) and 136(4) of the 2008 Act clearly envisage the commencement of business rescue proceedings after the granting of a final liquidation order. As it can be seen from the previous chapter, there have been many prominent cases where courts have grappled with this scenario.

4.2 The Interplay between Liquidation Proceedings and Business Rescue Proceedings

The interplay between liquidation proceedings and business rescue proceedings may be discerned in chapters 2 and 3 above in spite of the fact that the goals of the two processes are diametrically opposed.

The provisions of section 131(7) read with section 135(4) of the 2008 Act implicitly envisage the conversion of liquidation proceedings into business rescue proceedings, no matter how far the liquidation and winding-up proceedings might have progressed.¹⁹⁷ In terms of section 131(1), only affected persons, not the directors of the company, may apply to court for an order to place a company under supervision and to commence business rescue proceedings after liquidation proceedings have commenced. The launch

¹⁹⁶ “[A]n affected person may apply ‘at any time’...”

¹⁹⁷ Delpont *Henochsberg on the Companies Act 71 of 2008 and Commentary*. 2011 Vol 1 Lexis Nexis 471.

of business rescue proceedings does not alter the legal status of the company in liquidation, but merely stays the implementation of the winding-up order.¹⁹⁸

Section 131(6) of the 2008 Act provides that if the application for business rescue is refused after adjudication, the suspension of liquidation proceedings is ended. In *Firststrand Bank Limited v Imperial Crown Trading 143 (Pty) Ltd*,¹⁹⁹ the court held that if the application is granted, the suspension of liquidation proceedings endures until the business rescue proceedings end, in terms of section 132(2) of the 2008 Act. Section 135(4) contemplates a scenario where business rescue proceedings are converted into liquidation proceedings.²⁰⁰

In the case of *Oakdene Square Properties (Pty) and Others v Farm Bothasfontein (Kyalami) Pty Ltd and Others*,²⁰¹ the Supreme Court of Appeal made it clear that, while business rescue may seem to be an obvious choice, the option of liquidation should not be ignored, especially in instances where there are allegations of improper disposition of the company's assets. In these circumstances, liquidation would be more advantageous to creditors and shareholders since the liquidator is empowered, and has the machinery, to investigate and claw back certain assets lost as a result of impeachable transactions in terms of the Insolvency Act.²⁰²

In *Diener NO v Minister of Justice and Others*,²⁰³ the SCA held that, albeit Chapter 6 of the 2008 Act makes provision for business rescue failing in some instances and being converted into liquidation proceedings, its overwhelming focus is on business rescue and the mechanics of business rescue, rather than on liquidation.

¹⁹⁸ *ABSA Bank Limited v Makuna Farm CC* [2014] 3 SA 86 (GJ) at 8; and *ABSA Bank Limited v Cardio-Fitness*

Properties (Pty) Ltd and Others (46194/13) [2014] ZAGJHC JHC 40.

¹⁹⁹ 2012 2 All SA 560 (KZD).

²⁰⁰ Also see *Diener NO v Minister of Justice and Others* (926/2016) [2017] ZASCA 180; and *Yatzee Investments CC (Under Business Rescue) v Capx Finance (Pty) Ltd and Others* (3300/2015) [2015] ZAWCHC 117.

²⁰¹ (2013) 3 All SA 303 (SCA) (26 August 2015).

²⁰² 24 of 1936. See section 340(1) of the companies Act 61 of 1973.

²⁰³ (926/2016) [2017] ZASCA 180. Also see *Pouroullis v Market Pro Investments 106 (Pty) Ltd* (201370/2015) [2016] ZAGPJHC 12; and 2001 *Management Services (Pty) Ltd and Another v Anappa* (88079/14) [2016] ZAGPPHC 353.

4.3 The Legal Conundrum

Before (and even after) the SCA *Richter* judgment, courts have reached dissonant conclusions on the commencement of business rescue proceedings post the granting of a final liquidation order but have remained bound by the *Richter* decision due to the *stare decisis* principle. When this judgment was passed in June 2015 it caused a lot of turmoil in the realm of corporate insolvency in South Africa.

Prior to this judgment, the court held in *Van Staden v Angel Ozone Products CC and Others*²⁰⁴ that business rescue proceedings can convert liquidation proceedings no matter how far these proceedings are. As indicated in chapter 3 in *Richter v Bloempro CC and Others*,²⁰⁵ it was held that a business rescue application cannot be made in law after a final liquidation order has been made, unless that order is set aside on appeal. However, these cases were not on all fours with each other. *Van Staden* interpreted section 131(7) of the 2008 Act, while *Bloempro CC and Others* interpreted section 131(6). The SCA *Richter* judgment held that section 131(6) has the effect of suspending liquidations even after a final liquidation order had been granted.

Cases in support of the SCA's approach in the *Richter* judgment are: *Van Staden*; *ABSA Bank Ltd v Summer Lodge (Pty) Ltd* per Mr Acting Justice Van der Bijl ("Van der Bijl AJ"); *ABSA Bank Ltd v Summer Lodge (Pty) Ltd* per the learned Mr Justice Makgoba ("Makgoba J"); and *ABSA Bank Ltd v Makuna Farm CC* per the learned Mr Justice Boruchonitz ("Boruchonitz J").

Cases which hold opposing views include the following: *Zonnekus Mansion* per Mr Acting Justice Ferreira ("Ferreira AJ"); *Molyneux* per Rogers J; and *Richter* in court *a quo* per Bam J.

²⁰⁴ (54009/11) [2012] ZAGPHC 328; 2013 (4) SA 630 (GNP) (12 October 2012).

²⁰⁵ (69531/2012) [2014] ZAGPPHC 120. Also see Phungula 2017 *Stell LR* 584.

The SCA in the *Richter* judgment did not refer to the *Molyneux* case, nor the judgments of Van der Bijl AJ and Boruchowitz J.²⁰⁶

4.4 The *Stare Decisis* Principle

The principle of *stare decisis* is a judicial command enjoining courts to respect a decision already made in a given area of law. The practical application of the *stare decisis* doctrine is that courts are bound by their previous decisions, as well as the decisions of the courts superior to them.²⁰⁷

In *Credex Finance (Pty) v Kuhn*,²⁰⁸ Didcott J made a statement of principle which is summarised in the headnote to that judgment:

“The doctrine of judicial precedent would be subverted if judicial officers, of their own accord or at the instance of litigants, were to refuse to follow decisions binding on them in the hope that the appellate tribunals with the power to do so might be persuaded to reverse the decisions and thus vindicate them *ex post facto*. Such a course cannot be tolerated.”

The SCA in *Firstrand Bank Limited v Kona and Another*²⁰⁹ underscored that the observation of the doctrine of precedent and *stare decisis* is mandatory.

The Constitutional Court in *Camps Bay Rate Payers' Association and Another v Harrison and Another*²¹⁰ also expressed itself unequivocally regarding the observance by courts of the maxim *stare decisis* (or the doctrine of precedent). Therefore, the doctrine remains sacrosanct.

Against this backdrop, it is submitted that the SCA *Richter* judgment is binding on all courts in respect of the commencement of business rescue proceedings when liquidation

²⁰⁶ *Van der Merwe and Others v Zonnekus Mansion (Pty) Ltd and Others* (4653/2015) [2015] ZAWCHC 90; [2015] 3 All SA 659 (WCC) (10 June 2015) para 15.

²⁰⁷ Also see Bayethe “The doctrine of precedent and the value of s39(2) of the Constitution” April 2017 *De Rebus*.

²⁰⁸ 1977 3 SA 482 (N).

²⁰⁹ (20003/2014) [2015] ZASCA 11 (13 March 2015).

²¹⁰ 2011 4 SA 42 CC paras 28 - 301.

proceedings are already under way. This is the current legal position despite the criticism of the decision by some lower courts.²¹¹

Be that as it may, there appears to be new legal conundrums and challenges stemming from the decision to permit business rescue applications after the granting of a liquidation order. There are new legal lacunae and holes to be plugged. Some of these are highlighted in 4.6 below. Therefore, the SCA *Richter* judgment is not a panacea for all the problems created by the interface between liquidation proceedings and business rescue proceedings. It is submitted that the judgment might have also muddied the waters with respect to the country's corporate insolvency law.

4.5 Merits of Countenancing Business Rescue after the Commencement of Liquidation Proceedings

4.5.1 Advancing the Purposes of the New Companies Act as Set Out in Section 7 of the Act

As already pointed out in chapter 3, the spirit and purport of the new Companies Act is to engender a corporate rescue culture in order to realise the wide-ranging benefits of saving companies facing an unfortunate financial tailspin. To this end, business rescue, creditor workouts, compromises and other interventions aimed at saving the company ought to be encouraged.

In *Cardinet (Pty) Ltd v Wedgewood Golf and Country Estate (Pty) Ltd (in liquidation)*,²¹² Nyman AJ went to great lengths to ascertain that business rescue would result in a better return not only for the secured creditor that opposed the business rescue application, but also for all its creditors and stakeholders, than would result from the immediate liquidation of *Wedgewood*. It is a great positive that a good business can be revived through business

²¹¹ See *Van der Merwe and Others v Zonnekus Mansion (Pty) Ltd and Another* 2015 3 All SA 659 (WCC) para [17] where Ferreira J remarked as follows:

“I am bound by the Richter SCA judgment, even though I respectfully differ therewith, given the reasoning in the judgments of Bam J and Roger J in *Richter v Bloempro CC and Others* 2014 6 SA 38 (GP) and *Molyneux and Another v Patel and Others* (14618/2014) [2014] ZA WCHC 191 (27 November 2014) cases, respectively”.

²¹² (19599/2012) WCC [2013] (25 February 2013).

rescue and the involvement of the business rescue practitioner, even after the company had been effectively closed down through liquidation.²¹³ It is noteworthy though that business rescue does not necessarily entail the complete recovery of a company to the extent that, after the procedure, the company will have regained its solvency, its business or normal trading will have been restored, and its creditors paid.²¹⁴

4.5.2 Provision of a Last-gasp Window for New Investors to Turn Around the Company

The beleaguered debt-laden company might have only needed recapitalisation by way of a cash injection in order to move the needle and bring it back into the black. In *Richter v ABSA Bank Ltd*,²¹⁵ Dambuza AJA made the following dictum:

“It takes little to imagine instances developing after the issue of the final order that could lead to the circumstances of a company improving radically, such that it would become profitable if allowed to trade. It could be awarded a contract for which it had earlier tendered or secure funding for future projects; a major creditor might indicate a willingness to subordinate its claim. Accordingly, in the scheme of things, where, during liquidation, evidence becomes available that business rescue proceedings will yield a better return for shareholders and creditors and jobs will be retained, there could be no reason to deny business rescue only because a company is in final liquidation. Indeed, to allow it to do so would fall into the very scheme of business rescue envisaged by the Act and fulfil the objectives of providing for the revival of a financially distressed company with all its attendant social benefits”.

Permitting business rescue after the commencement of liquidation proceedings gives an opportunity to new independent investors who may want to invest in the company and

²¹³ Modise “Positive and negative effects of a business rescue order after liquidation” 2013 *Hogan Lovells Publications* 1.

²¹⁴ Cassim *et al Contemporary Company Law* 2012. Also see Burdette (part 1) 2004 *SA Merc LJ* 257.

²¹⁵ (20181/2014) [2015] ZASCA 100 para 15.

provide the required working capital. Cognisance should be taken of the fact that a company may only be commercially insolvent due to liquidity problems and liquidation used as an instrument *in terrorem* to exact payment from it. More often than not, companies run into cash flow problems due to significant delays in receiving payment from their customers, such as Government Departments, when in fact they show a positive balance sheet whereby assets exceed liabilities.²¹⁶ It is conceivable that there are businesses that can be saved at the time when the debtor company is already insolvent.²¹⁷

4.6 Demerits of Countenancing Business Rescue After the Commencement of Liquidation Proceedings

4.6.1 Conflict with the Definition of Business Rescue

The definition of business rescue makes it clear that the procedure is aimed at rehabilitating “financially distressed” companies. In terms of the 2008 Act, financial distress means that it appears to be reasonably unlikely that the company will be able to pay all its debts as they become due and payable within the immediately ensuing six months or it appears to be reasonably likely that the company will become insolvent within the immediately ensuing six months.²¹⁸ According to Phungula,²¹⁹ if it is accepted that business rescue has the effect of suspending liquidation proceedings post the final liquidation order, the purpose of business rescue cannot be achieved. The presumption is that when the final liquidation order is granted, the court is satisfied that the company is already insolvent²²⁰ and can no longer be able to pay its debts. It is submitted that applying for business rescue after the liquidation order has been granted is tantamount to second-guessing or gainsaying the court that issued the liquidation order in the first place. Furthermore, the definitions of financial distress and insolvency could inadvertently get

²¹⁶ Also see the Australian case of *The Bell Group Ltd (In Liq) v Westpac Banking Corporation* [No.9] 2008 WASC 239 para 1070.

²¹⁷ Burdette “Some initial thoughts on the development of a modern and effective business rescue model for South Africa (part 2)” 2004 *SA Merc LJ* 409.

²¹⁸ Section 128(1)(f) of the Companies Act 71 of 2008.

²¹⁹ Phungula “Proceedings over proceedings: How and when are liquidation proceedings suspended by an application for business rescue proceedings?” 2017 *Stell LR* 584.

²²⁰ S 4 of the Companies Act 71 of 2008 sets out the solvency and liquidity test.

conflated. It still remains unclear what should happen to the final liquidation order and the appointment of liquidators.²²¹

The fact that liquidators are not included in the definition of “affected person” in section 28 of the 2008 Act creates a quandary when a business rescue application is launched when liquidation proceedings are already in progress. As a result, it is not very clear how liquidation proceedings can be suspended with a business rescue application. However, in *Standard Bank of South Africa Limited v Gas 2 Liquids (Pty) Ltd*²²² where the court was faced with the task of interpreting section 131 of the 2008 Act, Satchwell J held that the mere lodgement of papers and issuance of a case number is not adequate to trigger a suspension of liquidation proceedings. The learned judge further held [at paragraph 23] that the provisional liquidator is entitled to service, as well as the Companies and Intellectual Property Commission, and all affected persons must be notified of the application.

4.6.2 Uncertainty Regarding the Control of the Company Already in Liquidation

It is still not clear who is in control of the company, its business and its assets when liquidation proceedings are suspended pending the outcome of a business rescue application. Strime²²³ expressed a serious concern regarding this state of affairs, especially if the period of suspension runs into a number of weeks or months, as is normal with opposed applications.

In *Maroos and Others v GCC Engineering (Pty) Ltd and Others*,²²⁴ Fabricius J held that the powers of the liquidators are suspended and the control of the assets vests in the Master of the High Court²²⁵ in accordance with the provisions of section 361(2) of the 1973 Act. The learned judge further held that the powers and obligations of the previous directors

²²¹ *Richter v Bloempro CC and Others* (69531/2012) [2014] ZAGPPHC 120 (14 March 2014) para 18(vi).

²²² (45543/2012) [2016] ZAGPJHC 38; 2017 (2) SA 56 (GJ) (10 March 2016).

²²³ Strime “Who is in control when a liquidation application is suspended pending the outcome of a business rescue hearing?” 2017 *Fluxmans Attorneys* <http://www.fluxmans.com/control-liquidation-application-suspended-pending-outcome-business-rescue-hearing-section-1316-companies-act-71-2008-act-colin-s/> (Accessed 21 May 2018).

²²⁴ (36777/2017) [2017] ZAGPPHC 297 (15 June 2017).

²²⁵ Hereafter “the Master”.

are re-vested with the same directors to control and manage the company pending the determination of the business rescue application so as to promote the objects of the Act. *In casu*, an independent manager was appointed to manage the affairs of the company and was instructed to provide security to the Master for the performance of his duties. The manager was further instructed not to sell any of the assets of the company without the written consent of the Master.

This ruling is being appealed and has been set down to be heard on 16 November 2018.

4.6.3 The Role of Courts in Business Decisions

In order to allow business rescue post-liquidation, the court has to consider whether the application for business rescue is *bona fide* or not and whether the company can be successfully rescued.²²⁶ It is submitted that in order to make a proper and objective assessment of the reasonable prospect of rescuing the company, the court is required not only to assess the *bona fides* of the applicant(s), but to also have a sound business acumen to understand the facts presented before it. The decision to embark on business rescue ought to be purely a business decision underpinned by proper due diligence. In *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 (Pty) Ltd and Others*,²²⁷ Eloff AJ complained that the information presented before the court was vague, hence there was no reason for him to believe that there was any prospect of the business of the respondent to be rescued. Nwafor,²²⁸ opines that the role of the court is simply to draw rational inferences from the facts placed before it. In the Australian court's case of *Vink v Truckwell (No. 2)* the court indicated that courts are not equipped to engage in business decisions and can only draw inferences from available facts, which may not yield the expected outcome in certain instances.

It is respectfully submitted that, in some instances, the bench might not be able to see the wood for trees in order to make a correct decision in the face of sophisticated commercial

²²⁶ See *Richter v ABSA Bank Ltd* (20181/2014) [2015] ZASCA 100; 2015 5 SA 57 (SCA).

²²⁷ (15155/2011) [2011] ZAWCHC 442; 2012 2 SA 423 (WCC) para 23. Also see *Pouroullis v Market Pro Investments 106 (Pty) Ltd* (201370/2015) [2016] ZAGPJHC 12 paras 26 and 27.

²²⁸ Nwafor "Exploring the goal of business rescue through the lens of the South African Companies Act 71 of 2008" 2017 *Stell LR* 597.

facts presented before the court. Consequently, the court might be railroaded into granting illegitimate business rescue orders even in instances where the business rescue remedy is being used as a subterfuge to frustrate liquidation and leave creditors in the lurch. It is indisputable that business rescue requires a lot of expertise from the courts as well, but the capacity of the bench in this regard is debatable.

By the same token, it is not the intention of the 2008 Act that in legitimate cases courts should grant post-liquidation business rescue orders which turn out to be a pyrrhic victory. The creation of specialised commercial courts to deal, *inter alia*, with business rescue applications might help address some of the concerns raised under this sub-heading, including speeding up the hearing of business rescue cases. The role of courts in business decisions is still a vexed issue.

4.6.4 Disruptions to Liquidation Proceedings

Permitting business rescue after the commencement of liquidation proceedings disrupts liquidation processes and puts liquidators in an unenviable position. A number of problems are created for liquidators, creditors and other stakeholders when the liquidation process is disrupted by a business rescue order, including the following:

- (a) How to undo the work already done by the liquidator in the process of dismantling the company;
- (b) How to recover the portions of the business already sold by the liquidator as a going concern and the disposed of or realised assets;²²⁹
- (c) How to safeguard the rights and interests of creditors and shareholders against the diminution in the value of stock and encumbered assets due to use, depreciation and obsolescence;
- (d) How to immediately finance the liquidator's costs of securing assets whilst business rescue proceedings are in progress;²³⁰

²²⁹ Levenstein 2017 para 8.3.2.

²³⁰ In *Cardinet (Pty) Ltd v Wedgewood Golf and Country Estate (Pty) Ltd (in Liquidation)*, the court ordered the applicant to indemnify the joint liquidators in respect of their reasonable fees and expenses incurred by them in the winding-up of Wedgewood.

- (e) Section 131(6) is silent on its effect on the powers of liquidators, as well as on the consequences of the suspension of liquidation proceedings;²³¹ and
- (f) Reversion of control of the assets and management of the company to the same directors who might have been the cause of the financial distress.²³²

As indicated earlier, business rescue can sometimes be used as a tool to frustrate liquidation. This can occur when various affected parties make applications for business rescue at different times during the winding-up process, resulting in repetitive disruptions and uncertainty regarding the liquidation process. In the case of *Van der Merwe and Others v Zonnekus Mansion (Pty) Ltd (in liquidation) and Another*,²³³ the court went to the extent of interdicting Mr Van der Merwe from launching further applications for the commencement of business rescue in respect of Zonnekus Mansion (Pty) Ltd without the prior written permission of the Senior Duty Judge of the Cape High Court. The court reached this decision after a series of four unsuccessful applications for an order to commence business rescue.

4.6.5 Abuse of the Business Rescue Procedure

The repetitive disruptions of liquidation proceedings mentioned in the preceding paragraph may be a palpable indication of the blatant abuse of the business rescue procedure. Admittedly, the broadening of the meaning of liquidation proceedings to include winding-up and de-registration has also opened up the business rescue process to abuse by (unscrupulous) affected persons.²³⁴

²³¹ Levenstein 2017 para 8.3.2, Delpont Henochsberg on the Companies Act 71 of 2008 and Commentary [at s131] opines that the suspension of liquidation proceedings entails the suspension of the “office of the liquidator” and no collection of, *inter alia*, assets by the liquidator can take place during the business rescue proceedings. Levenstein further submits that the liquidator becomes *functus officio* during the period of suspension.

²³² See *Rentacor (Pty) Ltd v Rheede and Barman* 1998 4 SA 469 (TPD) para 503; *PMG Motors Kyalami and Another v Firstrand Bank, Wesbank Division* 2015 1 All SA 437 (SCA); and *Maroos and Others v GCC Engineering (Pty) Ltd and Others* (36777/2017) [2017] ZAGPPHC 297 para 9.

²³³ (17150/2016) [2016] ZAWCHC 193 (19 December 2016).

²³⁴ Also see *Suzler Pumps (South Africa) (Pty) Ltd v O & M Engineering CC* (19740/2014) [2015] ZAGPPHC 59 where the court held that a business rescue application must not be filed as a knee-jerk reaction to thwart liquidation applications.

The court held in the case of the *Standard Bank of South Africa v Gas 2 Liquids (Pty) Ltd*²³⁵ that a business rescue application might be utilised by an obstructive debtor to avoid liquidation. In the most recent case of *Alderbaran (Pty) Ltd and Another v Bouwer and Others*,²³⁶ Davis AJ held that this case unequivocally illustrates the potential abuse of the business rescue remedy.

It is submitted that business rescue post-liquidation may be abused by (“delinquent”) directors as a provisional licence to trade recklessly in violation of the prohibition stipulated in section 22 of the 2008 Act in order to evade liquidation and keep creditors at bay.

Conversely, and in bizarre circumstances, between February and August 2018, the business rescue practitioners of Optimum Coal Mine (Pty) Ltd had to contend with 42 court cases instituted by the directors and creditors of the company who were trying to sabotage the business rescue process.²³⁷

4.6.6 Creation of Legal Uncertainty

Allowing business rescue applications at any stage of the liquidation process creates uncertainty in respect of liquidation proceedings. Van Niekerk²³⁸ is of the view that the SCA *Richter* judgment might cause harm to the legal belief that interpretations of statutes should advance legal certainty. Needless to say, the litany of court cases referred to above generates a lot of uncertainty regarding the liquidation process.

²³⁵ (45543/2012) [2016] ZAGPJHC 38; 2017 2 SA 56 (GJ) para 5.

²³⁶ (19992/2017) [2018] ZAWCHC 38; [2018] 3 All SA 71 (WCC) (22 March 2018) paras 1, 81 and 83.

²³⁷ Ryan “Business rescue practitioners face down 42 court cases from Gupta associates, creditors”. *Moneyweb*. 7 August 2018 <https://www.moneyweb.co.za/news/companies-and-deals/business-rescue-practitioners-face-down-42-court-cases-from-gupta-associates-and-creditors> (Accessed 29 August 2018).

²³⁸ Van Niekerk “Launching Business Rescue Applications in Liquidation Proceedings — (successfully) Flogging a Dead Horse? September 2015 *De Rebus* 164.

CHAPTER 5: A COMPARATIVE ANALYSIS: AUSTRALIA AND THE UNITED KINGDOM

As explained in chapter 1, South Africa and Australia have an Anglo history and share a common-law heritage. The company laws of Australia and South Africa are largely influenced by English law, thus it would make a lot of sense to do a comparative analysis with the United Kingdom. The recommendations laid down in the UNCITRAL Legislative Guide on Insolvency Law will also be briefly explored insofar as they relate to the conversion of liquidation proceedings to business rescue.

5.1 Australia

The Australian equivalent of business rescue is found in Part 5.3A of the 2001 Australian Corporations Act, as amended in 2007 (hereinafter referred to as the Act). Australia's corporate insolvency provisions form part of the country's general company law statute.²³⁹

5.1.1 Voluntary Administration

The business rescue procedure in Australia is known as voluntary administration.²⁴⁰ This procedure is applicable to a company which is insolvent or likely to be insolvent at some time in future.²⁴¹ In addition, the company must be capable of being rescued.²⁴² The board is empowered to appoint an administrator to look at ways of restructuring the business in order to turn it around, or make it attractive to buyers if it believes the company is or will become insolvent in the near future. In terms of the Act, a company is insolvent if it is unable to pay all its debts as and when they fall due.

It is noteworthy that voluntary administration in Australia is not necessarily a rescue procedure but a preliminary procedure to facilitate the possible rescue of a company.²⁴³ A

²³⁹ Levenstein LLD 114.

²⁴⁰ S 436A of the Corporations Act 50 of 2001.

²⁴¹ S 436A (1) of the Corporations Act 50 of 2001.

²⁴² S 436 of the Corporations Act 50 of 2001.

²⁴³ Keay "A Comparative Analysis of Administrative Regimes in Australia and the United Kingdom" 2008. In Omar (ed) *International Insolvency Law – Themes and Perspectives* 105.

company in need of rescue must first go into voluntary administration. The rescue of the company then commences after the signing of a deed of company arrangement with its creditors, which sets out the administrator's plan to rescue the company.²⁴⁴ Failure to agree upon a plan will usually lead the company to move on to liquidation procedures.

5.1.2 Commencement and Termination of Voluntary Administration

In Australia, voluntary administration commences when the administrator of the company is appointed²⁴⁵ following the initiation of the procedure by either the company, the liquidator or the person holding a charge over the whole or substantially the whole of a company's property. It is usually instigated by the directors of the company when they see insolvency looming with the hope that by appointing an administrator they may be able to overcome the company's problems and return to normal trading.²⁴⁶

The procedure terminates upon the occurrence of the specific circumstances set out in section 435C of the Act.²⁴⁷ An administration order could last up to four months, subject to the courts discretion.²⁴⁸

5.1.3 Switching from Liquidation to Voluntary Administration

Section 436A (2) of the Act provides that the board's right to appoint an administrator does not apply if a liquidator, or provisional liquidator, of the company has already been appointed. Anderson²⁴⁹ confirms that where the company is already being wound-up, neither the board nor the secured creditor can appoint an administrator, and there is no provision for a court to issue an order that an administrator be appointed. Section 436B (1) provides that a liquidator or provisional liquidator of a company may appoint an

²⁴⁴ Anderson "Viewing the proposed South African business rescue provisions from an Australian Perspective" 2008.

²⁴⁵ Section 435C of the Corporations Act 50 of 2001.

²⁴⁶ Australian Debt Solvers "The complete guide to business liquidation" 13 July 2018 <https://australiandebtsolvers.com.au/research-centre/a-guide-to-liquidation/> (Accessed 3 October 2018).

²⁴⁷ Museta "The development of business rescue in South African law". (LLM Dissertation UP 2011).

²⁴⁸ *Ibid.*

²⁴⁹ Anderson 2008 Potchefsroom Elektroniese Regsblad 1.

administrator of the company if he or she thinks that the company is insolvent, or is likely to become insolvent in future.

In terms of section 436D, an administrator cannot be appointed if the company is already under administration. Powers of the administrator while a company is under administration are set out in section 437A of the Act. In effect, the administrator assumes full control of the company's affairs, including dealing with the company's property and conducting investigations, if need be. He or she is entitled to form an opinion, *inter alia*, about whether it would be in the creditors' interests for the administration to end or for the company to be wound-up.²⁵⁰

The court has to adjourn the hearing of an application for an order to wind-up the company if the company is under administration and the court is satisfied that it is in the interests of the company's creditors for the company to continue under administration rather than be wound-up. Section 440A (3) prohibits the court from appointing a provisional liquidator of a company if the company is under administration and the court is satisfied that it is in the interests of the company's creditors for the company to continue under administration instead of having a provisional liquidator appointed.

Liquidation can either be voluntary (that is, decided by a resolution of members or creditors) or creditors vote for liquidation after the company has gone into voluntary administration or when a deed of company arrangement is terminated.²⁵¹ Involuntary liquidation occurs when the court appoints a liquidator to wind-up the company following an application by a creditor, a director or majority of shareholders.²⁵²

5.2 United Kingdom

The business rescue procedure in the United Kingdom is governed by the Insolvency Act of 1986, as amended by the Insolvency Act of 2000, and became operative on

²⁵⁰ S 438A of the Corporations Act No.50 of 2001.

²⁵¹ See se 439C of the Corporations Act No. 50 of 2001.

²⁵² Australian Debt Solvers "The complete guide to business liquidation" 13 July 2018
<https://australiandebtsolvers.com.au/research-centre/a-guide-to-liquidation/> (Accessed 3 October 2018).

29 December 1986. In terms of the English Insolvency Act, a company is insolvent if it is not able to pay all its debts as and when they fall due.²⁵³

5.2.1 Administration

The business rescue procedure in the United Kingdom is referred to as administration and the procedure is applicable to an insolvent company or to one that is likely to be insolvent.²⁵⁴ The administration procedure was introduced by the Insolvency Act of 1986 and was substantially revised by the Enterprise Act of 2002 to include a streamlined procedure allowing the company or its directors to appoint an administrator without the involvement of the court.²⁵⁵ It is intended for use as a rescue mechanism, the primary objective being to rescue the company as a going concern. Other options available to save a company in financial distress are administrative receiverships and company voluntary arrangements.²⁵⁶ Administrative receivership is historically the main option for a secured creditor with a floating charge over substantially the whole of the company's undertaking.²⁵⁷

Administration in the United Kingdom is sometimes said to be a precursor to business rescue. The company first has to sign an agreement with its creditors under a scheme of arrangement or creditor voluntary arrangement to facilitate the company's rescue.²⁵⁸

5.2.2 Commencement and Termination of Administration

In the United Kingdom, administration commences when the administrator is appointed at the instance of the holder of a floating charge, the company or its directors, or by means of a court order.²⁵⁹ The duration of administration runs concurrently with the tenure of the

²⁵³ Section 123 of the Act.

²⁵⁴ Keay (2008) 105.

²⁵⁵ Slaughter and May "An Introduction to English Insolvency Law" May 2015
<https://www.slaughterandmay.com/media/251437/an-introduction-to-english-insolvency-law.pdf>
(Accessed 16 April 2018).

²⁵⁶ Burdette (part 2) 2004 *SA Merc LJ* 409.

²⁵⁷ S 29 (2) of the Insolvency Act of 1986.

²⁵⁸ McCormack *Corporate Rescue Law: An Anglo-American Perspective* 2008 66.

²⁵⁹ Para 2 Schedule B1 to the Insolvency Act of 1986.

administrator.²⁶⁰ The appointment of an administrator ceases to have effect at the end of one year, beginning from the date on which it takes effect.²⁶¹ Nevertheless, the administrator's term of office may be extended by the court for a specified time through an application by the administrators but not for a period exceeding six months.²⁶²

Even though a company in the United Kingdom can achieve a successful financial re-organisation without the need to enter into any formal insolvency procedure, if creditors are not generally in support of the restructuring process or do not have confidence in the management of the company, it may be necessary to place the company under formal administration.²⁶³

5.2.3 Switching from Liquidation to Administration

Despite having unified insolvency legislation, the ease of switching from liquidation to business rescue (or vice versa) has not fully materialised in the Insolvency Act of 1986.²⁶⁴ Schedule B1 to the aforesaid Act makes provision for administration, and paragraph 37 allows a court to convert a liquidation to administration upon application by a floating charge holder. Paragraph 38 allows the liquidator of a company to apply to court for administration. A court may not order administration on a petition for winding-up even if the facts indicate that administration would be more appropriate.²⁶⁵ Conversely, an administration may be treated as a winding-up application.²⁶⁶

If an administrator files for the termination of the administration procedure because it has failed to achieve a rescue, the court does not have jurisdiction to order the winding-up of the company on the same application but has to file the prescribed petition for the winding-up of the company.²⁶⁷

²⁶⁰ Museta The Development of Business Rescue in South African Law (LLM Dissertation UP 2011).

²⁶¹ *Ibid.*

²⁶² Para 76(2)(a)–(b) of Schedule B1 to the Insolvency Act of 1986.

²⁶³ Levenstein LLD Thesis.

²⁶⁴ Loubser 2007 The Comparative and International LJ of Southern Africa 152–171.

²⁶⁵ *Ibid.*

²⁶⁶ See para 13(1)(e) of Schedule B1 to the Insolvency Act of 1986.

²⁶⁷ *Ibid.*

5.3 International Standards of Best Practice

On the international front, there has been a significant shift from oppressive and pro-creditor insolvency regimes to more debtor-friendly systems. In ancient Roman times debtors were treated harshly and, unless the debtor discharged the debt or someone came forward to guarantee payment, the creditor could take the debtor away with him and bind him with thongs and fetters, the weight of which would not be less than fifteen pounds.²⁶⁸ Certain statutes not only permitted indenture, they even went to the extent of entitling creditors to “cut up the debtor’s body.”²⁶⁹

The United Nations Commission on International Trade Law (UNCITRAL) completed a Legislative Guide on Insolvency Law in 2004 to encourage the adoption of effective national corporate insolvency regimes.²⁷⁰ Boraine²⁷¹ states that the guide is used by member states as a platform to reform their local insolvency laws in order to establish greater harmony on a global scale. The over-arching goal of UNCITRAL is to eliminate the barriers to trade created by the disparities between national laws governing international trade. The UNCITRAL Legislative Guide on Insolvency Law (hereinafter called the *UNCITRAL Guide*) focuses on the key elements of an effective insolvency system and presents a series of legislative recommendations which are used for benchmarking purposes.²⁷²

In addition to the best practices that have been set by UNCITRAL, there are other organisations that have developed instruments and tools to help countries and jurisdictions in establishing international principles of insolvency and best business rescue practice, and these include the World Bank, the International Monetary Fund, the International Federation of Insolvency Practitioners, the European Union and the European Bank for Reconstruction and Development. The World Bank collaborated with UNCITRAL to

²⁶⁸ Levenstein 2017 para 5.1.

²⁶⁹ *Ibid.*

²⁷⁰ Levenstein LLD 80.

²⁷¹ Boraine. “A Framework for International Insolvency.” 2018 Global Insolvency Practice Programme.

²⁷² Levenstein LLD 80.

produce the UNCITRAL *Guide*.²⁷³ INSOL International²⁷⁴ has also been collaborating with UNCITRAL over the last 21 years in insolvency proceeding analysis and best-practice development.²⁷⁵

The UNCITRAL *Guide* points out that in some jurisdictions the commencement standard provides the basis for commencement of either business rescue (“re-organisation”) or liquidation.²⁷⁶ Where a liquidation application is made by a creditor, the insolvency legislation may permit the debtor company to apply for the proceedings to be converted from liquidation to business rescue.²⁷⁷ In some jurisdictions where business rescue is favoured, business rescue proceedings must be commenced, but can be converted to liquidation if it is demonstrated that the debtor cannot be rescued.²⁷⁸ Another approach is neutral and the choice between business rescue and liquidation is only made after the debtor company’s financial situation has been assessed.²⁷⁹

According to the UNCITRAL *Guide*, in most insolvency systems providing for conversion, while it is often possible for business rescue proceedings to be converted to liquidation proceedings, most of these systems do not allow reconversion to business rescue once conversion of business rescue to liquidation has already occurred.²⁸⁰ The UNCITRAL *Guide* further recommends that devices should be designed to prevent the abuse of insolvency proceedings, such as commencing business rescue proceedings as a means of avoiding or delaying liquidation.²⁸¹

Burdette²⁸² states that the UNCITRAL *Guide*’s viewpoint is that even though a company may have been liquidated, insolvency procedures should be designed in such a way that the liquidator can use the business rescue provisions insofar as they will allow him to bring about a more beneficial return to creditors.

²⁷³ Burdette (part 1) 2004 *SA Merc LJ* 263.

²⁷⁴ The International Association of Restructuring, Insolvency and Bankruptcy Professionals.

²⁷⁵ Levenstein 2017 para 4.3.2.

²⁷⁶ United Nations UNCITRAL Legislative Guide on Insolvency Law 2005.

²⁷⁷ *Ibid.*

²⁷⁸ *Ibid.*

²⁷⁹ *Ibid.*

²⁸⁰ United Nations UNCITRAL Legislative Guide on Insolvency Law 2005 18.

²⁸¹ *Ibid.*

²⁸² Burdette 2004 *SA Merc LJ* 256.

The International Monetary Fund advises that insolvency law should allow for conversion from liquidation to rehabilitation, and that this should be initiated by the debtor, the administrator, the court or even the creditor.²⁸³ However, the International Monetary Fund further recommends that such a law should also provide for a conversion back to liquidation if rehabilitation is not feasible.²⁸⁴

5.4 Conclusion

In conclusion, South Africa, Australia and the United Kingdom use different terminologies²⁸⁵ to refer to the business rescue procedure although the scope of companies to which the procedure applies is almost the same.

In the South African system, there is a greater attempt to give the financially distressed company every possible chance to turn its fortunes around compared to the dispensation in Australia and the United Kingdom. Be that as it may, South Africa's business rescue regime is not at odds with the tenets of an ideal insolvency system as laid down in UNCITRAL Model laws. There are many similarities between the Australian system, the British system and the South African system. It is submitted that Australia and the United Kingdom are loath to countenance business rescue after the company has gone into liquidation. The conversion clauses referred to in 5.2.3 *supra* are seldom invoked in practice.

²⁸³ International Monetary Fund "Orderly and effective insolvency procedures": 1999 *Key Issues* ch 4.

²⁸⁴ *Ibid.*

²⁸⁵ South Africa ("business rescue"), Australia ("voluntary administration"), and United Kingdom ("administration").

CHAPTER 6: CONCLUSIONS AND RECOMMENDATIONS

6.1 General Conclusions and Recommendations

This study purported to answer the question whether the launching of business rescue applications after the commencement of liquidation proceedings is a legal conundrum in South Africa. The conclusion reached is that, following the June 2015 SCA *Richter* judgment,²⁸⁶ the question is now academic or moot. Business rescue proceedings can be commenced when liquidation proceedings are already under way and up to the point when they end with the de-registration of the company. In effect, the commencement of business rescue proceedings overrides the commencement and continuation of liquidation proceedings.

Even though this is the current legal position, countenancing the launch of business rescue proceedings after the commencement of liquidation proceedings is still a thorny issue and is marred by new legal problems as pointed out in chapter 4 above. Some lower courts are at variance with the SCA's decision in *Richter*.

Clearly, business rescue has brought about an evolution in South Africa's corporate insolvency jurisprudence. It has rapidly gained traction, and liquidation is gradually becoming an abhorrent word in the country's insolvency lexicon. Although liquidation is still an option, its spectre is fading away in respect of financially distressed companies as it is only opted for as a last resort. In the case of competing court applications, business rescue is now prioritised and this resonates well with international trends and the purpose of the 2008 Act²⁸⁷ as spelt out in section 7 of the Act. Arguably, section 7 forms the bedrock of business rescue, the chief aim being to rehabilitate ailing companies and avert liquidation with its concomitant far-reaching consequences. This is a testament to the fact that South Africa is shifting from a pro-creditor insolvency system to a more debtor-friendly dispensation, although directors still have to relinquish control of the company when it is in business rescue. However, the need to strike a correct balance between the advantages

²⁸⁶ *Richter v ABSA Bank Ltd* (20181)/2014) [2015] ZASCA 100 (1 June 2015).

²⁸⁷ Companies Act 71 of 2008.

of liquidation and corporate restructuring, as recommended in the UNCITRAL Legislative Guide on Insolvency Law,²⁸⁸ should not be overlooked in order to ensure that the country's insolvency system functions optimally.

The “reasonable prospect” of a rescue being achieved remains the litmus test and touchstone in all business rescue applications, even post-liquidation. When promulgating the 2008 Act, it was not the intention of the legislature to prop up companies which are beyond redemption. Accordingly, attempts should be made to rescue the company timeously before it reaches the tipping point and becomes hopelessly insolvent. Therefore, it is crucial for the board to realise timeously when the company is in the twilight zone of insolvency. To this end, forecasting and early-warning tools are of paramount importance to every company if directors want to successfully leverage the business rescue remedy. This could involve regularly performing the insolvency and liquidity test,²⁸⁹ which is a forward-looking diagnosis of the business. In this regard, business rescue can also be viewed as a management tool.

As indicated in chapter 4 above, the business rescue remedy is prone to abuse, especially when liquidation is imminent. There is a need for a peremptory requirement to conduct an independent pre-rescue assessment before the section 129(1)²⁹⁰ resolution can be passed by the board. In addition, it is submitted that specialised commercial courts and competent commercial judges to deal with business rescue cases are a *sine qua non* if the new dispensation is to function more efficiently in the long-term. Whilst the rescue culture is being encouraged, slovenly granting business rescue orders can perpetuate the abuse of the business rescue process.

The rumbling about the competence and probity of business rescue practitioners should not be ignored. The competence of business rescue practitioners is even more critical when business rescue is launched after the commencement of liquidation proceedings. In addition to more stringent statutory regulation, structuring the remuneration regime of

²⁸⁸ United Nations Commission on International Trade Law *UNCITRAL Legislative Guide on Insolvency Law* (2005) 11.

²⁸⁹ See s 4 of the Companies Act No. 71 of 2008.

²⁹⁰ Companies Act No. 71 of 2008.

business rescue practitioners in such a way that it provides stronger incentives for them to strive for successful rescues can somewhat help to address the concern. The need to curtail protracted business rescue proceedings which are motivated by nefarious reasons cannot be over-emphasised.

Finally, although its significance is being attenuated by business rescue, liquidation is certainly not a relic of the past. It still plays an important role in the country's commerce and insolvency system, despite being inimical to the growing rescue culture. For instance, it plays a vital role in the recovery of property improperly alienated or encumbered just before the commencement of insolvency proceedings against the company.

6.2 Recommendations for further Research:

- (a) There is a need to conduct an empirical study to evaluate the success rate of business rescues commenced post the final liquidation order; and
- (b) A more comprehensive study on the shortcomings of commencing business rescue post-liquidation is recommended with a view to resolving some of the new legal conundrums that have been created by the SCA *Richter* judgment. The transition from the liquidation culture to a business rescue regime is still fraught with legal problems. Fortunately, courts have been able to whittle down most of these.

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