BUSINESS RESCUE AS A VEHICLE FOR TAX EVASION

by

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Chapter 1: Introduction

1.1. Background

A company is an entity that functions as a means through which members of society may carry on economic activities. As identified by Mongalo,[1] companies are a business structure that dominates economic life in South Africa because of the number of resources that they plough into the South African economy and constitute a considerable portion of the country's gross domestic profit.[2] Companies also form an integral part of the community within which they conduct their business, the lives of their employees and persons with whom they transact. There is consequently a significant knock-on effect when a company fails. The effects of this failure are felt by the community dependent on the particular company, the South African economy and the fiscus in respect of the current and future collection of taxes. The continued subsistence of income-generating companies is thus in the interests of both society and the State. It follows that the concept of business or corporate rescue is of particular significance as it is intended as a mechanism to ensure the continuation of companies where they are in financial distress[3] and thereby protect these interests.

Business rescue is still a relatively new notion in South African law and was first introduced into South African law with the enactment of the Companies Act 71 of 2008 (the "Companies Act"). It was introduced to create "a system of corporate rescue appropriate to the needs of a modern South African economy".[4]Before the Companies Act, the process of "rescuing" business was something which had only taken place informally in terms of agreements between the creditors and the business itself. The alternative was attempting to resuscitate a company under the

[1]T Mongalo 'South Africanizing company law for a modern competitive global economy' (2004) 121(1) *South African Law Journal* 93.
[2]T Mongalo 'South Africanizing company law for a modern competitive global economy' 94.
[3]S129(1) and 131(4) Companies Act No. 71 of 2008.
[4]Department of Trade and Industry *South African Company law for the 21st Century: Guidelines for Corporate Law Reform* (GG 26493, General Notice 1183) of 23 June.

process of judicial management,[5] which was not adequately utilised and generally accepted as being unsuccessful.[6]

In light of the above, one would have expected the legislators to provide an explanatory memorandum or other similar detailed document that details the reasoning and intention behind the provisions contained in Chapter 6 of the Companies Act ("Chapter 6"). Such a document would have greatly assisted in the interpretation of the provisions ultimately included in the Companies Act, especially where the provisions of the Companies Act are vague or ambiguous. The difficulties in interpreting the legislation are further compounded by the confusing terminology used in the drafting of the provisions of Chapter 6 of the Companies Act. It has also been suggested that these shortcomings can be explained by the fact that the primary drafter of the Companies Act is Canadian and thus unfamiliar with South African laws and practices.[7] Regardless of the reason for the shortcomings of Chapter 6, the fact remains that there are indeed significant shortcomings in the legislation and as a result, stakeholders and affected parties have had to approach the courts to seek their intervention and assistance in the interpretation and application of the legislation.[8]

The Tax Administration Act 28 of 2011 (the "Tax Administration Act") was enacted only three years after the Companies Act of 2008; at a time when the corporate, accounting and legal fraternities were still coming to terms with how to implement, monitor and identify the problems with business rescue. The Tax Administration Act stipulates the powers and duties of the South African Revenue Service ("SARS"), its Commissioner ("CSARS") and its officials in respect of the administration of the tax

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[5]Chapter XV Companies Act No. 61 of 1973.

[6]T Mongalo 'An overview of company law reform in South Africa: from the Guidelines to the Companies Act 2008' (2010) *Acta Juridica (Modern company law for a competitive South African economy)* xiii-xxiii.

[7]Mr. Phillip Knight is a Vancouver-based legal counsel and plain-language drafting expert, and was appointed as the chief drafter for South Africa's company law reform process which produced the Companies Act No. 71 of 2008; Mongalo 'An overview of company law reform in South Africa: from the Guidelines to the Companies Act 2008' (2010) *Acta Juridica (Modern company law for a competitive South African economy)* xv at footnote 11; A Loubser 'Some Comparative Aspects of Corporate Rescue in South African Company Law' (LLD thesis, University of South Africa, Thesis SA, 2010) 6.

[8] See Chapter 3 below.

Acts. Neither the Companies Act nor the Tax Administration Act is perfectly drafted legislation,[9] but when reading them together one notes that there are significant incongruences between the two. There are also incongruences between the business rescue provisions of the Companies Act and other South African tax-related legislation. This is a serious problem for the fiscus as SARS is often a substantial creditor in business rescue proceedings and it would seem that it has yet to be acknowledged that SARS faces significant difficulties as a creditor in business rescue proceedings.

If one evaluates the provisions of Chapter 6 from a tax perspective, it would seem that the drafters thereof did not have due regard to the interplay between its provisions and the existing tax legislation, or its effect on SARS and consequently the fiscus, when drafting it. This particular problem was then further compounded by the introduction of the Tax Administration Act, which at times seems to operate in direct conflict with the provisions of Chapter 6. In the absence of a court order to the contrary, SARS is bound by the provisions of the Tax Administration Act as it is a creature of statute and this Act is its own empowering legislation. However, in terms of section 5 of the Companies Act, it shall be the overriding legislation where there is a conflict between its provisions and that of the Tax Administration Act – a clear problem for SARS as it is bound to follow the provisions of the tax Acts. In addition to the above, the incongruences between Chapter 6 and the tax legislation provide taxpayers with ample opportunities to engage in both tax avoidance and tax evasion. It is this behaviour and the deficiencies with the abovementioned legislation that forms the basis for this mini-dissertation.

[9] Both Acts have been subject to criticism and amendments since their promulgation. See C Divaris Tax Administration Weekly 23 TAW 2019 (WEEK 283) 19 June 2019; see also Chapters 2 and 3 below; see also E Levenstein 'Appraisal of the new South African Business Rescue procedure' (LLD Thesis, University of Pretoria 2015); See J Rushworth "A critical Analysis of the Business Rescue Regime in the Companies Act 71 of 2008" (2010) *Acta Juridica* 375.

1.2. Rationale for the mini-dissertation

The significance of this mini-dissertation is evident when one evaluates the literature available on this topic. There is limited literature available which analyses the shortcomings of Chapter 6 of the Companies Act in general. There is, unfortunately, an absence of literature available in which Chapter 6 is reviewed from a tax perspective. As a result, there is a gap in academic commentary in this regard as well as the necessary call for law reform to address the problems experienced in practice.

This mini-dissertation proposes amendments to the existing legislation in order to address the problems identified. These amendments are aimed at decreasing the available opportunities for taxpayers and business rescue practitioners to abuse the provisions of Chapter 6 for purposes of tax evasion. It is anticipated that this shall in turn ultimately lead to an increase in tax compliance and decrease the use of business rescue as a vehicle for tax evasion.

1.3. Research problem statement

The research problem statement that one is faced with in this particular mini-dissertation is that there are deficiencies with the provisions of Chapter 6 of the Companies Act and there are incongruences between Chapter 6 and the existing South African tax-related legislation, such that they may operate to facilitate tax evasion.

1.4. Research question

The primary question posed in this mini-dissertation is whether business rescue is a vehicle for tax evasion in South Africa. It is not merely sufficient to identify the shortcomings of business rescue provisions of the Companies Act and the Tax Administration Act in so far as they relate to one another. This mini-dissertation shall therefore also address the question of what legislative amendments would be required to rectify the shortcomings in the legislation to the extent that same is found to be inadequate.

1.5. Objectives

The objectives of this mini-dissertation are, namely to:

- identify the provisions of Chapter 6 which may or do facilitate tax evasion in South Africa;
- identify the incongruences between Chapter 6 and the existing tax legislation which may or do facilitate tax evasion in South Africa; and
- call for legislative reform in respect of the above and propose amendments to the relevant legislation.

1.6. Key words

Business rescue; tax evasion; business recovery; business rescue; corporate insolvency; corporate rescue; compromise; financial distress; insolvency; liquidation; mismanagement; moratorium; reorganisation; voluntary arrangement; tax administration; tax avoidance; tax evasion; fraud; South Africa.

1.7. Limitations

The focus of this dissertation is the facilitation of tax evasion by the provisions of Chapter 6 of the Companies Act. Due to limitations regarding the length of this dissertation an analysis of the powers and duties of the business rescue practitioners' powers and duties has been excluded. The final limitation is the fact that no criminal precedent could be found relating to the prosecution of persons for tax evasion relating to business rescue.

1.8. Nature of the study and sources

This mini-dissertation entails a comparative study of primary sources. These primary sources are analysed herein and used to illustrate difficulties with and incongruences between the existing tax and business rescue legal framework. The key primary sources in this comparative study are Chapter 6 of the Companies Act, the Tax Administration Act and the Value-Added Tax Act No. 89 of 1991 (the "VAT Act").

Secondary sources, including available commentary on the aforementioned legislation, explanatory memoranda, and opinions expressed in articles, are employed to further evaluate the primary sources. In this way, both primary and secondary sources were reviewed with a view to answering the research question.

Chapter 2: Analysis of Chapter 6 and the TAA

2.1. Introduction

In this chapter, the author distinguishes tax evasion from tax avoidance and unpacks the basic concept of business rescue as well as the benefits thereof. Thereafter the author analyses the existing business rescue and relevant tax legislation to determine whether the existing legislative framework allows for business rescue to be used to perpetrate tax evasion.

2.2. What do tax avoidance and tax evasion mean?

Tax avoidance is generally used to refer to the legal exploitation of a tax regime to one's own advantage by arranging one's affairs to reduce the amount of tax that is payable, whilst making full disclosure of the material information to the tax authorities.[10] Although such arrangement is not strictly illegal, it is usually in contradiction to the law it professes to follow.[11] Examples of tax avoidance involve using tax deductions, changing one's business structure through incorporation or establishing an offshore company in a tax haven.[12] Taxpayers may engage in tax avoidance to amorally abstain from complying with their duties to society, as part of a strategy of not supporting violent government activities or just to exercise the right of every citizen to find all the legal ways to avoid paying more tax than is absolutely necessary.[13]

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[10]OECD, International Tax Terms for the participants in the OECD Programme of Co-operation with Non-OECD Economies; N Musviba 'Tax Avoidance and Tax Evasion – the differences' available at *http://www.sataxguide.co.za/tax-avoidance-and-tax-evasion-the-differences/*, accessed on 26 March 2018.

[11]OECD, International Tax Terms for the participants in the OECD Programme of Co-operation with Non-OECD Economies.

[12]N Musviba 'Tax Avoidance and Tax Evasion – the differences' available at *http://www.sataxguide.co.za/tax-avoidance-and-tax-evasion-the-differences/*, accessed on 26 March 2018.

[13]Musviba 'Tax Avoidance and Tax Evasion – the differences'.

2.2.2. Tax evasion

Tax evasion refers to efforts by individuals and other entities to evade the payment of taxes by illegal means.[14] Tax evasion usually entails the deliberately misrepresenting or concealing the true state of their affairs to the tax authorities to reduce a tax liability or tax liabilities, and includes, in particular, dishonest tax reporting (for example by under-declaring income, profits or gains and overstating deductions)as well as a complete failure to report to the relevant revenue authorities at all.[15]Tax evasion is a crime in most countries and taxpayers who are found guilty of tax evasion are typically penalised by means of fines or even imprisonment.[16]

In South Africa tax evasion is a criminal offence under the Tax Administration Act 28 of 2011 (the "Tax Administration Act") that attracts a penalty of either a fine or imprisonment for a period of up to five years.[17] Intention is a prerequisite for liability for tax evasion under the Tax Administration Act.[18] Both persons who intentionally perpetrate tax evasion and persons who assist others to evade tax can be held liable for this criminal offence or fine under the relevant legislative provisions.[19] In the Short Guide to the Tax Administration Act[20] (the "short Guide to the TAA"), published by SARS, SARS states that evading tax includes conduct intended to reduce or extinguish the amount of tax that should be paid or inflate the amount that is refundable to the taxpayer.[21] Conduct that may constitute tax evasion includes intentionally making a false statement in a return[22] as well as using or authorising the use of fraud or contrivance.[23] In the Short Guide to the TAA SARS sets out its view that even the act of not filing a return can constitute intentional tax evasion under the provisions of the Tax Administration Act.[24]

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[14]Musviba 'Tax Avoidance and Tax Evasion – the differences'.
[15]OECD, International Tax Terms for the participants in the OECD Programme of Co-operation with Non-OECD Economies; Musviba 'Tax Avoidance and Tax Evasion – the differences'.
[16]Musviba 'Tax Avoidance and Tax Evasion – the differences'.
[17]S335 Tax Administration Act 28 of 2011.
[18]S335(1)-(2) Tax Administration Act 28 of 2011.
[19]S335(1) Tax Administration Act 28 of 2011.
[20]South African Revenue Service 'Short Guide to the Tax Administration Act, 2011 (Act 28 of 2011)' 3ed (2018) 84.
[21]South African Revenue Service 'Short Guide to the Tax Administration Act, 2011 (Act 28 of 2011)' 3ed (2018) 84.
[22]S335(1)(a) Tax Administration Act 28 of 2011.
[23]S335(1)(d) Tax Administration Act 28 of 2011.
[24]South African Revenue Service 'Short Guide to the Tax Administration Act, 2011 84.

It should be noted that this dissertation's primary focus is tax evasion in South African law that is facilitated by business rescue under Chapter 6 of the Companies Act 71 of 2008 (the "Companies Act").

2.3. What is business rescue?

What does it mean to rescue a company[25] as contemplated in Chapter 6 of the Companies Act? As business rescue is a novel concept introduced into South African law by legislation, one has to turn to this legislation as a starting point in answering this question. The relevant provisions of the Companies Act are discussed in further detail below as well as the fundamental concepts and definitions relevant to business rescue.

2.3.1. Business rescue

The Companies Act defines "rescuing the company" to mean achieving the goals set out in the definition of "business rescue" as stated in section 128(1)(b) of the Companies Act. Section 128(1)(b) of Companies Act defines the term "business rescue" to mean to "**facilitate the rehabilitation of a company that is financially distressed** by providing for three things, namely:

- the **temporary supervision** of the company, and of the management of its affairs, business and property;
- a **temporary moratorium** on the rights of claimants against the company or in respect of property in its possession; and

[25]Section 1 of the Companies Act 71 of 2008 defines a 'company' as a juristic person incorporated in terms of this Act, or a juristic person that, immediately before the effective date—
(a) was registered in terms of the—
(i) Companies Act, 1973 (Act 61 of 1973), other than as an external company as defined in that Act; or
(ii) Close Corporations Act, 1984 (Act 69 of 1984), if it has subsequently been converted in terms of Schedule 2;
(b) was in existence and recognised as an 'existing company' in terms of the Companies Act, 1973 (Act 61 of 1973); or
(c) was deregistered in terms of the Companies Act, 1973 (Act 61 of 1973), and has subsequently been re-registered in terms of this Act.

- the **development and implementation**, if approved, of a plan to rescue the company by restructuring its affairs, business, property, debt and other liabilities, and equity in a manner that maximises the likelihood of the company continuing in existence on a solvent basis or, if it is not possible for the company to so continue in existence, results in a better return for the company's creditors or shareholders than would result from the immediate liquidation of the company."[26]

The first term that must be understood is the concept of rehabilitation, but this is unfortunately not defined in the Companies Act. The Concise Oxford English Dictionary[27] defines "rehabilitate" as "the action of restoring something that has been damaged to its former condition"[28] and the objective of business rescue is to maximise the likelihood for solvency and ongoing existence of the affected company and avoid liquidation.[29] Therefore business rescue entails restoring companies that are not functioning properly, and have become financially distressed as a result, to a point where they function properly and are no longer financially distressed. This is the primary aim of business rescue.[30] In addition to the above, the definition of business rescue also allows for a situation where a company may wind-down through business rescue if the ultimate rescue of a company is not possible and creditors would receive a higher dividend through this process than what would be possible through liquidation. This is not the primary aim of business rescue, but is instead a possible beneficial alternative course of action where the primary objective cannot be achieved.[31]

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[26]See section 128(1)(b) Companies Act 71 of 2008, author's own emphasis added.
[27]J Pearsall *Concise Oxford English Dictionary* 10ed (2002).
[28]Pearsall *Concise Oxford English Dictionary* 1207.
[29]Levenstein 'Appraisal of the new South African Business Rescue procedure' 278; E Levenstein "Business Rescue: help is at hand" (November 2008) *Without Prejudice* 12-14; LJ Sher *The appropriateness of business rescue as opposed to liquidation – a critical analysis of the requirements for a successful business rescue order as set out in section 131(4) of the Companies Act 71 of 2008* (LLM dissertation, University of Johannesburg 2013).
[30]J Kunst, A Boraine and D Burdette *Insolvency Law* SI 51 ed (2018) 18.3.2.
[31]Kunst, Boraine and Burdette *Insolvency Law* SI 51 ed (2018) 18.3.2; See Rushworth "A critical Analysis of the Business Rescue Regime in the Companies Act 71 of 2008" (2010).

2.3.1.1. Financial distress

The second important definition for purposes of understanding the concept of business rescue is "financially distressed". Section 128(1)(f) of the Companies Act defines this, in reference to a particular company at any particular time, to mean that—

- "it appears to be reasonably unlikely that the company will be able to pay all of 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."[32]

It is companies that meet the above mentioned criteria that are the intended target market for rehabilitation by business rescue under Chapter 6 and not companies that are insolvent.[33]This means that the end result or aim of business rescue is to get the company to a position whereby it is reasonably likely to pay its debts falling due or shall no longer become insolvent within an immediately ensuing six month period. It is also submitted that act of evaluating whether a company is financially distressed involves a factual inquiry into the company's financial affairs and projections for a period of six months after the date on which the analysis is performed.

2.2.1.2. Affected person(s) in business rescue

In respect of business rescue an "affected person" in relation to the company is defined as a shareholder or creditor of the company, any registered trade union representing the company's employees, and the employees and their representatives themselves if such employees are not represented by a trade union.[34] As noted by Levenstein[35] the term "creditor" is not defined in the Companies Act, but includes amounts that are due and payable prior to the date of commencement of business rescue proceedings and the company's employees.[36]

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[32]S128(1)(f) Companies Act 71 of 2008.
[33]Levenstein 'Appraisal of the new South African Business Rescue procedure' 280.
[34]S128(1) Companies Act 71 of 2008.
[35]'Affected person' as defined in section 128(1) Companies Act 71 of 2008.
[36]Levenstein 'Appraisal of the new South African Business Rescue procedure' 283.

2.3.1.3. Benefits of business rescue

To properly contextualise what makes business rescue so attractive to companies, it is necessary to briefly highlight the benefits that flow from placing a company into business rescue. Although some of these benefits were designed to give companies in business rescue a fighting chance of being rehabilitated, they are also open to abuse. Some of these benefits are briefly discussed below.

2.3.1.3.1. Moratorium against enforcement actions

The moratorium on all "enforcement actions" taken by claimants against the company or in respect of any property in its possession for the duration of the business rescue.[37] In contrast, liquidation proceedings provide the company with the following more limited protections:

- All executions and attachments that are in force against the company's estate are rendered void and the claimants must lodge and prove their claims in the estate.[38]
- All civil proceedings instituted against the company prior to liquidation are suspended after the commencement of liquidation proceedings and may continue after the liquidator is given notice as contemplated in section 239(2) of the Companies Act 1973, failing which they are considered abandoned unless a court directs otherwise.[39]
- Claims may be enforced against the company by instituting legal proceedings, but the liquidator must be given a notice contemplated in section 239(2) of the Companies Act 1973, failing which they are considered abandoned unless a court directs otherwise.[40]

2.3.1.3.2. Less compliance and administrative burdens

Business rescue is not subject to the same stringent and burdensome compliance and administrative requirements as liquidation. Examples include:

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[37]S133(1) Companies Act 71 of 2008.
[38]S359(1)(b) Companies Act 61 of 1973; s366 Companies Act 61 of 1973.
[39]S359(1)(a) Companies Act 61 of 1973; s359(2) Companies Act 61 of 1973.
[40]S359(2) Companies Act 61 of 1973.

- In voluntary business rescue proceedings the appointment of a business rescue practitioner ("BRP") is done based on the nomination of the directors of the company.[41] In business rescue by court order the court may appoint the BRP based on the nomination by an affected party and subject to the ratification by the majority of creditors who hold an independent voting interest.[42] The nominated BRP shall likely be appointed, provided that this person meets the threshold of requirements of section 138 of the Companies Act. The appointment of a liquidator in both voluntary liquidation and liquidation by court order is done by the Master of the High Court after consideration of the creditors' nominations.[43] In liquidations the persons who are appointed as liquidators are required to meet detailed and more stringent and a conditions prior to their appointment.[44] Furthermore, a person may still not be appointed as a liquidator if the Master is of the opinion that the nominated person should not be appointed as the liquidator in the relevant estate.[45]
- In liquidation proceedings the relevant Master of the High Court oversees the proceedings and may make certain determinations regarding the process, while in business rescue there is no independent third-party or dedicated oversight body that performs similar functions.
- A company may continue to trade normally after the business rescue proceedings end due to a court order setting aside the resolution to commence business rescue,[46] the BRP files a notice of termination with CIPC,[47] the business rescue plan has been rejected and the proceedings have not been extended in terms of section 153 of the Companies Act,[48] or the business rescue plan is adopted and the filing of a notice of "substantial implementation" with CIPC.[49] After the commencement of the winding-up of a company by liquidation

[41]S129(3)(b) Companies Act 71 of 2008.
[42]S131(5) Companies Act 71 of 2008.
[43]S367 Companies Act 61 of 1973; s368 Companies Act 61 of 1973; s369 Companies Act 61 of 1973; s370 Companies Act 1973.
[44]S365 Companies Act 61 of1973; s367 Companies Act 61 of1973; s368 Companies Act 61 of1973; s369 Companies Act 61 of1973; s370 Companies Act 61 of1973.
[45]S370(1) Companies Act 61 of1973; s373 Companies Act 61 of 1973.
[46]S132(2)(a)(i) Companies Act 71of 2008.
[47]S132(2)(b) Companies Act 71 of 2008.
[48]S132(2)(c)(i) Companies Act 71 of 2008.
[49]S132(2)(c)(ii) Companies Act 71 of 2008.

the proceedings may only be stayed or set aside upon application to a court and make such order subject to any conditions it deems fit.[50]

2.3.1.3.3. Continuation of the company

As stated above, business rescue functions as a legal restructuring of the company's affairs, debts, finances, equity, property etc. in terms of an approved business rescue plan in order to rehabilitate the company.[51] In contrast, the purpose of liquidation the orderly winding-down of the company through the establishment of a *concursus creditorum* so that the company may be terminated.[52]

2.3.1.3.4. Voting rights

In business rescue the size of creditors' claims (i.e. the value thereof) against the company and the classification thereof determine the value of their voting rights. It is, however, uncertain as to what voting rights, if any, post-commencement creditors have.[53] Secured and creditors have a voting interest equal to the value of the amount owed to that creditor.[54] The same position applies to unsecured creditors to the extent that their claims would be subordinated in liquidation, and if so then they only have a voting interest equal to the amount that such creditor could reasonably expect to receive in liquidation.[55]In liquidation creditors' may vote on all matters relating to the administration of the estate, other than directing the liquidator to consent to, admit or compromise any claim in the estate.[56] However, in order to do so the creditors are first required to prove their claims in the company's estate so as to qualify as proven creditors.

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[50]S354(1) Companies Act 61 of 1973.
[51]Levenstein 'Appraisal of the new South African Business Rescue procedure' 278; E Levenstein "Business Rescue: help is at hand" (November 2008) *Without Prejudice* 12-14; Sher *The appropriateness of business rescue as opposed to liquidation – a critical analysis of the requirements for a successful business rescue order as set out in section 131(4) of the Companies Act 71 of 2008*.
[52]PM Meskin, JM Kunst, B Galgut et. al *Henochsberg on the Companies Act 71 of 2008* (2011+) 448; Levenstein 'Appraisal of the new South African Business Rescue procedure' 283.
[53]*Walker v Syfret NO* 1911 AD 141.
[54]S145(4)(a) Companies Act 71 of 2008.
[55]S145(4) Companies Act 71 of 2008.
[56]S52(1) Insolvency Act 24 of 1936.

A creditor holding any security for his claim shall, except in the election of a trustee and upon any matter affecting the security, be entitled to vote only in respect of the amount by which his claim exceeds the amount at which he valued his security, when proving his claim, or if he did not value his security, in respect of the amount by which his claim exceeds the amount of the proceeds of the realisation of his security in terms of section 83.

2.3.1.3.5. SARS is a concurrent creditor

SARS is often a creditor with a substantial claim in both liquidation and business rescue proceedings. SARS is ranked as a concurrent creditor of a company in business rescue proceedings which means that SARS claim is to be paid with other concurrent creditors, as opposed to before them like in liquidation where SARS is a preferent creditor.[57]

2.3.1.3.6. Companies in liquidation placed into business rescue

Furthermore, it is possible for a company to be taken out of liquidation and placed into business rescue.[58] Where liquidation proceedings have already commenced by or against the company at the time an application is made to a court to place the company into business rescue, then the liquidation proceedings will be suspended until the court adjudicates on it or if the application for business rescue is successful, after the business rescue proceedings end.[59] The benefit hereof is that is functions as a failsafe mechanism whereby companies may to be removed from liquidation and commence business rescue proceedings where, for instance, their prospects improve after the date of commencement of liquidation proceedings and it is just and equitable to commence business rescue proceedings for financial reasons.[60]

[57]S99(1)(b) Insolvency act 24 of 1936; s101 Insolvency Act 24 of 1936.
[58]S131(7) Companies Act 2008.
[59]S131(6) Companies Act 71 of 2008.
[60]See section 131(4)(a)(i)-(iii) of the Companies Act 71 of 2008 for further circumstances in which the court may make an order placing a company into business rescue.

2.3.1.3.7. Significant indemnity for BRPs

BRPs enjoy significant protection from liability for acts or omissions committed during the course and performance of their duties and responsibilities as a BRP.[61] BRPs are not liable for any act or omission performed in good faith in exercising his function and powers under Chapter 6.[62] Persons who are to be appointed as liquidators are required to provide security to the satisfaction of the Master, for the proper performance of his or her duties as liquidator, as a prerequisite for their appointment to the office as liquidator.[63]Business rescue practitioners are only required to provide security in voluntary business rescue proceedings where an affected person has applied to a court for an order to this effect as contemplated in section 130(1)(c) of the Companies Act.[64]

2.4. Legislative analysis

2.4.1. Conflicts between the Companies Act and tax Acts

The first step in commencing with a legislative analysis of Chapter 6 is to understand the interplay between the provisions of the Companies Act and other legislation. In terms of section 5(4)(b) of the Companies Act the provisions of the Companies Act prevail where there exists any inconsistency between a provision of the Companies Act and a provision of any other national legislation if it is impossible to comply with or apply one of the inconsistent provisions without contravening the provision of the national legislation.[65]

As a result, where there is a conflict between any tax Act, like the Value-Added Tax Act No 89 of 1991 (the “VAT Act”), or the Tax Administration Act and the Companies Act, then the provisions of the Companies Act shall override that of the relevant tax

[61]S140(3)(c) Companies Act 71 of 2008.
[62] S140(3)(c)(i) Companies Act 71 of 2008;
[63]S368 Companies Act 61 of 1973; s370(1) Companies Act 61 of 1973; s374 Companies Act 61 of 1973; s375(1) Companies Act 61 of 1973.
[64]S130(1)(c) Companies Act 71 of 1973.
[65]This is subject to certain exceptions, which include where the national legislation concerned is any applicable provisions of a number of specified Acts but not including any tax legislation.

Act. The SARS, as a creature of statute,[66] is bound to perform its functions, of administering the tax legislation and collecting revenue on behalf of the National Revenue Fund, in line with its empowering legislation. Consequently, SARS would be unable to act in accordance with the Companies Act were a conflict with the tax legislation to arise and the provision(s) of the Companies Act to override the tax legislation as contemplated in section 5 of the Companies Act. Whether just an oversight on the part of the legislature or intentional, SARS is placed in a precarious position where these conflicts manifest because it is obliged to comply with the tax Acts and in many cases cannot derogate from the provisions thereof unless a court orders it to do so.

2.4.2. "Enforcement action" under section 133(1) of the Companies Act

2.4.2.1. The moratorium

The concept of a moratorium on claims against the company is a cornerstone of the corporate rescue concept.[67] Section 133(1) of the Companies Act provides for a temporary moratorium on legal proceedings, including any "enforcement action", against a company from the date of commencement of business rescue and for the duration thereof. The moratorium relates to any such proceedings or actions being taken, in any forum, against the company in business rescue and in relation to any property belonging to such company, or lawfully in its possession.[68] There are, however, a few exceptions to the moratorium, namely:

- where the BRP has given written consent for such proceedings to be instituted or actions to be taken;[69]
- with the leave of a court and subject to any terms that this court deems fit to impose thereon;[70]
- as a set-off against any claim made by the company in any legal proceedings;[71]

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[66]*Rampersadh and Another v Commissioner for the South African Revenue Service and Others* (5493/2017) [2018] ZAKZPHC 36 (27 August 2018) para 12; *V Z Nondabula v The Commissioner: SARS & Another* Eastern Cape Local Division: Mthatha case unreported case no. 4062/2016.

[67]Levenstein 'Appraisal of the new South African Business Rescue procedure' 378; Meskin *Insolvency Law and Business Rescue* (1990+) 18.6*; Investec Bank Ltd v Bruyns* [2012] JOL 28420 (WCC).

[68]S133(1) Companies Act 71 of 2008); *Shamla Chetty t/a Nationwide Electrical v Hart NO and Another* 2014 JDR 0585 (KZD); [2015] JOL 32738 (KZD).

[69]S133(1)(a) Companies Act 71 of 2008.

[70]S133(1)(b) Companies Act 71 of 2008.

- any criminal proceedings against the company or any of its directors or officers;[72]
- proceedings regarding property or a right over which the company exercises the powers of a trustee;[73] or
- proceedings by a regulatory authority in the execution of its duties after written notification to the business rescue practitioner.[74]

The Companies Act is silent on the meaning of "enforcement action". It should be noted that this particular term does not have an accepted definition in South African law. As a result, the term is a point of contention between creditors and BRPs with the parties being left with little alternative but to approach the courts for their intervention on and to obtain decisive clarification of the matter. However, on an ordinary reading of the words the most likely interpretation for the term is that it means that no person may proceed to compel the company in business rescue to make good on any claim or right that this person may have against the company, nor may such company be compelled to comply with any obligation it may have to any person while the company is in business rescue (subject to the limited legislated exceptions thereto).

From a tax perspective, this places SARS in a precarious position with regard to its performance of its duties under the Tax Administration Act and tax-related legislation. The Tax Administration Act prescribed the framework within which SARS may administer the tax Acts and, unless ordered otherwise by a court, it has to comply with its obligations in terms thereof. For example, SARS enforcement of the "pay now argue later" rule,[75] where the payment of a tax liability is not suspended under section 164 of the Tax Administration Act, may constitute an enforcement action under section 133(1) of the Companies Act. Ordinarily where the payment of a tax debt is not suspended in terms of section 164, the Tax Administration Act prescribes that SARS may give the taxpayer at least ten business days' notice to make payment of a tax debt and if after the expiry of this period the debt remains

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[71]S133(1)(c) Companies Act 71 of 2008.
[72]S133(1)(d) Companies Act 71 of 2008.
[73]S133(1)(e) Companies Act 71 of 2008.
[74]S133(1)(f) Companies Act 71 of 2008.
[75]*Metcash Trading Limited v Commissioner for the South African Revenue Service and Another* (CCT3/00) [2000] ZACC 21; 2001 (1) SA 1109 (CC); 2001 (1) BCLR 1 (CC) (24 November 2000).

unpaid then SARS may file a certified statement with the registrar or clerk of the competent court that sets out the amount of tax payable.[76] The relevance of the certified statement endorsed by the clerk or registrar is that it must be treated as a civil judgment in favour of SARS[77] and would ordinarily be used by SARS to attach or execute against the taxpayer's assets.

As a result of the above mentioned ambiguity in section 133(1) of the Companies Act, it is possible to interpret the section to mean that the section precludes SARS from proceeding with the issuing of the letter of demand for payment, file the certified statement as contemplated in the Tax Administration Act, or use an already endorsed certified statement to attach or execute against the taxpayer's assets.

Another example is section 191 of the Tax Administration Act which compels SARS to set off amounts due to the taxpayer in terms of section 190 of the Tax Administration Act against tax debts owed to SARS and any remaining amount due under the Customs and Excise Act[78]. SARS is compelled to do this in terms of the Tax Administration Act, but is prohibited from complying with its own legislation by section 133(1) of the Companies Act if the taxpayer concerned is a company in business rescue.

2.4.2.2. Duration of the moratorium

When reading paragraph (ii) of the definition of "business rescue" in section 128(1)(b) and section 133(1)of Companies Act together, it is evident that the moratorium provided for in section 133(1) is indeed intended to be temporary.[79] As there is no maximum time-limit set for such moratorium or business rescue proceedings, the moratorium shall stay in place for as long as the company is in business rescue.

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[76]S164(6)(b) Tax Administration Act 28 of 2011; s172(1) the Tax Administration Act 28 of 2011.
[77]S174 Tax Administration Act 28 of 2011.
[78]Customs and Excise Act 91 of 1964.
[79]Meskin *Insolvency Law and Business Rescue* (1990+) 18.6; *Gormley v West City Precinct Properties* (*Pty*) *Ltd and Another*, *Anglo Irish Bank Corporation Ltd v West City Precinct Properties* (*Pty*) *Ltd and Another* (19075/11, 15584/11) [2012] ZAWCHC 33 (18 April 2012) para 13.

Although the Companies Act prescribes certain time-periods for the performance of certain functions of the BRP and milestones in the business rescue process, there are no limitations of the period for which companies may remain in business rescue. In addition, the mere fact that the business rescue plan must contain the nature and duration of any moratorium for which the plan itself makes provision[80]does not limit the general moratorium in terms of section 133(1) unless the plan itself specifically states a position to the contrary. It follows that the business rescue moratorium may remain in place for as long as the company remains in business rescue, unless the BRP consents to the contemplated legal proceedings or a court order to proceed therewith is obtained.

2. 4.2.3. Exceptions to the moratorium

The Companies Act gives the BRP an unfettered discretion to consent to legal proceedings or enforcement actions contemplated in section 133(1) of the Companies Act. As a result, a BRP may provide such consent in circumstances where to do so would unreasonably prejudice other affected persons or creditors. An example of such circumstance is the BRPs consenting to the directors of a company proceeding to recover their back-pay from the company where SARS is the company's only other creditor and the said directors are responsible for the company's financial distress. Another possible scenario is that the BRP unreasonably withholds his or her consent to legal proceedings or enforcement actions. In this situation, the affected person has no alternatives but to either wait for the business rescue proceedings to end or approach the court for the permission to proceed therewith. It is a reasonable conclusion that SARS would be one such creditor, especially where the purpose of the business rescue is to delay SARS collection of tax debt.

2.4.3. Process for the commencement of business rescue

Sections 129(1) and 131(4), read with the definitions under section 128 of Chapter 6 of the Companies Act, set out the circumstances in which a company may lawfully

[80]S150(2)(b)(i) Companies Act 71 of 2008.

commence with business rescue proceedings. This may take place in one of two ways; by the passing of a company resolution to begin business rescue proceedings[81] or by court order made upon application of an affected person as defined in the Companies Act.[82] Each avenue for the commencement of business rescue has its own procedure and these procedures are examined in greater detail below.

2.4.3.1. Voluntary business rescue

Under section 129(1) of the Companies Act, the board of a company may resolve that the company commence business rescue proceedings if its members have reasonable grounds to believe that the company is financially distressed and there appear to be a reasonable prospect of rescuing it ("voluntary business rescue").

The Companies Act offers no definition of what is intended by "reasonable prospects of rescuing the company", but by implication, this would have to mean that there exists a reasonable possibility of rehabilitating the company to the point that it is no longer in financial distress. Regarding the requirement of "reasonable prospects", the legislation offers no guidance as to what should inform this evaluation nor does it provide examples of what would constitute this or from whose perspective the prospects should be evaluated as being reasonable (i.e. is it in the eyes of a reasonable man, accountant, attorney, business analyst or board member?). It is thus submitted that the "reasonable prospects" at least means that a reasonable person would conclude that there is a likelihood of success.

Creditors only become aware of a business rescue upon notification thereof or once the resolution has been filed with CIPC. There is consequently nothing that creditors can do to prevent companies from filing for voluntary business rescue by special resolution if there are no reasonable grounds for its directors to believe that the company is in financial distress, reasonable prospects of it being rehabilitated, or where the financial distress is fictitious or contrived for purposes of gaining the

[81]S129 Companies Act 71 of 2008.
[82]S131 Companies Act 71 of 2008.

benefits that flow from business rescue. The only realistic remedy available to creditors is to make application to a court to set the business rescue resolution aside as this shall result in the process being void ab initio. Unfortunately doing so comes at a substantial cost to the creditor.

2.4.3.2. Business rescue by court order

The courts have slightly different grounds in terms of which they may place a company into business rescue by court order, namely the court must satisfy itself that either:

- the company is financially distressed;
- the company has failed to pay over any amount in terms of an obligation under or in terms of 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 is a reasonable prospect of rescuing the company.[83]

Here creditors would rely on the court to properly interrogate the facts placed before it and, especially those upon which the applicant seeks to have the company placed into business rescue to ensure that the company is only placed into business rescue where the aforementioned grounds are well and truly met. This is positive from the perspective of having an objective, independent party acting as a check and balance.

The challenge posed to creditors in circumstances where a company is facing a court application to place it in business rescue is that in order to have any say in same the creditors would have to participate in a costly and time-consuming litigation process. There is a real risk in such process that not all creditors shall receive notice of the proceedings before a final order is granted but be negatively affected by the ultimate result were the company to be placed into business rescue. An additional drawback is that where such order is ultimately granted, affected persons may only approach the court to alter same, which is also a costly and time-consuming process. It is, therefore, possible that where affected persons are precluded from

[83]S131(4) Companies Act 71 of 2008.

participating in or instituting such litigation proceedings to protect their own interests in circumstances where they do not have the necessary financial means to do so.

2.4.5. Pre-commencement versus post-commencement debt

The relevance of the classification of debt as having been incurred before the commencement of business rescue ("pre-commencement debt") and after the date of commencement of business rescue ("post-commencement debt") is that it has a bearing on the voting interest of the relevant creditor when adopting the business rescue plan.[84] In SARS case, it is a concurrent creditor in business rescue proceedings unless it has obtained security from the company in business rescue prior thereto and would therefore instead be a secured creditor. To the extent that creditors' claims arise after the commencement of business rescue, they are considered to be post-commencement debt and may possibly have a voting interest in the business rescue (if provided for in the business rescue plan) which shall be equal to the value of the amount of their claim. Unfortunately, the determination as to whether SARS claim in respect of a tax liability amounts to a pre-commencement or post-commencement debt is not always clear-cut, examples of which include:

- where a tax debt that is only determined or quantified after the commencement of tax debt, but which relates to a pre-commencement tax period ("a later-maturing tax debt"); and
- the VAT claw-back in terms of section 22(3) of the VAT Act.

With regard to a later-maturing tax debt, sometimes a company commences with business rescue before the submission of the company's tax return(s) relating to a pre-commencement tax period, before commencement of an audit by SARS, or after the commencement of an audit by SARS but before the issuing of a letter of findings under section 42(2)(b) of the Tax Administration Act or the finalisation of such audit in terms of section 42(6) of the Tax Administration Act. As the rules regarding the classification of pre-commencement debt are unclear, companies or business rescue practitioners with unsavoury motives could use the classification as a means of

[84]S145(4)-(6) Companies Act 71 of 2008.

either including SARS as a creditor in the business rescue or excluding it from same in order to suit any possible unsavoury intentions. An example of how such unsavoury intentions could manifest include expediently pushing forward with the business rescue proceedings that entail a winding down of the company while SARS is in the process of raising an assessment but before SARS has a liquid debt.

Under section 22(3) of the VAT Act, the reduction of a debt (for instance in terms of an adopted business rescue plan or compromise under section 155 of the Companies Act) by a creditor may result in the debtor having to make an output tax adjustment and pay the output tax on the portion of the debt reduced.[85] Any input tax previously claimed by the debtor must be "clawed-back" in this manner if the full amount of the debt has not been paid in full within twelve months from the date it was incurred.[86] In situations where the debt of the business in business rescue is reduced in this manner after the date of commencement of business rescue, then it shall most likely be classified as a post-commencement debt and would accordingly not be subject to the business rescue plan nor form part of SARS voting interest in the business rescue.

2.4.5. Personal liability of BRPs and third parties

As stated above, the BRP assumes all management control and functions of the company under business rescue[87] and has the responsibilities, duties and liabilities of a director of the company contained in sections 75 to 77 of the Companies Act.[88] All of these duties and responsibilities assumed by the BRP are accompanied by a substantial immunity provided under the Companies Act in respect of the BRP's acts or omissions, where same was committed in good faith in the course of the exercise of the BRP's powers and performance of the BRP's functions.[89] BRPs may only be held liable for acts or omissions that they perform in their official capacity as a BRP if it can be shown that the BRP acted in absence of good faith or the conduct

[85]S22(3) of the Value-Added Tax Act 89 of 1991.
[86]S22(3) of the Value-Added Tax Act 89 of 1991.
[87]S140(1)(a) Companies Act 71 of 2008.
[88]S140(3)(b) Companies Act 71 of 2008.
[89]S140(3)(c)(i) Companies Act No 71 of 2008.

amounted to gross negligence.[90] These are substantial thresholds to meet in order to hold a BRP liable for his or her conduct during their term as an appointed BRP. This makes it difficult for any affected person, including SARS, to pursue the BRP in circumstances where the BRP's conduct is not in the best interests of the stakeholders, or results in loss to the company or other affected persons.

The relevance of a public officer for tax purposes is that this person is held liable for all acts, matters or things that company must do under any tax Act and the Tax Administration Act.[91] There is nothing in the Companies Act that prohibits such appointment of the BRP as the public officer of the company in business rescue for tax purposes, but this Act does limit the extent to which SARS may hold the BRP personally liable as the above-mentioned limitations on the personal liability of the BRP apply.

2.4.6. Settlement and compromise

A conflict exists in the application of both Acts as SARS cannot conclude a settlement or compromise in circumstances outside of those prescribed in the Tax Administration Act, but is effectively compelled to do so as the circumstances prescribed for same under the Companies Act differ materially and the Companies Act is overriding legislation.

Insofar as settlement and compromise of tax debt is concerned, SARS may only do so in terms of Part F of Chapter 9 when concerned with a "disputed"[92] tax debt as defined and Part D of Chapter 14 of the Tax Administration Act respectively. This is because SARS is obliged to collect tax properly chargeable under the tax Acts on behalf of the National Revenue Fund and may only derogate from this duty by accepting the payment of an amount less than the tax debt properly chargeable in

[90]S140(3)(c) Companies Act No 71 of 2008.
[91]S246(5) Companies Act 71 of 2008.
[92]Section 142 of the Tax Administration Act 28 of 2011 defines a "dispute" as a disagreement on the interpretation of either the relevant facts involved or the law applicable thereto, or of both the facts and the law, which arises pursuant to the issue of an assessment or the making of a 'decision'

limited circumstances.[93] During business rescue proceedings creditors are often required to compromise or settle for the payment of a lesser amount than the amount owed to them by the company in terms of the business rescue plan.[94]

2.4.6.1. Settlement

With the settlement of a disputed tax debt, SARS may only consent to the settlement of a tax debt where it is to the best advantage of the State to do so[95] having regard to specific circumstances that include, for instance, whether settlement is a cost-effective way to promote compliance with the tax Acts. In addition, SARS may not agree to the settlement of a tax debt where none of the appropriate circumstances of settlement mentioned in section 146 of the Tax Administration Act exist and, *inter alia*, the dispute constitutes intentional tax evasion or fraud or the taxpayer has not complied with provisions of a tax Act and the compliance is of a serious nature.[96] A term of the business rescue plan could be that SARS must settle a disputed tax debt and once the plan is adopted it shall be binding on SARS even if SARS voted against the adoption thereof.[97] Under the Companies Act, a creditor can be bound by an adopted business rescue plan even if the relevant creditor voted against such a plan.[98] It is therefore conceivable that SARS may be bound to settle a tax debt where it is unable to do so under the Tax Administration Act.

2.4.6.2. Compromise

Insofar as a compromise is concerned, SARS may only compromise in circumstances where the taxpayer does not dispute the relevant tax debt and it, is

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[93]These circumstances include an instalment payment agreement in terms of Part D of Chapter 10 of the Tax Administration Act, a permanent write-off of a tax debt under Part C of Chapter 14 of the Tax Administration Act 2011 and a compromise of a tax debt in terms of Part D of Chapter 14 of the Tax Administration Act; See also *CIR v The Master* 1957 3 SA 693 (C) 701-702; *AM Moolla Group (Ltd) v CSARS* 2003 JOL 10840 (SCA) paras 17-20; s143(1) Tax Administration Act 28 of 2011; s193(1)-(2) Tax Administration Act 28 of 2011.

[94]S154 Companies Act 71 of 2008; Kunst, Boraine and Burdette *Insolvency Law* SI 51 ed (2018) 18.18.

[95]S146(1) Tax Administration Act 28 of 2011.

[96]S146(1)(e) Tax Administration Act 28 of 2011.

[97]S152(2) Companies Act 71 of 2008; S153(1)(ii) Companies Act 71 of 2008.

[98]S152(2) Companies Act 71 of 2008; S152(3)(b)-(c) Companies Act 71 of 2008; S152(4) Companies Act 71 of 2008.

done on request of the taxpayer. The request must be supported by a detailed statement that sets out, *inter alia*, detailed information regarding the financial position of the taxpayer.[99] Furthermore, SARS is unable to compromising a tax debt in circumstances described under section 203 of the Tax Administration Act that includes where the debtor is a company and SARS has not first explored holding persons personally liable for the said tax debt in terms of Part D of Chapter 11 of that Act.[100]

In strong contrast to the stringent compromise provisions of the Tax Administration Act, is a compromise under the Companies Act. There are effectively two means of compromise of debt, namely section 155 of this Act and the adoption of a business rescue plan that makes provision for the compromise of the tax debt. Section 155 of the Companies Act allows for the compromise of a debt of all creditors and all creditors who are members of a particular class of creditors ("section 155compromise").[101]The Companies Act does not stipulate any grounds upon which compromise may or may not be adopted by the creditors. The only requirements for the adoption of a section 155 compromise are that where a company is in business rescue it is in financial distress as defined in the Companies Act,[102] a notice of a meeting to consider a compromise proposal and the proposal that complies with section 155(3) of the Companies Act is delivered to all creditors or all creditors of a particular class of creditors and CIPC,[103] and that the proposal must be supported by persons representing at least seventy five percent (75%) of the value of the creditors or class of creditors present in person or by proxy and voting at the meeting.[104]

For purposes of section 155 compromise, the legislation does not stipulate a number of days' notice that must be given to a creditor or, where creditors like SARS have numerous offices in South Africa, that the notice must be served on the creditor's registered head office or even how the notice must be transmitted. This places

[99]S200-201 Tax Administration Act 28 of 2011.
[100]S203(f) Tax Administration Act 28 of 2011.
[101]"Commission" as defined in section 1 of the Companies Act 71 of 2008; s155(2) Companies Act 71 of 2008.
[102]S155(1) Companies Act 71 of 2008.
[103]S155(2) Companies Act 71 of 2008.
[104]S155(6) Companies Act 71 of 2008.

creditors like SARS at a substantial disadvantage when faced with a section 155 compromise because the BRP or company that wishes to compromise a tax debt for nefarious means may simply serve the notice of meeting and proposal at an obscure SARS branch office located hundreds of kilometres from the meeting venue (possibly even in another province) on the day before the meeting is to take place (e.g. one business day) and still discharge the requirement regarding service of the notice of the meeting and proposal under the Companies Act. The reality is that SARS is an organ of state that employs in excess of twelve thousand employees across the country and it is an unreasonable expectation that its employees in a branch office, whose job functions are to primarily assist large numbers of taxpayers with submission of returns, resolving queries and to render other such administration and processing assistance, shall attend to the notice or attend the meeting on such short notice. Due to the fact that section 155 only requires that that seventy-five percent of the relevant creditors in attendance and voting at the meeting must vote in favour of adoption for the proposal to be adopted and rendered binding on all persons whom it concerns, it is possible that such proposal may be binding on SARS where it was not served with proper notice of the meeting and was unable to attend the same.

Another form of compromise often manifests in the business rescue plan itself. The wording of the plan and rehabilitation steps to be taken may in effect constitute a compromise and once adopted shall be binding on the relevant creditors whether they voted in favour of same or not.[105] As a result SARS shall be bound to the compromise of its debt as per the adopted plan. This may be used as a mechanism to greatly reduce the company's tax debt where SARS is the only independent creditor of the company and is binding on SARS unless withdrawn by agreement or set aside by a court.

2.4.7. Business rescue vs. liquidation

This section focuses on certain practical implications of business rescue for SARS, and the fiscus, when compared to liquidation. The aspects addressed hereunder

[105]S100 Insolvency Act 24 of 1936.

include the differences between how SARS claim would be ranked in the two processes, the mechanisms available for the investigation of the company's affairs, and the real possibility of removing a company in preliminary and even final liquidation and placing it into business rescue.

2.4.7.1. Ranking of creditors' claims

The first noticeable difference between business rescue and liquidation proceedings from the perspective of SARS as a creditor is that SARS enjoys preferential creditor status in the liquidation proceedings,[106] while it ranks as a mere concurrent creditor in business rescue proceedings. The relevance of a creditor's ranking is that it determines the order in which the creditor's claim shall be satisfied which in turn translates into the amount of money it shall receive in respect of its claim against the company. To contextualise, in liquidation proceedings referent creditor is entitled to the satisfaction of its claim from the proceeds of the realisation of unsecured assets and rank before concurrent creditors,[107] but after the costs in the administration of the estate and the claims of secured creditors.[108] Concurrent creditors are paid from the amount of money that is left in the estate of the company after all other claims have been paid in full and in proportion to the amount that is owed to them.[109]

In business rescue proceedings the ranking differs as Chapter 6 of the Companies Act has created new rankings for certain claims. The highest ranking claims are the BRP's fees and his or her expenses associated with the business rescue proceedings.[110] These claims rank above any claim of the other creditor in the business rescue proceedings. The next tier of creditors' claims those for services rendered by employees of the company in business rescue as these claims are deemed to be post-commencement finance.[111] This is then followed by the claims of secured creditors including those who obtained security over the company's assets

[106]S99(1)(b) Insolvency Act 24 of 1936; s101 Insolvency Act 24 of 1936.
[107]S99(1)(b) Insolvency Act 24 of 1936; s101 Insolvency Act 24 of 1936; Kunst, Boraine and Burdette *Insolvency Law* SI 51 ed (2018) 12.4.1.1-2; Kunst, Boraine and Burdette *Insolvency Law* SI 51 ed (2018) 12.4.8-9.
[108]Kunst, Boraine and Burdette *Insolvency Law* SI 51 ed (2018) 12.4.1.1-2.
[109]Kunst, Boraine and Burdette *Insolvency Law* SI 51 ed (2018) 12.4.1.3.
[110]S135(3) Companies Act 71 of 2008; s143 Companies Act 71 of 2008.
[111]S135(1) Companies Act 71 of 2008; s135(3)(a) Companies Act 71 of 2008.

after business rescue proceedings commenced (as this is secured post-commencement finance).[112] Thereafter, these claims are unsecured post-commencement financing[113] and finally what follows are the claims of concurrent creditors, including SARS and remaining employees' claims against the company in business rescue.

It is evident that the change in SARS ranking as a creditor in business rescue proceedings to that of a subservient concurrent claim is a great departure from the position in liquidation. The change in ranking results in a situation whereby it is possible to force SARS to forego a substantial portion of the value of its claim where the business rescue plan is adopted due to a vote in favour of same by the other creditors. As it is possible to create artificial claims of employees, post-commencement finance etc. during business rescue where the company commences business rescue with the view of reducing its existing tax debt and the BRP is compliant with or orchestrating such scheme, this aspect of business rescue can be exploited for purposes of tax evasion.

2.4.7.2. Investigation into the affairs of the company

Unlike in liquidation proceedings,[114] Chapter 6 of the Companies Act does not make provision for a BRP to hold an inquiry into the affairs of the company in business rescue. The only investigative means provided for in business rescue is an investigation into the company's affairs with the purpose of considering whether there is a reasonable prospect of the company being rescued.[115] Although the directors of the company are obliged to co-operate and assist the BRP,[116] the BRP cannot compel these individuals to testify under oath or produce documentation through this process.

Business rescue relies almost entirely on the good faith, will and abilities of the BRP to investigate the affairs of the company. The BRP does not typically act under the

[112]S135(2)(a) Companies Act 71 of 2008; s135(3)(b) Companies Act 71 of 2008.
[113]S135(2)(b) Companies Act 71 of 2008; s135(3)(b) Companies Act 71 of 2008.
[114]Item 9 of Schedule 5 to the Companies Act 71 of 2008; s417-18 Companies Act 61 of 1973.
[115]S141 Companies Act 71 of 2008.
[116]S142 Companies Act 71 of 2008.

"supervision" of an independent body or office like the Master of the High Court unless ordered to render reports or make application to a court as contemplated in Chapter 6 of the Companies Act. Consequently, it falls to the creditors and other affected persons in the business rescue proceedings to try to keep the BRP honest and hold him or her to account (sometimes at a substantial time and financial cost to the affected person). It should be noted that the Companies Act does not contain any mechanism to compel the BRP to investigate the affairs of the company nor does it provide any sanction for the BRP's failure to do so, other than the removal of the BRP by application to a court for the BRP's removal where the BRP is still alive.[117] The costs of such application shall be borne by the applicant unless a cost order is granted against the BRP or any other person. In light of the above, the lack of independent oversight over the BRP and construction of the provisions of the Companies Act regarding the BRP's investigative duties creates an opportunity for the perpetration of tax evasion and to hide same where it has already taken place prior to the commencement of business rescue.

It should be noted that an inquiry in terms of the Companies Act 51 of 1973 (the "previous Companies Act") is not the only mechanism by which an inquiry can be held into the affairs of the company as SARS is still able to pursue an inquiry in terms of the Tax Administration Act,[118] but this is just for purposes of the administration of the tax Acts and can have material financial implications for SARS as it is run solely at SARS expense.

[117]S139 Companies Act 71 of 2008.
[118]S50-51 Tax Administration Act 28 of 2011.

Chapter 3: Analysis of the case law

3.1. Introduction

In this chapter, the author explores some of the issues identified in Chapter 2 within the context of the existing body of case law to determine whether business rescue is being used as a vehicle for tax evasion. This chapter also explores if business rescue could be used as a vehicle for tax evasion in circumstances where the case law did not concern tax. In order to make a determination as to whether it could be used for the latter, the author examines how business rescue is being used to the prejudice affected persons. This is then evaluated against the legislative requirements for tax evasion under the Tax Administration Act[119] to determine whether it meets the requirements of tax evasion.

3.2. Commencement of business rescue

A number of avenues for abuse of the process for the commencement of business rescue have been outlined in Chapter 2.[120] One such risk is that of companies may commence business rescue proceedings when they do not factually meet the requirements to do so. This risk is the greatest in respect of business rescue by voluntary resolution because there is no independent person or body, like a court, that scrutinises the state of the company against the legislative requirements for business rescue before the company is officially placed in business rescue.

Business rescue by voluntary resolution relies entirely on the good faith,[121] expertise and judgment of the company's directors or members to evaluate whether the company meets the requirements for business rescue. That being said, there is also nothing that prohibits the mere institution of an application for business rescue even in circumstances where the requirements of business rescue by court order are not

[119]See section 235 Tax Administration Act No. 28 of 2011.
[120]See 2.4.3 above.
[121]*Griessel and Another v Lizemore and Others* (2015/24751) [2015] ZAGPJHC 189; [2015] 4 All SA 433 (GJ); 2016 (6) SA 236 (GJ) (31 August 2015) para 139.

met. This is especially attractive where the company is already facing liquidation and the consequences that flow from this. This does not in itself constitute tax evasion under section 255 of the Tax Administration Act.

3.2.1. Business rescue by court order

There are court cases that demonstrate that the risks of companies commencing voluntary business rescue and persons instituting applications for business rescue where the company is incapable of rehabilitation have indeed materialised.[122]I n the case of *Burmeister v Spitskop Village Properties Ltd*[123] the company had been in liquidation for 4 years and the liquidator had taken "far-reaching steps" during this time period which could not be undone without bringing about unwanted consequences.[124] In addition, the court found that the company had lost its "substratum" with the result that there was nothing to rehabilitate and it had no means of carrying on any business or trade.[125] What this means is that the company could not be rescued as it had no means of operating, there was effectively nothing left of the company to rescue and the company was insolvent. Consequently, the court held that the company could not be placed into business rescue and should instead be wound up.[126] The judgment on appeal is in line with the body of case law that deals with the need for the existence of reasonable prospects of success of business rescue as a requirement to commence business rescue and that no such prospects could exist where the company no longer had a substratum.[127] Although this requirement is supported by the cases, there is no check and balance that prevents abuse of the commencement of business rescue. As a result, creditors

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[122]*Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 (Pty) Lt*d (15155/2011) [2011] ZAWCHC 442; 2012 (2) SA 423 (WCC) (25 November 2011); *Burmeister and Another v Spitskop Village Properties Ltd and Others* (76408/*2013*) [2015] ZAGPPHC 1094 (21 September 2015); *Burmeister and Another v Spitskop Village Properties and Others (Commissioner for the South African Revenue Service Intervening)* (76408/2013) [2016] ZAGPPHC 72 (22 January 2016).

[123]*Burmeister v Spitskop Village Properties Ltd* (21 September 2015) *supra*; *Burmeister v Spitskop Village Properties Ltd* (22 January 2016) *supra*.

[124]The undesirable consequences in *Burmeister and Another v Spitskop Village Properties Ltd* (21 September 2015) included holding an inquiry in terms of sections 417 and 418 of the Companies Act, 1973, as well as the tracking, tracing and recovery of foreign assets and money held outside of South Africa (at 42-44).

[125]*Burmeister v Spitskop Village Properties Ltd* (21 September 2015) *supra* paras 29-30.

[126]*Burmeister and Another v Spitskop Village Properties Ltd* (21 September 2015) *supra* paras 48-49.

[127]*Burmeister and Another v Spitskop Village Properties Ltd* (21 September 2015) *supra* paras 29-30.

such as the Registrar of Banks and SARS are being forced to intervene in applications for business rescue instituted where there were in fact no reasonable prospects of rescuing the company concerned in order to oppose these applications.[128]

3.2.2. Voluntary business rescue

There is also a growing body of case law that confirms that companies are commencing voluntary business rescue in circumstances where they do not meet the legislative requirements. As discussed above,[129] there is no independent check and balance to confirm that companies that commence voluntary business rescue are doing so in compliance with the legislation. It is submitted that this makes voluntary business rescue a viable and attractive means of perpetrating and concealing tax evasion as discussed earlier.[130] The resolution to commence business rescue must be taken in good faith and the failure to do that could result in the court setting aside the resolution, which renders it void ab initio, but requires that the courts are approached to obtain such an order.[131] This is not ideal as instituting legal proceedings would cost the applicant time and money.

In the cases of *Cawood and Beer NNO v Tiar Construction CC*[132] and *Cawood and Beer NNO v Phehla Umsebenzi Trading 48 CC*[133] SARS successfully intervened in the application instituted by the erstwhile BRPs to convert the business rescue into liquidation. SARS also successfully instituted a counter-application to set aside the resolution to commence business rescue and wind-up both entities.[134] Insofar as Tiar Construction CC ("Tiar") was concerned, the judgment states that the Commissioner contended that there were never any prospects of rescuing Tiar and the conversion

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[128]*Southern Palace Investments 265 v Midnight Storm Investments 386 supra*.
[129]See 2.4.3.1 above.
[130]See para 3.2 above.
[131]*Griessel v Lizemore supra*.
[132]*Cawood and Beer NNO v Tiar Construction CC (Commissioner for the South African Revenue Service intervening)* (ZAGPHC) unreported case no. 93288/2015 (06 June 2018).
[133]*Cawood and Beer NNO v Phehla Umsebenzi Trading 48 CC (Commissioner for the South African Revenue Service intervening)* (ZAGPHC) unreported case no. 93289/2015 (06 June 2018).
[134]A single judgment was handed down in respect of these cases seemingly due to the facts that the cases were enrolled on the same day, heard at the same time and there some shared facts in both matters; *Cawood and Beer NNO v Tiar Construction CC* and *Cawood and Cawood and Beer NNO v Phehla Umsebenzi Trading 48 CC supra* para 9.

of the business rescue to liquidation would result in the business rescue practitioners being unduly entitled to fees to the prejudice of the affected persons.[135] In the judgment, the court noted that in the case of Tiar the financial statements showed that the financial distress as a resulted from the advancement of significant loans to connected parties. It was further noted that Tiar made significant distributions of profits to its members even after becoming aware of its tax liability proceeded to.[136]

In respect of Phehla Umsebenzi Trading 48 CC ("Phehla"), the court noted that the financial statements evidenced that Phehla's financial distress was also due to it advancing significant interest-free loans to connected parties and subsequently failing to call them up.[137] In its papers the Commissioner alleged that if Phehla or the BRPs had called these loans up then it would have been able to pay all of its creditors including its tax debt[138] and that the recipients of the loans included entity that had stopped trading per CIPC's records and entities that had not submitted tax returns for a substantial number of tax years.[139] The Commissioner also alleged that the BRPs failed to discharge their duties to investigate Phehla's affairs, call up the loans advanced by both entities to, *inter alia*, connected parties and take control of Phehla's assets.[140]

The court noted and expressed concerns that a couple of years passed before the BRPs concluded that the entities were beyond rehabilitation and as noted by the court, and in spite of this passage of time, placed insufficient evidence before the court as to what steps they had taken to investigate the affairs of and rehabilitate the entities which ultimately counted against them.[141] In addition to the above, the court

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[135] *Cawood and Beer NNO v Tiar Construction CC* and *Cawood and Cawood and Beer NNO v Phehla Umsebenzi Trading 48 CC supra* para 16.
[136] *Cawood and Beer NNO v Tiar Construction CC* and *Cawood and Cawood and Beer NNO v Phehla Umsebenzi Trading 48 CC supra* paras 23-25 and 56.
[137] *Cawood and Beer NNO v Tiar Construction CC* and *Cawood and Cawood and Beer NNO v Phehla Umsebenzi Trading 48 CC supra* paras18-19 and 57-58.
[138] *Cawood and Beer NNO v Tiar Construction CC* and *Cawood and Cawood and Beer NNO v Phehla Umsebenzi Trading 48 CC supra* para 20.
[139] *Cawood and Beer NNO v Tiar Construction CC* and *Cawood and Cawood and Beer NNO v Phehla Umsebenzi Trading 48 CC supra* para 18.
[140] *Cawood and Beer NNO v Tiar Construction CC* and *Cawood and Cawood and Beer NNO v Phehla Umsebenzi Trading 48 CC supra* paras 20 and 26.
[141] *Cawood and Beer NNO v Tiar Construction CC* and *Cawood and Cawood and Beer NNO v Phehla Umsebenzi Trading 48 CC supra* para 38.

infers that the BRPs spent an undue amount of time and effort on interactions with SARS to renegotiate its tax debts in spite of the fact that the actual causes of the financial distress of each entity were not its tax liabilities.[142]

In light of the various observations made by the court in the Tiar and Phehla matters, it is possible that the entities were in a state of artificial or self-induced financial distress. It is submitted that the circumstances described by the court in the Tiar and Phehla judgment are indicative that, at least insofar as the Commissioner is concerned, the assets of Tiar and Phehla were dissipated by the members and other beneficiaries of loans prior to resolving to commence business rescue, and either the BRPs assisted the members in concealing this with the assistance of persons to whom work was outsourced by the BRPs or the persons to whom the work was outsourced under the watch of the BRPs assisted the members to do so. In light of the above, persons with an intention to evade tax or assist others in evading tax could commence business rescue, where a company is not in financial distress or is incapable of rehabilitation, and use it to assist them to evade tax by:

- making, allowing the making of or causing the making of a false statement or entry in a return or other document, or signs a return or other document submitted without reasonable grounds for believing that it was true;[143]
- preparing, maintaining or authorising the preparation or maintenance of false books of account or other records, or falsifying or authorising the falsification of books of account or other records;[144] and
- making use of, or authorising the use of, fraud or contrivance.[145]

[142]*Cawood and Beer NNO v Tiar Construction CC* and *Cawood and Cawood and Beer NNO v Phehla Umsebenzi Trading 48 CC supra* para 41.
[143]S235(1)(a) Tax Administration Act No. 28 of 2011.
[144]S235(1)(b) Tax Administration Act No. 28 of 2011.
[145]S235(1)(d) Tax Administration Act No. 28 of 2011.

3.3. Moratorium on “enforcement actions”

3.3.1. Enforcement action

As discussed in Chapter 2, there is a moratorium on legal proceedings, including enforcement actions, during the period that a company is in business rescue.[146] Furthermore, an “enforcement action” is not a concept that is defined in the Companies Act and has not been ascribed any generally accepted meaning in South African law. Nevertheless, the Companies Act prohibits the taking of any such action against a company in business rescue. Although the courts have given some consideration to what could constitute an “enforcement action” under section 133(1) of the Companies Act,[147] this concept within the context of tax has yet to be considered.

Insofar as the general meaning of the business rescue moratorium is concerned, there is not much clarity in this regard either. In *Cloete Murray NO v First Rand Bank Ltd t/a Wesbank*[148] the Supreme Court of Appeal (“SCA”) had to consider section 133(1) in a dispute over whether the cancellation of a contract constituted an “enforcement action” as envisaged in the section. Fourie AJA commented obiter that an “ ‘enforcement action’ relates to formal proceedings ancillary to legal proceedings, such as the enforcement or execution of court orders by means of writs of execution or attachment.”[149] He also noted that the phrase “legal proceedings” usually bears the meaning of a lawsuit and that an “enforcement action” was a kind of legal proceedings or has its origins in legal proceedings because per section 133(1) the proceedings could only begin or continue in a “forum”, which usually refers to a court or tribunal.[150]The court then concluded that the word “forum” relates to formal

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[146] Section 133 Companies Act No. 71 of 2008.

[147] See *Chetty v Hart NO* 2014 JDR 0585 (KZD)wherein the court held that legal proceedings as contemplated in section 133 of the Companies Act do not include arbitration proceedings.

[148]*Cloete Murray and Another NNO v First Rand Bank Ltd t/a Wesbank* 2015 (3) SA 438 (SCA).

[149]*Cloete Murray NO v First Rand Bank Ltd t/a Wesbank supra* para 31; See *Alderbaran (Pty) Ltd and Another v Bouwer and Others* (19992/2017) [2018] ZAWCHC 38; [2018] 3 All SA 71 (WCC); 2018 (5) SA 215 (WCC) (22 March 2018) para 35.

[150]*Cloete Murray NO v First Rand Bank Ltd t/a Wesbank supra* paras 31 and 32; *Chetty v Hart* (20323/2014) [2015] ZASCA 112; 2015 (6) SA 424 (SCA); [2015] 4 All SA 401 (SCA) (4 September 2015) para 14.

proceedings ancillary to legal proceedings like the execution of court orders through writs of execution or attachment orders.[151]

A problem manifests when considering these remarks of the SCA to the collection of taxes. This problem relates to an application for judgments under section 172 of the Tax Administration Act and the execution of attachments as well as sales in execution based on section 172 judgments. Section 172 judgment is obtained from the clerk or registrar of the relevant court and is of similar force and effect to a court order or judgment. Consequently, it is arguable that the business rescue moratorium also functions to stop SARS in its tracks insofar as collection steps are concerned. As stated in Chapter 2, the position regarding the application of the moratorium to SARS application of set-off under section 191 is also still unclear and required clarification. However, if “enforcement steps” is to be interpreted using its ordinary meaning then the moratorium indeed prohibits such set-off.

3.3.2. Moratorium

The next issue under consideration is the use of business rescue to perpetrate tax evasion through the use of the moratorium. As discussed in Chapter 2 and above, the benefit of the business rescue moratorium may be open to abuse and could facilitate a situation of prejudice to SARS and other affected persons. There is also the risk of a company’s business rescue proceedings continuing for an excessive period of time during which SARS shall be unable to take steps to collect a tax liability. It is feasible that if business rescue is used to delay or defer payment or execution of a claim against the company, that the same tactic can be employed against SARS to delay its collection and enforcement of the submission of outstanding tax returns.

As stated above, the already limited case law relating to criminal prosecutions for tax evasion does not have any judgments as yet that relate to business rescue. As a result, one must turn to the civil cases regarding the abuse of the business rescue

[151] *Cloete Murray NO v First Rand Bank Ltd t/a Wesbank supra* paras 32-33.

process for the purpose of benefitting from section 133(1) to determine whether this could be used to perpetrate tax evasion. In Davis AJ's judgment delivered in *Alderbaran (Pty) Ltd v Bouwer*[152] he identifies this case as being demonstrative of the potential for abuse of the business rescue process and moratorium.[153] A default judgment had been obtained against Alderbaran (Pty) Ltd ("Alderbaran") due to its failure to pay a portion of the purchase price of an immovable property.[154] Alderbaran's sole director subsequently placed the company into voluntary business rescue with the purpose of using the business rescue moratorium against enforcement steps to stop a sale in execution of immovable property.[155] In addition, connected persons to the sole director purport to be Alderbaran's creditors in respect of alleged unsecured loans that were not evidenced by the production of documentary proof thereof.[156]

Although this case does not specifically concern the abuse of the business rescue process for achieving a benefit to the prejudice of SARS or tax evasion, it demonstrates that the business rescue moratorium is open to abuse and is an attractive means to delay or avoid enforcement actions such as collection steps instituted against companies by their creditors. Also, companies could effectively keep affected persons at bay for long periods of time by continuously filing voluntary business rescue resolutions to benefit from a near-perpetual business rescue moratorium. In SARS case this could mean an inability to collect on substantial tax debts for significant periods of time to the prejudice of the National Revenue fund. The moratorium could also thus be used for the purpose of tax evasion the non-submission of tax returns of the company in business rescue to frustrate SARS participation in the business rescue, especially if the company does not have an unpaid tax liability prior to the date of commencing business rescue. This could in turn be used to conceal tax evasion perpetrated by the company, or its directors and other individuals in their personal tax affairs.[157]

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[152] *Alderbaran (Pty) Ltd v Bouwer supra*.
[153] *Alderbaran (Pty) Ltd v Bouwer supra* paras 1 and 81.
[154] *Alderbaran (Pty) Ltd v Bouwer supra* para 6.
[155] *Alderbaran (Pty) Ltd v Bouwer supra* para 9.
[156] *Alderbaran (Pty) Ltd v Bouwer supra* para 22.
[157] S235(a) Tax Administration act No. 28 of 2011; s235(c) Tax Administration Act No. 28 of 2011.

In the case of *Griessel v Lizemore*,[158] the BRP did not take steps to interrogate the facts that were presented to him by the sole director who nominated him for the appointment of BRP and he failed, to take certain steps, including engaging with the shareholders.[159] The judgment also makes mention of serious allegations made against the sole director by the other shareholders including the dissipation of company assets for his benefit and the benefit of persons connected to him, and implying that he neglected his fiduciary duties towards the company.[160] This matter is demonstrative of the possibility that directors may resolve to commence business rescue as a means of avoiding liability for these allegations through the moratorium under section 133(1) and appointed a compliant BRP who would allow him to remain in control of the company while it was in business rescue. It is also feasible that, if given the opportunity for the business rescue to run its course as it was before the intervention of the shareholders, the sole director could have exploited these circumstances to continue to dissipate assets and conceal his conduct. The *Griessel v Lizemore*[161] judgment makes no mention of the company's tax affairs. It is thus unknown whether the sole director or the company was tax compliant, but it stands to reason no individual would declare any benefits received in terms of dissipation of assets from a company where such individual also tried to conceal the said dissipation. The act of non-declaration or under-declaration of one's income by way of the making of a false statement or entry in a return or other document could constitute tax evasion in the absence of reasonable grounds to believe that this is true.[162] It is therefore possible for the business rescue moratorium to be used to perpetrate tax evasion for both individuals and the company in business rescue in this way.

3.4. Compromise

As discussed above, the operation of section 155 of the Companies Act presents challenges to SARS as SARS can only compromise tax liabilities under the

[158]*Griessel v Lizemore supra*.
[159]*Griessel v Lizemore supra* paras 7-8.
[160]*Griessel v Lizemore supra* para 139.
[161]*Griessel v Lizemore supra*.
[162]S255(1)(a) Tax Administration Act No. 28 of 2011.

circumstances contemplated in the Tax Administration Act. The judgment handed down by Raulinga J in the matter of the *CSARS v Cross Atlantic Properties*[163] concerns the rescission of an order sanctioning a compromise in terms of section 155 of the Companies Act. This case involves unravelling the steps in a scheme that was aimed entirely at reducing Cross Atlantic Properties (Pty) Ltd's tax liability by 80 percent by not giving the Commissioner notice of certain proceedings and inducing the court to sanction the order by omissions or possible misrepresentations.

To briefly summarise the facts, the Commissioner sought to rescind the sanctioning order for reasons including that:

- The Commissioner had not been given notice of the application to the court to sanction the compromise and the Commissioner would have opposed the application had he been given notice thereof;
- The Commissioner's claim had been reduced to R0.20 in the rand (i.e. by 80 percent) in terms of the compromise;[164]
- The Commissioner did not receive notice of the sanctioning order and the order was granted on an *ex parte* basis in spite of the fact that it materially affected the rights of the Commissioner;[165] and
- The Commissioner was precluded from compromising the tax liability under sections 201 and 203 of the Tax Administration Act.[166]

The compromise was adopted at a meeting purportedly held in terms of section 155(2) read with section 155(6), attended by a single concurrent creditor by proxy, and attended by no preferent creditors (including SARS).[167]. In spite of the fact that there were two classes of creditors, a single meeting was held for both at which the concurrent creditor represented by proxy voted to accept the compromise and it was on this basis that the compromise was adopted and sanctioned under section 155 of the Companies Act.[168] The relevance of the different classes of creditors is that such creditors would not vote with the same purpose or have the same interest and

[163]*Commissioner for the South African Revenue Service v Cross Atlantic Properties (Pty) Ltd and Others* (43580/2015) ZAGPPHC 554 (4 August 2017).
[164]*CSARS v Cross Atlantic Properties supra* para 23.
[165]*CSARS v Cross Atlantic Properties supra* paras 7 and 25.
[166]*CSARS v Cross Atlantic Properties supra* para 27.
[167]*CSARS v Cross Atlantic Properties supra* para 6.
[168]*CSARS v Cross Atlantic Properties supra* para 17.

benefits when voting for or against a compromise under section 155 and there would at least need to be representation from each class of creditor in attendance at the meeting in order for such vote to be binding on the class of creditors itself.

Furthermore, the sanctioning of a section 155 compromise is one such order that should not be granted *ex parte* and without notice being served on the persons whose claims are compromised especially when such persons were not present at a meeting convened for the purpose of adopting the compromise.[169] The court held that a valid compromise, insofar as it involves SARS, is one that the Commissioner is not precluded from entering into under the Tax Administration Act.[170]

The case of the *CSARS v Logikal Consulting (Pty) Ltd*[171] bears some similarities to the aforementioned case. However, in this matter, it was alleged and upheld by the court that the Commissioner did not receive proper notice of the meeting at which the compromise was voted on and adopted. The factual nexus outlined in the judgment is that the Commissioner received notice of the meeting by registered post on the day before the meeting and at a branch office, as opposed to its head office.[172] The court acknowledges that due to the size of SARS, a notice received less than 24 hours before a meeting will not reach the relevant person and did not do so in this case.[173] The court notes that the notice of the meeting was deliberately sent to a SARS branch office instead of SARS designated address for delivery of which the first three respondents were made aware.[174] The court further noted the attitude taken by these three respondents by again choosing not to give SARS notice of the sanctioning application for “no apparent reason” despite the fact that this order adversely affects the rights of SARS as it is accepted that in such circumstances proper notice is required.[175] As a result, a punitive cost order was granted in the matter.

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[169]*CSARS v Cross Atlantic Properties supra* para 25.
[170]*CSARS v Cross Atlantic Properties supra* para 23.
[171]*Commissioner for the South African Revenue Service v Logikal Consulting (Pty) Ltd* and Others (96768/2016) [2018] ZAGPPHC 159 (29 March 2018).
[172]*CSARS v Logikal Consulting (Pty) Ltd supra* paras 46-52.
[173]*CSARS v Logikal Consulting (Pty) Ltd supra* para 28.
[174]*CSARS v Logikal Consulting (Pty) Ltd supra* para 79.
[175]*CSARS v Logikal Consulting (Pty) Ltd supra* para 80.

The above mentioned two cases illustrate that section 155 of the Companies Act can be used to perpetrate tax evasion. The conduct of the persons involved as outlined in the judgment could meet the requirements of tax evasion under the Tax Administration Act insofar as false statements were made, records or books of account were falsified, or to the extent, contrivance or fraud was used or authorised.[176] In addition, the court was required to provide substantial interpretation and develop precedent in respect of the section in order to mitigate the risk that this may take place again in future.

3.5. Business rescue vs. liquidation

Some of the differences between business rescue and liquidation were discussed and compared in Chapter 2. Included in this discussion was the importance of inquiries under sections 417 and 418 of the previous Companies Act, which were contrasted with the activities in business rescue as reliant entirely on the skill, good faith and willingness of the BRP. Sections 417 and 418 of the previous Companies Act make provision for an inquiry to be convened that entails summoning persons to be questioned under oath or affirmation regarding the affairs of the insolvent company.[177] This mechanism was also highlighted as important for the protection of creditors during the liquidation process. Insofar as business rescue is concerned, the BRP is not regulated and does not typically act under the supervision of an independent body or office. It is this important difference that could allow for tax evasion already perpetrated to go undiscovered or for it to be perpetrated during the business rescue process as a result of the affairs of the company not adequately coming to light. This aspect is discussed below insofar as it relates to business rescue being used to avoid or delay the aforesaid inquiry and then this is evaluated as a possible means to perpetrate tax evasion.

[176]S235(1) Tax Administration Act No. 28 of 2011.
[177]S417(1) Companies Act No. 61 of 1973.

3.6.1. Avoiding section 417 and 418 inquiries

The *Van Staden v Pro-Wiz (Pty) Ltd*[178] case pertains to, *inter alia*, the locus standi of liquidators to oppose an application for business rescue instituted in terms of section 131(1) of the Companies Act.[179] It is stated in the judgment that Oljaco CC ("Oljaco") had not been trading since 2014 and had no significant assets.[180] It was placed into final liquidation in May 2015.[181] Then in April 2017 Pro-Wiz Group (Pty) Ltd ("Pro-Wiz") instituted an urgent application to place Oljaco CC into business rescue in terms of section 131(1) of Companies Act, which was served on the same day that an inquiry in terms of section 418 of the previous Companies Act[182] was to commence.[183]

The sole member of Oljaco was meant to be interrogated at the inquiry on the same day that the application was served but failed to appear at the inquiry and a warrant had subsequently been issued for his arrest as a result.[184] This application was not accompanied by a business rescue plan nor did the applicant bother to consult with the liquidators or its principal creditor before launching the application.[185] The liquidators of Oljaco were cited as respondents therein and opposed this application on grounds that included that:

- the application for business rescue was an abuse of process of court and the business rescue process that was directed to avoid interrogation in the enquiry convened under section 418 of the previous Companies Act; and
- that the sole member of Oljaco and a director of Pro-Wiz were trying to strip Oljaco of assets and conceal them from creditors.[186]

In the judgment, SARS was recognised as the principal creditor in Oljaco's estate.[187] SARS successfully intervened in and opposed the application for business rescue in

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[178] *Van Staden and Others NNO v Pro-Wiz (Pty) Ltd* (412/2018) [2019] ZASCA 7 (8 March 2019).
[179] *Van Staden v Pro-Wiz (Pty) Ltd supra* paras 1-3
[180] *Van Staden v Pro-Wiz (Pty) Ltd supra* para 18.
[181] *Van Staden v Pro-Wiz (Pty) Ltd supra* para 16.
[182] *Van Staden v Pro-Wiz (Pty) Ltd supra* paras 16-17.
[183] *Van Staden v Pro-Wiz (Pty) Lt*d *supra* paras 17-18.
[184] *Van Staden v Pro-Wiz (Pty) Lt*d *supra* para 17.
[185] *Van Staden and Others NNO v Pro-Wiz (Pty) Ltd* (412/2018) [2019] ZASCA 7 (8 March 2019) para 22.
[186] *Van Staden v Pro-Wiz (Pty) Lt*d *supra* paras 18-21.

this matter. SARS highlighted that its own claim had been significantly under-stated in all business rescue projections made by Pro-Wiz, accused the sole member of Oljaco of dissipating Oljaco's assets and trying to conceal that this had occurred, and identified Pro-Wiz as being in possession of many of those assets.[188] Thereafter the application for business rescue was postponed several times and Pro-Wiz subsequently served a notice of withdrawal of the application two days before the hearing date and only tendered SARS costs.[189]

In the judgment the court acknowledges that the purpose of business rescue is rehabilitating a business that has fallen on hard times but is still capable of rehabilitation or, where that is not possible, to be used to ensure that creditors receive an better dividend than creditors would in liquidation.[190] The court was of the view that it could not have been the case in Pro-Wiz' application and that the application was instead instituted for motives ulterior to a genuine belief that the entity could be rehabilitated by business rescue.[191] The court expressed the following view:

> "[21] It is apparent that Pro-Wiz could never have thought that a viable business rescue could be instituted in relation to Oljaco. Its failure to engage with the liquidators or the principal creditor on that subject prior to launching its application speaks volumes in that regard. The timing of the application suggested that its true purpose was to stultify the interrogation of Mr Smith. The failure to deal with any of the issues raised by the liquidators and SARS in this regard indicates that no response was possible. Finally, the withdrawal at the very last minute, without explanation, when confronted with the reality of having to argue the application in court, conveyed the impression of an absence of any bona fide belief in the merits of the case and a lack of intention genuinely to pursue it. I conclude that it was brought to provide a reason for avoiding Mr

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[187] *Van Staden v Pro-Wiz (Pty) Ltd supra* para 21.
[188] *Van Staden v Pro-Wiz (Pty) Ltd supra* paras 99-100.
[189] *Van Staden v Pro-Wiz (Pty) Ltd supra* paras 2 and 20.
[190] *Van Staden v Pro-Wiz (Pty) Ltd supra* para 22.
[191] *Van Staden v Pro-Wiz (Pty) Ld*.

> Smith's interrogation and with a view to delaying the liquidators in their enquiries as to the squirreling away of assets."[192]

The *Van Staden NNO v Pro-Wiz (Pty) Ltd* case demonstrates the risk of entities commencing business rescue or making use of business rescue for purposes of avoiding these inquiries. As identified above, business rescue presents a number of avenues for persons with ulterior motives of perpetrating or continuing to perpetrate tax evasion and to concealing it. The fact that business rescue enables individuals to avoid sections 417 and 418 inquiries is a further advantage to the process that functions in conjunction with those ways and means already identified above that can assist tax evasion perpetrators and would-be perpetrators in their endeavours. In addition and as stated above, this could function as mechanisms for the concealment of tax evasion and for it to be perpetrated during the business rescue process due to inadequate ventilation of the company's affairs.

[192] *Van Staden v Pro-Wiz (Pty) Ltd* *supra* para 21.

Chapter 4: Recommendations and conclusion

4.1. Introduction

As discussed above, there are various gaps and ambiguities in Chapter 6 of the Companies Act.[193] There are also significant incongruences between the tax legislation and Chapter 6 of the Companies Act which may facilitate tax evasion and prejudice the state. Consequently, it is submitted that legislative amendments are required to remedy the problems identified and decrease the opportunities for business rescue to be used to perpetrate tax evasion. What follows in this chapter are recommendations of necessary legislative amendments that would address these incongruences and ambiguities.

4.2. Amend section 5 of the Companies Act

Where there are inconsistencies between the provisions of the Companies Act and the Tax Administration, section 5(4) of the Companies Act stipulates that the provisions of the Companies Act shall override that of the Tax Administration Act to the extent that the two cannot co-exist. This section of the Companies Act does, however, specify legislation to which this general rule does not apply. The Tax Administration Act is not included in the list of exceptions and is consequently subordinated to the Companies Act in those circumstances.

The challenge posed to SARS by this is the fact that SARS is obliged to follow the tax Acts and cannot derogate from these Acts unless ordered by a court to do so. As discussed earlier, there are inconsistencies in the application of section 155 of the Companies Act and section 200 read with section 201 of the Tax Administration Act[194] in relation to compromise of a debt. There are also inconsistencies in the application of the set-off contemplated in section 191 of the Tax Administration Act[195] and the moratorium against enforcement steps contained in section 133(1) of the Companies Act. As a result, SARS has to comply with the provisions of the

[193]Companies Act 71 of 2008.
[194]Tax Administration Act 28 of 2011.
[195]S191(1) Tax Administration Act 28 of 2011.

Companies Act and ignore the above mentioned provisions of the Tax Administration Act but is unable to do so. It is therefore recommended that section 5(4) of the Companies Act should be amended to include the Tax Administration Act, 2011, as overriding legislation in the event of inconsistency as contemplated in section 5(4).

4.3. Additional definitions

As identified earlier,[196] certain key words and phrases used in Chapter 6 of the Companies Act are not defined therein. The phrase “enforcement step” is introduced in the moratorium contained in section 133(1) of the Companies Act and creditors are prohibited from taking such steps during the operation of the business rescue proceedings. It would seem that based on an ordinary meaning of that phrase could be interpreted widely and the Companies Act provides no guidance as to what would constitute an enforcement step.[197] In addition, the terms "rehabilitate” is also not defined in the Companies Act.[198] To define these terms would provide clarity as to what the ultimate goal of the business rescue plan is as well as at what point a company in business rescue could be considered to have been rescued. Another phrase that should also be clarified is "reasonable prospects of rescuing the company”. This phrase is particularly important as it forms one of the prerequisites for commencing business rescue.[199] In light of the above, it is recommended that definitions for the concepts “enforcement step”, “rehabilitate” and “reasonable prospects of rescuing the company” should be introduced into section 128 of the Companies Act.

4.4. Notify SARS of all intentions to commence business rescue

There are circumstances in which SARS may be erroneously or intentionally excluded from participation in the business rescue process as an affected person. It follows that there will be circumstances where SARS claims are not yet determined

[196]See paragraph 2.3. above.
[197] See paragraph 3.2.1. above.
[198]See paragraph 2.3.1. above.
[199]See paragraphs 2.4.3.1 and 2.4.3.2 above.

at the time that a company commences business rescue as there is a later-maturing tax debt and that the commencement of business rescue at this time could be used as a means of excluding from or including the tax debt in the business rescue process.[200] In light of the above, it is recommended that the legislature:

- Include a provision in Chapter 6 of the Companies Act that requires SARS to be properly notified of the intention to place an entity in business rescue under sections 129 and 131 of the Companies Act within a reasonable time before doing so; and
- amend sections129(3), 131(2), and 155(2) of the Companies Act to specifically require that SARS must be properly notified of the proceedings.

4.5. Elevate SARS claims to preferent

SARS is not ranked as preferent creditor in business rescue.[201] In business rescue the highest ranking claims are for the BRPs remuneration and the costs as per section 143 of the Companies Act, thereafter the remuneration for amounts owing relating to employment which became due and payable during the business rescue proceedings, then the post-commencement financing, whether secured or unsecured, and lastly the unsecured claims against the company may be paid.[202] An argument in favour of the current ranking of there being no preferent creditors, like SARS, in business rescue is that the State continues to benefit from the subsistence of the company if it is successfully rescued. This is because the State shall enjoy the benefit of the continued collection of the company's taxes and the continued employment of the company's employees.[203]

Conversely, taxes collected by SARS are applied for the benefit of the greater body of the South African public.[204] In addition, withholding taxes, such as VAT and PAYE, are collected by the company from persons other than the company and remitted to

[200]See paragraph 2.4.5. above.
[201]See paragraphs 2.3.1.3.5. and 2.4.7.1. above; *The Commissioner for the South African Revenue Service and Beginsel NO* 2013(1) SA 307(C).
[202]ML Vorster 'Re-evaluating Statutory Preferences in Insolvency law' (LLM dissertation, University of Pretoria 2018) 25.
[203] Vorster 'Re-evaluating Statutory Preferences in Insolvency law'.
[204]Vorster 'Re-evaluating Statutory Preferences in Insolvency law' 25.

SARS. It is therefore recommended that these taxes are elevated to that of preferent claims in the business rescue process. The ideal situation would be one in which both SARS pre-commencement and post-commencement claims were elevated to this status, but a more reasonable middle-ground is that this should be the position in respect of all tax debts for all taxes that arise after the commencement of business rescue.

4.6. Clarification of post-commencement financing

The status of tax debts arising from tax returns that were required to have been submitted before the date of commencement of business rescue is uncertain at present. It is recommended that the position of SARS' claims in respect of tax debts not yet determined at the date of the commencement of business rescue is clarified. It would be ideal for SARS if these claims did not to form part of post-commencement financing and are instead considered costs incurred outside of the business rescue process, especially insofar as the tax liabilities arise as a result of VAT and PAYE as the company is merely receiving or withholding amounts on SARS behalf, and remitting the amounts to SARS. In addition to the above, it is recommended that section 135 of the Companies Act is amended so that the ranking of post-commencement financing claims create different classes of post-commencement financing creditors. This would curtail the extent to which tax liabilities due to SARS may be considered post-commencement financing.

4.7. Compromise

The deficiencies in section 155 of the Companies Act and the effect thereof were discussed earlier.[205] It was also noted that SARS instituted litigation proceedings to address and undo the effect of persons taking advantage of these deficiencies.[206]It is therefore recommended that the provisions of section 155 are amended to bring them in line with such precedent and eliminate any ambiguities that exist within the text itself. These amendments should include:

[205]See 2.4.5, 2.4.6.2 and 3.5 above.
[206]See paragraph 3.5. above.

- stipulating that the provisions of section 155 of the Companies Act must be read together with sections 200 and 201 of the Tax Administration Act insofar as the compromise of SARS' claim is sought; and
- incorporating the condition that a compromise under the section shall only be valid and enforceable insofar as all creditors whose claims are compromised received proper notice of the meeting to compromise. Furthermore, where the compromise is to be sanctioned by a court order then this should take place either on an *ex parte* basis with proper notice being served on the creditors whose claims have been compromised or that the application for sanctioning may not be instituted on an *ex parte* basis.

4.8. Independent regulatory body

Section 138 of the Companies Act sets out the requirements for the qualification of persons as BRPs, while subsection (1)(a) thereof refers to persons who are members of a number of professions and does so in the alternative. Consequently, one of the criteria stipulated for the accreditation of persons as BRPs includes membership to those professions as accredited by the CIPC. Furthermore, it is assumed that the qualification and expertise of one of the mentioned professions are sufficient in isolation to provide the required knowledge base and skill set for the business rescue practitioner's profession. It is submitted that business practitioners are required to draw on expertise found in, at least, all three professions to successfully rescue companies in financial distress and therefore require their own training, accreditation and regulation. Moreover, there is currently no list of all licensed BRPs and accreditation is done on a case by case basis by the courts. If the concept of business rescue is going to achieve its aims, then there must also be a greater level of regulation of the process and protection provided to all parties involved therein.

In light of the above, it is recommended that the legislature consider establishing an independent regulatory body to attend to work that includes the following:

- development of mechanisms for accreditation of business rescue practitioners ("BRPs");

- development and enforcement of a code of conduct for the BRPs' profession;
- regulate the BRPs' profession;
- enforce compliance with Chapter 6 of the Companies Act, 2008;
- increase awareness of and promote early intervention in financially distressed companies through the business rescue process; and
- provide training, including continuous professional development training, for BRPs and persons who occupy management positions in South African companies.

4.9. Dispute resolution processes and forums

Approaching the courts for intervention may easily result in lengthy and costly litigation for the parties. Litigation is typically not a cost-effective or time-efficient dispute resolution mechanism and can delay the finalisation of business rescue proceedings. In turn, this prejudices parties affected by the business rescue and can negatively impact the prospects of success of the business rescue. It is therefore recommended that dispute resolution processes and dispute resolution forums are established to deal with disputes relating to business rescue proceedings efficiently and cost-effectively. It is further recommended that dispute resolution forums such as specialised courts could be established by the Department of Justice, while alternative dispute resolution forums could be established by the independent regulatory body proposed above. A further recommendation is to consider making alternative dispute resolution mechanisms such as mediation and arbitration as the first step or preferred option for these disputes because parties often are required to continue a working relationship for the duration of the business rescue or after its termination. This would ultimately be a cost-effective and efficient way for parties like SARS to address issues and concerns.

4.10. Training and accreditation of BRPs

4.10.1. Training required for initial accreditation

Section 138(1)(a) of the Companies Act allows persons to take up appointments as BRPs if such a person is a member in good standing of a legal, accounting or

business management professional body.[207] Consequently, the training and accreditation of BRPs is currently dependent on the qualifications obtained by members of each professional body, admission criteria of these professional bodies, different codes of ethics applicable to each profession and that each profession adequately regulates its members and holds them accountable for their conduct. Furthermore, there are no business rescue specific training requirements stipulated as a prerequisite for the accreditation of BRPs. It is recommended that the legislation is amended to also require BRPs complete specialised training and/or qualifications specific to business rescue and insolvency.

4.10.2. Training requirements for maintaining accreditation

Many professional bodies require their members to complete continued professional development ("CPD") training each calendar year to remain members in good standing. Currently no such requirement exists for BRPs. It is recommended that BRPs should also be required to complete training courses specific to the BRP profession to maintain their accreditation within the profession.

4.11. Limited number of business rescue matters per BRP

Business rescue is intended to be a temporary process whereby companies can be both rehabilitated as soon as possible and, where rehabilitation is not possible, an expedient process for affected persons to obtain a higher dividend than what they would receive if the company was liquidated. The duties of BRPs stipulated in Chapter 6 of the Companies Act can require a substantial amount of time and effort to execute; especially in circumstances where the employees, directors or members are non-cooperative or the company's affairs are in disarray. The prospects of success of the business rescue decrease and risk of prejudice to affected persons, like SARS, increase when BRPs have insufficient time and resources to execute their duties accurately and expediently. These are unfair and unnecessary risks for all parties involved in the business rescue to bear. Considering the above, it is proposed that a limitation is imposed on the number of appointments that any BRP

[207] S138(1)(a) Companies Act 71 of 2008.

may accept or hold simultaneously. This may be achieved through the monitoring of appointments by the proposed business rescue regulatory authority or the introduction of this limitation in regulations to the Companies Act.

4.12. Independent appointment of BRPs

In voluntary business rescue the directors or members of the company bear the responsibility of deciding whether the company meets the requirements of section 129(1) of the Companies Act. These persons are also responsible for appointing the BRP in terms of section 129(3).[208] As a result, there is a real risk of collusion between the appointed BRP and the directors or members of the company resolving to commence business rescue. It follows that directors or members may use the business rescue process to hide fraud, dissipation of company assets, and contraventions of legislation including the Companies Act and Tax Administration Act. There is also a risk of collusion when business rescue commences by court order[209] as the affected person who institutes the application also nominates a person to be appointed as a BRP.[210] In light of the above, it is recommended that an independent oversight body should allocate a business rescue practitioner to each company commencing business rescue.

4.13. Curtail BRP fees and disbursements

The position at present is that business rescue proceedings can continue for extended periods and the BRP can charge fees that he or she deems appropriate. The highest ranking claims are the BRP's fees and disbursements.[211] The BRP also has the discretion to subcontract work to be performed during and relating to the business rescue proceedings to any third parties he or she deems appropriate for any fees he or she deems appropriate. Affected persons should have a right to review BRPs' fees as well as any related disbursements (such as fees of third-party accountants or consultants) incurred on the authorisation of the BRP during the

[208]Companies Act 71 2008.
[209]S131 Companies Act 71 of 2008.
[210]S131(5) Companies Act 71 of 2008.
[211]S135(3) Companies Act 71 of 2008; s143 Companies Act 71 of 2008.

business rescue proceedings and object to the payment thereof. It is recommended that the introduction of a special forum for the determination of such disputes in a similar, but more expedited, manner to the taxation of legal costs is considered.

4.14. Pre-assessment prior to commencing business rescue

There is currently no mechanism or requirement for the pre-assessment of whether a company meets the requirements of financial distress, reasonable prospects of rescue or whether business rescue would yield a higher dividend for affected persons than liquidation before a company may formally commence with business rescue. As a result, there is nothing preventing companies from commencing business rescue fraudulently, or when there are no reasonable prospects of successfully rescuing the company or obtaining a higher dividend for creditors than in liquidation. It is thus recommended that a pre-assessment report should be required before companies are finally placed into business rescue by voluntary resolution or court order. Moreover, if the pre-assessment is done by a person independent of the company and ultimately an appointed BRP, it would create an independent process to curtail the abuse of the business rescue process to evade tax and protect all affected persons.

4.15. Investigation of the affairs of the company

As discussed above, one of the drawbacks of the business rescue process is the fact that no business rescue process achieves the same result as sections 417 and 418 of the previous Companies Act[212] (“section 417 and418 inquiries”). There is also no prescribed procedure for the BRP to interview employees, directors or members in the discharge of the BRP’s duties in section 141 of the Companies Actor compels such persons to make full disclosure to the BRP. It is therefore recommended that similar mechanisms are introduced into Chapter 6 of the Companies Act. In doing so the BRP shall be able to interview the directors, financial management and other employees of the company to thoroughly investigate the reasons for the financial distress of the company regardless of whether such persons are co-operative or not.

[212]S417-418 Companies Act 61 of 1973.

It is further recommended that the legislature considers not making these interviews confidential or alternatively formulating exceptions to any confidentiality afforded that relates to bodies like SARS, the South African Reserve Bank, the National Prosecuting Authority and the Public Protector.

4.16. Limiting the section 133(1) moratorium

As canvassed above, there is room to abuse the section 133(1) moratorium on enforcement steps through the commencement of business rescue where, amongst other circumstances, the legislative grounds to commence business rescue are not met.[213]This abuse should be addressed by the legislature as a matter of urgency. It is recommended that the moratorium contemplated in this section be curtailed by introducing a further exception in this section that takes into account the set-off contemplated in section 191 of the Tax Administration Act[214] in respect of all assessments raised after the date of commencement of the business rescue. This can either be done in respect of all types of taxes or in respect of at least taxes such as Pay-As-You-Earn tax ("PAYE") and VAT where the company is required to withhold the amount of tax or receive payment of the tax and remit the money to SARS.

It is also recommended that the section 133(1) moratorium is limited to a specific period, after which time the BRP should be required to advance reasons to a court or the independent regulatory body as to why the moratorium should be extended. In addition, it is recommended that affected persons should be provided with a similar opportunity to approach the proposed regulatory body or a court to advance reasons as to why the above mentioned moratorium should be lifted or not be extended.

4.17. Suspension of proceedings under section 131(6)

As noted above, under section 131(6) of the Companies Act, 2008 liquidation proceedings are suspended if an application in terms of section 131 of the

[213]See 2.4.2 and 3.3. above.
[214]S191(1) Tax Administration Act 28 of 2011.

Companies Act, 2008 is instituted.[215] As a result, the liquidation proceedings are completely halted and the company is left in a state of limbo. It is recommended that the liquidator should remain the custodian of all company assets, remain empowered to continue the day-to-day operations of the business if it is still trading and be required to obtain the authorisation of the Master of the High Court to dispose of any company assets.

4.18. Punitive consequences

4.18.1. Wrongful initiation of business rescue proceedings

Chapter 6 of the Companies Act in its current form is open to abuse that include the initiation of business rescue proceedings in circumstances where the legislative requirements have not been met or have been fraudulently induced. Affected persons, such as SARS, are prejudiced by wrongful initiation of business rescue proceedings and currently have no statutory right to restitution for any damages incurred as a result. There are also no stipulated punitive measures for persons responsible for the wrongful initiation of business rescue proceedings. A balance should be struck between the need to save the jobs created by company in business rescue and the continued operation of the company, and the need to protect jobs created by affected persons as well as not cause affected persons to experience financial distress.

In light of the above, it is recommended that legislative provisions should be inserted that stipulate punitive consequences for those who initiate business rescue proceedings in circumstances that do not meet the legislative requirements. It is further proposed that in this instance the commencement of business rescue should mean the filing of a resolution to commence business rescue resolution in terms of section 129(b) of the Companies Act and the issuing of an application for business rescue at any court in the Republic of South Africa. In addition to the above, it is recommended that the punitive consequences include criminalising the wrongful initiation of business rescue proceedings and the imposition of fines.

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[215]S131(6) Companies Act 71 of 2008.

4.18.2. Collusion involving the BRP and BRPs who are not independent

It is similarly recommended that punitive consequences should be introduced into the Companies Act that penalise any person appointed as a BRP who is not independent of the company's employees or their relatives at the commencement of the business rescue or at any time during the duration of the business rescue. Punitive consequences should also be applicable to situations where BRPs are found to have colluded with the employees, members or shareholders of any company during the business rescue proceedings to conceal and dissipate assets, conceal mismanagement, conceal contraventions of the Companies Actor any other relevant legislation like the Tax Administration Act, or commit or conceal fraud. It should be noted that it may be more appropriate for the regulation of this conduct to be enforced by the proposed independent regulatory body.

4.18.3. BRPs who fail to carry out their duties

There is currently no mechanism by which affected persons can compel BRPs to perform or hold BRPs accountable for the failure to perform their duties, other than through the courts. Court proceedings are lengthy, expensive and the BRP could on-charge the litigation costs to the company in business rescue. This litigation would undoubtedly further prejudice the affected persons and should be avoided. A system whereby BRPs were to face punitive consequences such as fines, criminal charges, claims for damages and the risk of losing their accreditation as BRPs would function as an incentive to perform their duties with due skill and care, and in accordance with the Companies Act.

Chapter 5: Conclusion

The introduction of business rescue as a concept into South African law has changed South Africa's approach to corporate rescue to a culture of restructuring distressed businesses to avoid the termination of business through liquidation.[216] The discussions traversed in this mini-dissertation detail the shortcomings in Chapter 6 of the Companies Act that are capable of exploitation by opportunistic persons seeking to delay or evade the assessment and payment of tax liabilities of companies. The challenges identified from a tax perspective when applying the provisions of Chapter 6 of the Companies Act make for a challenging landscape for SARS to operate and address any potential or actual tax evasion. Briefly the issues identified as are follows:

- Uncertainty as a result of inadequate and/or no definitions provided for key concepts used in Chapter 6, including "enforcement step", "rehabilitation" and "reasonable prospects of rescuing the company";
- The wide ambit of the moratorium on enforcement steps conflicting with SARS prescribed duties and actions to be taken by SARS in terms of the Tax Administration Act;
- Indefinite length of the moratorium on enforcement steps;
- Lack of checks and balances regarding the meeting of the requirements for companies to commence business rescue;
- Wide powers, unfettered discretions and immunity granted to BRPs
- Lack of accountability and consequence management BRPs;
- Ambiguities and incongruences in the application of the Companies Act and Tax Administration Act regarding to settlement and compromise, and the failure of the Companies Act to require that proper notice is served on creditors in the event of a compromise under section 155; and
- Deficiencies in the investigation tools available to BRPs when compared to liquidation.

[216]Levenstein 'Appraisal of the new South African Business Rescue procedure' 649.

An analysis of the available case law confirms that Chapter 6 is indeed being abused and used to commit acts that *prima facie* appear to qualify as tax evasion as contemplated in the Tax Administration Act. The civil case law were analysed as no relevant criminal cases could be found. It would thus seem that SARS has yet to pursue any matters criminally on the grounds of tax evasion. However, the absence of criminal case law on the subject does not prove that business rescue has not or is not currently being used as a vehicle for tax evasion. A possible reason for the gap in the criminal case law could be evidentiary challenges as the burden of proof in criminal proceedings is that of beyond a reasonable doubt and is a far higher bar to meet than in civil proceedings. Another possible explanation could be that this is a symptom of the significant failures in governance at SARS from 2014 to 2019. It should again be noted that the concept of business rescue and its accompanying provisions have only been in effect for the last decade and that the period of troubles at SARS overlap with a substantial portion thereof. Over approximately half a decade SARS experienced operational challenges as a result the "reckless mismanagement" thereof and failures of governance and integrity during the period 2014 to 2019.[217] As noted by Nugent J in his report to the President, the effects of these failures may only become apparent in later years.[218] In light of the above, it is submitted that business rescue could be used as a vehicle for tax evasion and *prima facie* is being used as a vehicle for tax evasion.

This mini-dissertation also makes recommendations which, if implemented, could minimise the room for abuse of the business rescue process as a vehicle for tax evasion. Attention is also given to the BRP and the limitations of oversight and accountability of the Practitioners. Recommendations in this regard have been made which falls in line with other professions and national legislative controls and accountability. Business Rescue as a concept will remain a positive vehicle to rescue companies from termination and avoid the negative impact of the accompanying job losses and loss of the collection of future taxes from the company. Closing the gaps for persons to use the legislation for tax evasion should therefore be considered as it

[217]J Nugent 'Final Report: Commission of inquiry into Tax Administration and Governance at SARS' (2018) paras 3-7 available at http://www.thepresidency.gov.za/report-type/commission-inquiry-tax-administration-and-governance-sars.

[218]J Nugent 'Final Report: Commission of inquiry into Tax Administration and Governance at SARS'.

will have a negative impact on the purpose of the legislation and the fiscus, and is not in the spirit that it was intended.

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