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THE VIABILITY OF BUSINESS RESCUE PROCEEDINGS FOR SMALL TO MEDIUM ENTERPRISES

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By

TSHEPO MTIMKULU

Prepared under the supervision of

Dr JS van Wyk

Faculty of Law, University of Pretoria

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ABSTRACT

In 1996, South Africa became a constitutional democracy where the Constitution, rather than Parliament, governs the rule of law. Amongst many commitments of the constitutional dispensation were the eradication of poverty and inequality, socio-economic empowerment and the realization of human rights for everyone particularly, the rights to dignity, equality and freedom. The above-mentioned rights could be achieved where the economic resources of the Republic are enjoyed by everyone without fear, favour or prejudice. In South Africa, SMEs play a crucial role in the economy by employing most skilled and unskilled workers. By employing many workers, SMEs contribute the majority of the Republic' s public purse. However, the survival of SMEs has been a huge challenge over the years since most of them are under-capitalized, are family businesses and are historically excluded from mainstream financial resources. Traditionally, under the previous regime, financially distressed companies, including SMEs, could be revived through judicial management. The Companies Act 71 of 2008 replaced judicial management with business rescue which also is designed to resuscitate financially distressed companies rather than liquidate these entities. Whether the incumbent legal framework is effective for the survival of SMEs and preserving them as going concern has been a subject of debate. This paper investigates the viability of the business rescue legal framework in South Africa, with the focus on SMEs. The paper questions whether much has or is being done to prevent SMEs from going under and preserving their role as a backbone of the South African economy.

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List of abbreviations

ASGISA	Accelerated Shared Growth Initiative for South Africa
CIGA	Corporate Insolvency and Governance Act
CSBP	Centre for Small Business Promotion
CSSICDR	Committee to strengthen Singapore as an International Centre for Debt Restructuring
ILRC	Insolvency Law Review Committee
LRA	Labour Relations Act
SEDA	Small Enterprise Development Agency
SMEs	Small to Medium Enterprises
SOA	Scheme of arrangement
UNCITRAL	United Nations Commission On International Law

CHAPTER 1: INTRODUCTION

1.1. Introduction

South Africa has recently underwent turbulent socio-economic challenges which have resulted in a surge of massive unemployment, poverty and continuing inequality.[1] The Covid-19 pandemic illustrated the lack of preparedness by the country in dealing with global disasters.[2] Moreover, the lack of effective and adequate procedural mechanisms to deal with financially distressed companies, particularly small and medium business enterprises (SMEs) may have exacerbated the continuing rise of job insecurities.[3] Many SMEs are continually forced to wind up when they can be resurrected through effective mechanisms in order to curb the rising socio-economic challenges.[4]

In South Africa, a company under financial distress generally has two alternatives other than winding-up.[5] On the one hand, a company may choose to enter into a compromise with its creditors,[6] and on the other, resort to business rescue proceedings.[7] Section 128 of the Companies Act 71 of 2008,[8] provides that a business rescue proceeding is a temporary management and supervision of a company's affairs.[9] This includes the management of a company's creditors, the implementation of a rescue plan, the

[1] Herbst "A Practical Guide to Business Rescue for Small Business Owners" 2023 *MoneyWeb*.
[2] Scott and Jewel "Covid-19: Life Insurance Industry prepared for the unprepared" 2020 *Risk* 29.
[3] Maphiri "The Suitability of South Africa's Business Rescue Procedure in the Reorganization of Small-to-Medium-Sized Enterprises: Lessons from Chapter 11 of the United States Bankruptcy Code" 2018 *Mich. Bus. & Entrepreneurial L. Rev.* 101 at 102.
[4] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev.* 102.
[5] Sharrock *et al Hockly's Insolvency Law* (2017) 275; Burke-Le Roux and Pretorius "Exploring Entrepreneurial Learning During Formal Business Rescue Processes: Insights from the South African Experience" 2017 SA *Journal of Human Resource Management* 1 at 1; Naidoo, Patel and Padia "Business Rescue Practices in South Africa: An Explorative View" 2018 *Journal of Economic and Financial Sciences* 1 at 1.
[6] A compromise is regulated in terms of section 155 of the Companies Act.
[7] Sharrock *et al Hockly's Insolvency Law* 275; Rajaram, Singh and Sewpersadh "Business Rescue: Adapt or Die" (2018) 21 *South African Journal of Economic and Management Sciences* 1 at 3.
[8] Companies Act 71 of 2008.
[9] Section 128 of the Companies Act 71 of 2008; Matenda *et al* "South African Business Rescue Regime: Systematic Review Highlighting Shortcomings, Recommendations and Avenues for Future Research" 2023 *Research in Business & Social Science* 100 at 101.

restructuring of the company and the supervision of all financial affairs of the company, including properties, liabilities and asserts.[10]

This research will show that adequate, effective and specific business rescue procedures for small and medium business enterprises may be valuable in alleviating the continuing socio-economic challenges such as unemployment in South Africa.[11] Many unskilled workers who are employed by SMEs continue to lose their job securities when these companies are wound up.[12] This research intends to show that there is a need for special rehabilitative rules designed to resuscitate SMEs instead of applying the existing rules which may be unsuitable. The study will also determine whether the South African business rescue legal framework complies with the internationally accepted World Bank: Principles for Effective Insolvency and Creditor/Debtor Regimes (2015).

1.2. Problem statement and research aims

In *Koen v Wedgewood Village Golf and Country Estate (Pty) Ltd*[13] the court said:

> "It is clear that the legislature has recognised that the liquidation of companies more frequently than not occasions significant collateral damage, both economically and socially, with attendant destruction of wealth and livelihoods. It is obvious that it is in the public interest that the incidence of such adverse socio-economic consequences should be avoided where reasonably possible. Business rescue is intended to serve that public interest by providing a remedy directed at avoiding the deleterious consequences of liquidations in cases in which there is a reasonable prospect of salvaging the business of a company in financial distress."[14]

Business rescue proceedings play a huge role in the survival of South African companies, particularly at a time where the economy appears to be facing huge challenges. In South Africa, SMEs play an invaluable role through the creation of

[10] Section 128 of the Companies Act, Matenda 2023 *Research in Business & Social Science* 101.
[11] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev* 102.
[12] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev* 102.
[13] 2011 ZAWCHC 464.
[14] 2011 ZAWCHC 464 para 14.

employment for many unskilled employees. In *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 Ltd*[15]it was said that the purpose of a business rescue procedure is to rehabilitate companies that are in genuine financial distress rather than those seeking a temporal reprieve from their creditors.[16]

This research will consider business rescue in South Africa, with particular focus on SMEs. As such, this research aims to determine whether there is a need for special rules of rehabilitation as going concerns for SMEs. To do so, it aims to show that SMEs play a crucial role in the overall survival of the South African economy particularly in the preservation of unskilled South African workers. It does so against the background of the general application of ordinary and existing rehabilitation and liquidation rules on SMEs, which tend to create socio-economic risks and stagnation in South Africa.[17]

1.3. Research questions

Against this background, the following research questions are asked:

1. Which legal framework applies to SMEs in financial distress in South Africa? What are the core components of this framework?
2. What is the socio-economic role of SMEs in South Africa and what are the challenges faced by SMEs in South Africa?
3. Which legal framework applies to SMEs in financial distress in Singapore? What are the core components of this framework?
4. When comparing the legal frameworks, and considering the challenges of SMEs, what are the shortcomings of the South African framework and how can this framework be enhanced?

[15] 2012 (2) SA 423 (WCC).
[16] *Engen Petroleum Ltd v Multi Waste (Pty) Ltd & others* 2012 (5) SA 596 (GSJ); *Absa Bank Ltd v Newcity Group (Pty) Ltd, Cohen v Newcity Group (Pty) Ltd & another* [2012] ZAGPJHC 144 (18 August 2012)).
[17] Olawale and Smit "Business environmental influences on the availability of debt to new SMEs in South Africa" 2010 *African Journal of Business Management* 1778 at 1778.

1.4. Research methodology and choice of comparative jurisdiction

The methodology chosen for this study is purely qualitative in nature, desk-top limited and deals primarily with the South African sources of the law including statutory law, common law, and case law. Statutory law will also include regulations and other policy governing business rescue in South Africa. The study further considers journal contributions, textbooks, international and foreign laws and principles.

On a comparative perspective, the study chose the Singapore legal framework was for its progress made with respect to corporate rescue mechanism which commenced with the recommendations of the ILRC[18] and the CSSICDR[19] and culminated to the Act of 2017.[20] In that respect, it will be illustrated, first, that South Africa might learn from the Singapore "cram down" rules. In terms of South African law, "if a business rescue plan has been rejected … the practitioner may … apply to court to set aside the result of the vote by the holders of voting interests … on the grounds that it was inappropriate".[21] This is a stark contrast with the Singapore's approach which clearly gives the court power over the dissenting creditors.[22]

Second, it will be highlighted that the South African legal framework might learn from the Singapore "super-financing" mechanism. Rather than section 135(2) of the Companies Act of 2008, which provides that "[d]uring the business rescue proceedings, the company may obtain financing",[23] the Singapore 2017 Act makes for a "super-priority" finance scheme that may override any existing security interests or rights.[24] This legislative framework in line with the United Nations Commission on International

[18] Insolvency Law Review Committee (ILRC) (2010); Companies Acts 71 of 2008; 61 of 1973 and 46 of 1926.
[19] Committee to strengthen Singapore as an International Centre for Debt Restructuring (CSSICDR).
[20] Companies (Amendment) Act 2017 (hereafter, the 2017 Act).
[21] Section 153(1)(a)(i)-(ii) of the Companies Act.
[22] Section 70(1) (a) -(d) of the IRDA read with Section 211H of the 2017.*Cf* Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 622.
[23] Section 35(2) of the Companies Act. Cf Stoop and Hutchison "Post-Commencement Finance" 16. Calitz and Freebody "Post-Commencement Finance" 265.
[24] Section 211E of the 2017 Act. Cf Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 477; Cf Stoop and Hutchison "Post-Commencement Finance" 16. Calitz and Freebody "Post-Commencement Finance" 265.

Trade Law (UNCITRAL) significantly ensures that the property and other asserts of the company, particularly an SME can remain a going concern for its business operations.[25]

1.5. Limitations of the study

The focus of the research is business rescue in South Africa and how the legal framework applies SMEs. The question is whether the existing legal framework is effective and sustainable for the survival of South African SMEs rather than liquidation. The research will not be discussing other alternatives for financially distressed companies such as the compromise procedure found in section 155 of the Companies Act and formal liquidation proceedings. Moreover, the paper will only discuss judicial management insofar as it provides a historical foundation of business rescue and, as such, only a general overview will be provided.

1.6. Overview of core considerations

1.6.1. The definition of SMEs

The statutory definition of SMEs is significant in the determination whether these entities are entitled to benefits of business rescue under Chapter 6 of the Companies Act 71 of 2008. However, on a conceptual basis, SMEs may be defined as being inextricably linked to the owner, although not always only "one-man business",[26] but also other forms of business entities that are

> "[s]eparate and distinct business entity, including cooperative enterprises and non-governmental organisations, managed by owner or more which including its branches or subsidiaries if any is predominantly carried on in any sector or sub-sector of the economy mentioned in column 1 of the Schedule…"[27]

In South African law, although the concept of an SME is not exactly defined as it may change over time, there is nevertheless agreement that its definition might be affected

[25] Chuanzhong "A Critical Evaluation of the New Cram-down" 270.
[26] Boraine and Van Wyk "Various Aspects to Consider with Regard to Special Insolvency Rules for Small and Medium-Sized Enterprises in South Africa" 2015 *Int. Insolv. Rev* 243.
[27] National Small Business Act 102 of 1996.

by legislation.[28]This means that legislation may dictate the nature, the type and the number of creditors required or a certain number of employees in order for a juristic or non-juristic entity to qualify as an SME.[29] On that respect, it is generally agreed in South African law that whether the entity is a natural or a juristic person, in order for it to qualify as an SME, there must be a direct link between the business of the entity and the owner.[30] Further, with regard to the number of employees, it is generally agreed that a medium enterprise might have approximately 200 fulltime employees, 50 for a small enterprise; 20 for a very small enterprise and; 5 for a micro enterprise.[31]

1.6.2. The purpose of business rescue proceedings

Section 7(k) of the Companies Act provides that the purposes of the Act include to "provide for efficient rescue and recovery of financially distressed companies, in a manner that balances the rights and interests of all relevant stakeholders".[32] Section 128 of the Companies Act defines business rescue as a temporary management and supervision of a company's affairs.

In the *Swart v Beagles Run Investments* and *Southern Palace Investments v Midnight Storm Investments* cases, the courts determined that the business rescue procedure is intended to achieve better returns for creditors or shareholders.[33] However, prior to the business rescue, the court said, it must be proven that there are sufficient resources in the enterprise to benefit the shareholders.[34]

In *AG Petzetakis International Holdings v Petzetakis Africa*[35] and *Gormley v West City Precinct Properties*[36]the courts expressed doubt as to whether recourse may be had to

[28] Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 240-241.
[29] Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 241.
[30] Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 243.
[31] Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 245.
[32] Section 7(k) of the Companies Act.
[33] *Swart v Beagles Run Investments 25 (Pty) Ltd (Four Creditors intervening)*; *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 Ltd* (2012(2) SA 423 (WCC).
[34] See also *Koen & another v Wedgewood Village Golf & Country Estate (Pty) Ltd & others* 2012 (2) SA 378 (WCC); *Oakdene Square Properties (Pty) Ltd & others v Farm Bothasfontein (Kyalami) (Pty) Ltd*; *Farm Bothasfontein (Kyalami) (Pty) Ltd v Kyalami Events and Exhibitions (Pty) Ltd* 2012 (3) SA 273 (GSJ).
[35] *AG Petzetakis International Holdings Ltd v Petzetakis Africa (Pty) Ltd & others (Marley Pipe Systems (Pty) Ltd & another intervening*) 2012 (5) SA 515 (GSJ).

business rescue where the only aim was to secure better returns for shareholders and creditors.[37] The courts reiterated that the purpose of business rescue is to rehabilitate companies in need of restructuring in order to continue being economically productive.[38]

Loubser, however, seemingly doubts the effectiveness of business rescue as compared to liquidation in all instances.[39] The author argues that most companies that undergo business rescue have little chance of ever becoming solvent again.[40] The author argues that liquidation in such circumstances is a better alternative in order to avoid unnecessary costs and time.[41]

1.6.3. Financial distress

The main purpose of a business rescue is to rehabilitate a financially distressed company so that it may return as a going concern.[42] In that respect, the anticipation is that a business rescue practitioner will propose an actionable plan for the rescuing of the company.[43]Generally, a company is financially distressed if "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".[44] Moreover, a company is considered financially distressed if "it appears to be reasonably likely that the company will become insolvent within the immediately ensuing six months".[45]In this respect, where there is a genuine intention to rehabilitate a company, a court will prefer a

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[36] *Gormley v West City Precinct Properties (Pty) Ltd & another, Anglo Irish Bank Corporation Ltd v West City Precinct Properties (Pty) Ltd & another* [2012] ZAWCHC 33 (18 April 2012).
[37] *AG Petzetakis International Holdings Ltd v Petzetakis Africa (Pty) Ltd & others (Marley Pipe Systems (Pty) Ltd & another intervening*) 2012 (5) SA 515 (GSJ) para 11; *Gormley v West City Precinct Properties (Pty) Ltd & another, Anglo Irish Bank Corporation Ltd v West City Precinct Properties (Pty) Ltd & another* [2012] ZAWCHC 33 (18 April 2012) para 6.
[38] *AG Petzetakis International Holdings Ltd v Petzetakis Africa (Pty) Ltd & others (Marley Pipe Systems (Pty) Ltd & another intervening*) 2012 (5) SA 515 (GSJ) para 11; *Gormley v West City Precinct Properties (Pty) Ltd & another, Anglo Irish Bank Corporation Ltd v West City Precinct Properties (Pty) Ltd & another* [2012] ZAWCHC 33 (18 April 2012) para 6. Cf *Oakdene Square Properties (Pty) Ltd & others v Farm Bothasfontein (Kyalami) (Pty) Ltd*; *Farm Bothasfontein (Kyalami) (Pty) Ltd v Kyalami Events and Exhibitions (Pty) Ltd* 2012 (3) SA 273 (GSJ) para 22.
[39] Loubser A 2013 *S.A. Merc. L.J* 456-457.
[40] Loubser A 2013 *S.A. Merc. L.J* 456-457.
[41] Loubser 2013 *SA Merc LJ* 456-457.
[42] Sharrock *et al Hockly's Insolvency Law* 276.
[43] Sharrock *et al Hockly's Insolvency Law* 276.
[44] Section 128(1)(f) of the Companies Act.
[45] Section 128(1)(f) of the Companies Act.

business rescue procedure more than the wounding up of the company.[46]In that regard, the court in *Mvulane Holdings (Pty) Ltd v The Business Rescue Practitioner of De Beers Consolidated Mines (Pty) Ltd*,[47] refused to grant an order for business rescue after noting that the company was not financially distressed as it had the capacity to meet its debts as they became due.[48] Where however, there is a genuine interest to rehabilitate the company, three fundamental aspects must be present – temporary supervision, a temporary *moratorium* on claims by creditors and a business rescue plan.[49]

1.6.4. Voluntary business rescue

The directors of a company may through a resolution decide to place the company under business rescue.[50] In order to do so, the board must have "reasonable grounds to believe that the company is financially distressed";[51] and that "there appears to be a reasonable prospect of rescuing the company".[52] A voluntary business rescue procedure may not be had if the company is already undergoing sequestration.[53] After five days of filing the resolution, the directors of a company must file notice to every affected person wherein they state their reasons for a business procedure.[54] Moreover, the company must appoint a business rescue practitioner with the requisite skill and experience and who must accept the appointment in writing.[55] Once a business rescue resolution has been adopted, the company may not adopt another resolution to commence liquidation proceedings.[56]

[46] Sharrock *et al Hockly's Insolvency Law* 276; *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments* 386 Ltd (2012 (2) SA 423 (WCC).
[47] *Mvulane Holdings (Pty) Ltd v The Business Rescue Practitioner of De Beers Consolidated Mines (Pty) Ltd* (1117/2019) [2020] ZAFSHC 67 (30 March 2020).
[48] *Mvulane Holdings (Pty) Ltd v The Business Rescue Practitioner of De Beers Consolidated Mines (Pty) Ltd* (1117/2019) [2020] ZAFSHC 67 (30 March 2020)
[49] Sharrock*et al Hockly's Insolvency Law* 277.
[50] Sharrock*et al Hockly's Insolvency Law* 277.
[51] Section 129(1)(a) of the Companies Act.
[52] Section 129(1)(b) of the Companies Act.
[53] Section 129(2)(a) of the Companies Act.
[54] Section 129(3)(a) of the Companies Act.
[55] Section 129(3)(b) of the Companies Act.
[56] Section 129(6) of the Companies Act.

1.6.5. Compulsory business rescue

Any affected person may, at any time apply to the court for an order to place the company under business rescue.[57] As compared to voluntary surrender, this application may be made even after liquidation proceedings have commenced.[58] However, an application for compulsory business rescue may not be made to court where the company has already adopted a resolution commencing with the voluntary rescue procedure.[59] An applicant for a compulsory business rescue must notify and serve a copy to the Commission, the company and other affected persons.[60] This application has the effect of suspending any liquidation proceedings against the company until the business rescue fails or is terminated by the court.[61] The court may put the company in business rescue if it is satisfied that the company is financially distressed; or the company has failed to pay its employment or contractual debts; or the court has justifiable financial reasons; and there is a reasonable prospect for rescuing the company.[62]

1.6.6. Consequences of business rescue

A company in financial distress that has accessed the procedure, and its creditors are subjected to several restrictions. Among the many effects of business rescue are that all legal proceedings against the company, including sureties by or on behalf of the company may not be enforced during the proceedings.[63] The company may however, deal with any of its properties during the business rescue if such dealings are: within the ordinary business of the company; the company will receive a fair value and; the

[57] Section 131(1) of the Companies Act.
[58] Section 131(6) of the Companies Act; *Van Niekerk v Seriso 321 CC & another* [2012] ZAWCHC 63 (20 March 2012).
[59] Section 131(1) of the Companies Act.
[60] Section 131(2)(a)-(b) of the Companies Act.
[61] Section 131(6) of the Companies Act. See also *Maroos v GCC Electrical Engineering Pty Ltd* [2017] ZAGPPHC 297 and *ABSA Bank Ltd v Summer Lodge (Pty) Ltd* (63188/2012, 63189/2012, 63190/2012) [2013] ZAGPPHC 544 (23 May 2013) wherein the courts expressed different opinions as to whether a business rescue application suspends a liquidation process.
[62] Section 131(4) of the Companies Act.
[63] Sharrock *et al Hockly's Insolvency Law* 280; section 133 (1) and (2) of the Companies Act.

transaction is in terms of the business rescue.[64] The employment contracts of employees must remain on the same terms and conditions prior to the business rescue and any retrenchments must be in terms of the Labour Relations Act 66 of 1995.[65] Besides employment contracts and those contracts where section 35A of the Insolvency Act apply, all other contracts of the company under business rescue may become suspended at the discretion of the practitioner.[66] After the suspension of the contracts, the other party may rely of contractual damages.[67]

1.6.7. A brief overview of challenges faced by SMEs in the business rescue legal framework

The definition of "financial distress" in terms of the Companies Act, it is said, may not be suitable for SMEs and their chances of survival.[68]The Companies Act limits the definition of financial distress to a company's debt repayment or solvency capacity to only six ensuing months before an intervention may be had.[69] This limitation may not be entirely suitable for SMEs given that most SMEs face financial troubles within the first year of incorporation.[70] Peteni notes the following:

> "The requirement for satisfying the court is strict for SMEs, and places a burden for SMEs in distress, for the court must not simply be satisfied that the SME is financially distressed but should also be satisfied of the reasonable prospect of rescuing the SME. The general vulnerability of SMEs makes court access on its own a burdensome process because business rescue proceedings by court application are accompanied by their own inherent high court costs which places a burden on SMEs".[71]

[64] Sharrock, van der Linde and Smith, *Hockly's Insolvency Law* 281; section 134 (1)(a) of the Companies Act.
[65] Sharrock *et al Hockly's Insolvency Law* 282; section 136 (1)(a) and (b) of the Companies Act.
[66] Section 136(2)(a) of the Companies Act.
[67] Section 136 (3) of the Companies Act.
[68] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev* 113.
[69] Section 128(1)(f) of the Companies Act.
[70] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev* 113.
[71] Peteni *An Analysis of the Application of South African Business Rescue Provisions on Small to Medium Enterprises (SMEs)* (2021, LLM dissertation, University of Fort Hare) 49.

One of the reasons for the early financial distress for SMEs is that, most of them are family business which are financed by meagre family capital.[72] As such, if the definition of financial distress could be extended and designed specifically to target SMEs, most of them would be resuscitated earlier prior to eventual collapse.[73]It is submitted the six months interval required in order for business rescue to be had may perhaps be removed insofar as SMEs are concerned.[74]

The Companies Act may require that SMEs may be able to apply for business rescue proceedings at the earliest sign of financial or other economic distress.[75] Moreover, it is submitted that the use of "reasonable prospect of rescuing the company" as a requirement for business rescue in terms of the Companies Act limits the chances of SMEs accessing business rescue procedures.[76] If the Companies Act could rather incorporate the phrases "possibility" or "probability", more SMEs would find that business rescue provides for a flexible and accessible process.[77]

Moreover, the Companies Act provides that a business rescue practitioner may be elected from good standing members of the legal, accounting, or business management profession.[78] Indications are that this limitation may result in many SMEs not being able to access business rescue proceedings resulting in their collapse. Suggestions are that for an effective business rescue mechanism, perhaps any person with recognized skill and expertise, particularly with the operation of SMEs must be eligible to be a practitioner.[79] Moreover, since the Companies Act provides that a practitioner may delegate their duties, they may work together with an SME recognized expert.[80]

Another challenge associated with business rescue practitioners is the discretionary powers bestowed on these professionals and their affordability when it comes to the

[72] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev* 107.
[73] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev* 113.
[74] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev* 114.
[75] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev* 114.
[76] Section 129(1)(b) of the Companies Act; Le Roux and Duncan "The Naked Truth: Creditor Understanding of Business Rescue: A Small Business Perspective" 2013 *SAJESBM* 57 at 59.
[77] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev* 115.
[78] Section 138(1) of the Companies Act.
[79] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev* 116.
[80] Naidoo, Patel and Padia 2018 *Journal of Economic and Financial Sciences* 3.

need for expert intervention.[81] Indications are that the wide powers given to practitioners may not be entirely suitable for the survival of SMEs, particularly given that a majority of SMEs are family businesses.[82] Requiring a third party in the form of a practitioner to take over such business may not be economically viable and may reduce their chances of survival.[83]

Moreover, there have been indications that many SMEs collapse because of lack of sufficient financial resources to pay for business practitioner services.[84] As such, suggestions are that perhaps there should be subsidies or other financial alternatives designed to cushion SMEs from exorbitant business practitioner fees.[85] This is exacerbated by the fact that SMEs by virtue of their nature, are historically excluded from the mainstream funding mechanisms in South Africa.[86]

According to Boraine and Van Wyk,[87] amongst the many changes that may be introduced in small to medium-sized rescue proceedings are expedited proceedings, alternative workable procedures, commencements proceedings, informal procedures and remedies.[88] Others areas that are in need of reform include the treatment of asserts as well as restructuring issues.[89] The authors argue that, for business rescue procedures to be fully effective, there need be caution against those small enterprises who genuinely need assistance and those who do not.[90] It is those enterprises who disturb the survival chances of genuine business enterprises that have a role to play in the economy. The authors also argue that small to medium business enterprises that are operating as sole proprietors are more likely to be refused those legal remedies that are reserved for juristic persons.[91] Normally these sole proprietors such as business

[81] Suggestions are that the ordinary tariffs charged by business rescue practitioners may not be suitable for a majority of South African SMEs resulting in many of them opting for leaving their small businesses to die naturally in times of financial distress.
[82] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev* 116.
[83] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev* 117.
[84] Peteni *South African Business Rescue* 51.
[85] Peteni *South African Business Rescue* 51.
[86] Peteni *South African Business Rescue* 52.
[87] Boraine and Van Wyk 2015 *Int. Insolv. Rev* 228-246.
[88] Boraine and Van Wyk 2015 *Int. Insolv. Rev* 235.
[89] Boraine and Van Wyk 2015 *Int. Insolv. Rev* 235.
[90] Boraine and Van Wyk 2015 *Int. Insolv. Rev* 238.
[91] Boraine and Van Wyk 2016 *Int. Insolv. Rev* 238.

operated directly by the owner are not regarded as juristic persons and therefore lack the legal capacity to act in certain ways when they encounter financial distress.[92]

It is submitted that, in order for SMEs to continue adding value to the South African economy, a dual business rescue system may be adopted.[93] The size of the SME, their annual turnover, and the number of employees should determine whether a company is regarded under formal or informal business procedures.[94] The dual system may be effective in alleviating cost difficulties and formalities particularly for small enterprises. Moreover, suggestions are that perhaps an informal and less procedural business rescue procedure should be developed for SMEs.[95] Such a procedure may resemble the section 155 compromise between SMEs and their creditors albeit, with specifically designed rules and compulsory regulation for both SMEs and their creditors.[96]

1.6.8. The Ministry of Small Business development

In South Africa, like in other jurisdictions, the need to preserve SMEs as going concerns is not a new phenomenon.[97] This is exemplified by the creation of the Ministry of Small Business Development – tasked with overseeing the sustenance of SMEs with an initial investment of R6.5 billion – in 2014.[98] Underscoring the creation of the Ministry was the realisation that, of the approximately six million SMEs that were operational, 67 percent served as the only means of income for the SME owners.[99] The Department of Small Business Development (DSBD) was subsequently established in 2014 with the mandate to ensure the development and sustenance of small businesses in South Africa in order

> "[t]o lead and coordinate an integrated approach to the promotion and development of entrepreneurship, Small, Micro and Medium enterprises (SMMEs) and C-operatives, and to

[92] Boraine and Van Wyk 2016 *Int. Insolv. Rev* 238.
[93] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev* 130.
[94] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev* 130.
[95] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev* 130.
[96] Maphiri 2018 *Mich. Bus. & Entrepreneurial L. Rev* 130.
[97] Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 231.
[98] Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 231.
[99] Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 231.

ensure an enabling legislative and policy environment to support their growth and sustainability".[100]

This may be achieved through "the coordination, integration and mobilisation of efforts and resources towards the creation of an enabling environment for the growth and sustainability of small businesses and co-operatives".[101]It is submitted that the establishment of the Ministry of Small Business Development, among other bodies, created to oversee and promote the survival of South African SMEs is one of the major landmarks promulgated in South Africa.[102]

1.6.9. The World Bank Principles on Insolvency

The World Bank's Principles for Effective Insolvency and Creditor/Debtor Regimes recognises the need for effective debtor/creditor rights and insolvency systems for international financial stability.[103] Developed in 2001, the principles designed to create an international benchmark for domestic debtor/creditor systems in order to counteract international financial disasters.[104] The domestic assessment of debtor/creditor systems is also vital in the provision of assistance to member states by the World Bank. Moreover, compliance with international standards helps promotes economic growth, commerce and investments for member states.[105] The principles are, moreover, designed to be flexible and to accommodate the cultural, economic, legal, and social context of all member states.[106]

The principles provide that where a business enterprise is viable, rehabilitation should be preferred than liquidation.[107] The underlying question is whether the business is more likely to benefit the creditors as a going concern or wounded up.[108] The principles also take into cognizance the importance of preserving viable business entities in order

[100] https://www.dsbd.gov.za (Date assessed: 29 March 24).
[101] https://www.dsbd.gov.za (Date assessed: 29 March 24).
[102] https://www.dsbd.gov.za (Date assessed: 29 March 24).
[103] World Bank: Principles for Effective Insolvency and Creditor/Debtor Regimes (2015) 1.
[104] World Bank: Principles for Effective Insolvency and Creditor/Debtor Regimes (2015) 1.
[105] World Bank: Principles for Effective Insolvency and Creditor/Debtor Regimes (2015) 2.
[106] World Bank: Principles for Effective Insolvency and Creditor/Debtor Regimes (2015) 2.
[107] World Bank: Principles for Effective Insolvency and Creditor/Debtor Regimes (2015) 8.
[108] World Bank: Principles for Effective Insolvency and Creditor/Debtor Regimes (2015) 8.

to preserve job opportunities for employees.[109] The principles provide that rehabilitation should have both formal and informal procedures and should be procedurally accessible. Moreover, the rehabilitation process must have stringent regulatory framework in order to avoid abuse of the system.[110] Furthermore, rehabilitation must ensure a fair balance of the rights of all stakeholders including creditors, debtors and other affected persons.[111] The following aims must be kept in mind when dealing with domestic insolvency matters:[112]

i. Achieving maximum "value of a firm's assets and recoveries by creditors".

ii. "Provid[ing] for the efficient liquidation of both nonviable businesses and businesses whose liquidation is likely to produce a greater return to creditors and reorganization of viable businesses".

iii. Achieving a "balance between liquidation and reorganization, allowing for easy conversion of proceedings from one procedure to another".

iv. "Provid[ing] for equitable treatment of similarly situated creditors, including similarly situated foreign and domestic creditors".

v. "Provid[ing] for timely, efficient, and impartial resolution of insolvencies".

vi. "Prevent[ing] the improper use of the insolvency system".

vii. "Prevent[ing] the premature dismemberment of a debtor's assets by individual creditors seeking quick judgments".

viii. "Provid[ing] for a transparent procedure that contains, and consistently applies, clear risk allocation rules and incentives for gathering and dispensing information".

[109] World Bank: Principles for Effective Insolvency and Creditor/Debtor Regimes (2015) 8.
[110] World Bank: Principles for Effective Insolvency and Creditor/Debtor Regimes (2015) 8.
[111] World Bank: Principles for Effective Insolvency and Creditor/Debtor Regimes (2015) 8.
[112] World Bank: Principles for Effective Insolvency and Creditor/Debtor Regimes (2015) 15.

1.8. Significance of the study

It has been highlighted that business rescue is one effective method of maintaining and preserving the economic viability without having to liquidate the company. First and foremost, it goes without saying, that the survival of a company far outweighs its ending, particularly in South Africa where there is high unemployment. As such, the survival and rehabilitation of a company goes a long way in maintaining the families of the people who are employed especially in small to medium enterprise. National interest, through employment and government interest, and international developments – both briefly referred to above – indicate that this is a contemporary research topic. The study therefore focuses on what may be done to improve business rescue proceedings particularly for small to medium enterprises.

1.9. Structure of the dissertation

Chapter 1 provides background information of business rescue in South Africa through detailing the problem statement, the hypothesis, research questions, research objectives.

Chapter 2 discusses the legal South African legal framework in the regulation of business rescue with particular focus of SMEs. This chapter provides a historical development of business rescue prior and after the Constitution of the Republic of South Africa, 1996.

Chapter 3 discusses the role of SMEs and their contribution to the socio-economic survival in South Africa. Moreover, the chapter discusses challenges faced by SMEs in the current business rescue legal framework in South Africa.

Chapter 4 discusses the legal framework of business rescue in Singapore.

Chapter 5 deals with the comparative overview of the South African and Singapore's legal frameworks and concludes the study by providing recommendations for reform.

CHAPTER 2: THE SOUTH AFRICAN LEGAL FRAMEWORK

2.1. Introduction

In the previous chapter, it was highlighted that an effective business rescue framework for SMEs in South Africa may alleviate socio-economic challenges such as unemployment, poverty and inequality. Levenstein[113] observes:

> "The challenge for corporate South Africa will be to ensure that there is a change in mindset on the part of the industry from a 'liquidation culture' to one of rather saving companies with the resultant retention of jobs, businesses remaining in operation and a maximisation of returns for creditors."

Unskilled South African workers employed by SMEs continue to endure job insecurity when companies are wound up due to financial challenges.[114]Although their working conditions may undergo some changes, the process of business rescue proved to less traumatic than the psychological effects of losing one's income .[115] In *Employees Solar Spectrum Trading83 (Pty) Ltd v AFGRI Operations Ltd*,[116]an *obiter* remark was made that there must be a balancing exercise undertaken when considering the labour rights of the employees and the company's interests in the business rescue process.[117]Liquidation not only affects the employees themselves, but also their families, suppliers, and the wider community.[118]

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[113] Levenstein "The New Companies Act: Business Rescue Now an Option" 2010 *Management Today* 6, 8. See also Maphiri "Business Rescue Procedure" 102. See Jombe and Pretorius "Direct and Indirect Impact of Business Rescue on Employment" 2022 *Journal of Contemporary Management* 1, 2; Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 230; Olawale and Smit "Business Environmental Influences" 1778.

[114] Maphiri "Business Rescue Procedure" 102; Jombe and Pretorius "Direct and Indirect Impact of Business Rescue" 4.

[115] Jombe and Pretorius "Direct and Indirect Impact of Business Rescue" 24.

[116] *Employees Solar Spectrum Trading83 (Pty) Ltd v AFGRI Operations Ltd, In re; AFGRI Operations Limited vSolar Spectrum Trading 83 (Pty) Ltd*(6418/2011, 18624/2011, 66226/2011, 66226A/2011) 2012 ZAGPPHC 359 (16 May 2012) para 11.

[117] See *Khosa v Minister of Social Development; Mahlaule v Minister of Social Development* 2004 (6) SA 505 (CC) para 46, where the court emphasized the rights of the employers to their salaries and other benefits during the business rescue proceedings. See, however, *Marques v Group Five Construction (Pty) Ltd* 2020 ILJ 677 (LC) para 3, where the court held that the mere non-payment of the salaries of the employees was not sufficient to find an urgent application. Marumoagae and Phiri "Potential Constitutional Concerns Regarding Employees' Rights During Business Rescue Proceedings" 2021 *Stell*

Generally, the debate regarding the need for an effective, targeted and specific-orientated business rescue legal framework in South Africa has existed for quite some time.[119] The modern and advanced Anglo-American legal systems such as the United States, the United Kingdom and Australia, have been instrumental in fuelling the debate.[120]

This chapter lays the foundation for the question as to whether the South African business rescue framework has any targeted and effective mechanisms designed for financially distressed companies that are categorised as SMEs.[121] The focus is on financial rehabilitation, meaning the return to a going concern, as opposed to liquidation. This requires a brief understanding of the historical disposition of business rescue procedures in the pre- and post-Constitutional contexts in South African law, and an analysis of the present dispensation.

In providing a historical context of the business rescue legal framework, the study will discuss the practice of judicial management under the Companies Act 46 of 1926[122] and the Companies Act 61 of 1973.[123] It will be advanced that, notwithstanding its benevolence, judicial management was less successful owing, among others, to its inherent deficits and its prioritisation of the "creditor" as opposed to the resuscitation of the "business".[124]The study will further discuss the current business rescue framework in terms of the Companies Act. It will be advanced that the current legal framework

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LR 496, 506 argue that the court probably erred when it failed to consider the importance of the employees' right to social security during the process of business rescue.

[118] Jombe and Pretorius "Direct and Indirect Impact of Business Rescue" 24; Loubser "Judicial Management as a Business Rescue Procedure in South African Corporate Law (2004) *SA Merc LJ* 137, 137; Zvobgo "A Comparative Study into the Effectiveness of Business Rescue Strategies in South Africa and the Judicial Management System in Zimbabwe" (Unpublished LLM mini-dissertation: University of Pretoria, 2016) 3; Van Zyl "Business Rescue Proceedings in South Africa: Some Concerns from the Perspectives of Creditors" (Unpublished LLM mini-dissertation: University of Johannesburg, 2018) 5-6.

[119] Levenstein "Business Rescue Now an Option" 8.

[120] Levenstein "Business Rescue Now an Option" 6; Loubser "Judicial Management as a Business Rescue" 137; Burke-Le Roux and Pretorius "Business Rescue Processes" 1.

[121] Loubser "The Business Rescue Proceedings in the Companies Act: Concerns and Questions (Part 1)" 2010 *TSAR* 501-514 at 514; Jombe and Pretorius "Direct and Indirect Impact of Business Rescue" 4.

[122] Companies Act 46 of 1926. Hereafter the 1926 Act.

[123] Companies Act 61 of 1973. Hereafter the 1973 Act.

[124] Loubser "Effective Corporate Rescue Procedure" 438.

allows for commencement through the actions of any "interested person" including the directors of the company, the shareholders, employees, and a trade union.[125]

2.2. Judicial management

Judicial management was traditionally established for the purpose of assuming management or supervision over a financially failing company in order to resuscitate it.[126]Henning[127] observed that

> "[t]he purpose of judicial management is to enable a company suffering a temporary setback due to mismanagement or other special circumstances, to once more become a successful concern. The existing management is altered by replacing the board of directors with a court appointed judicial manager who proceeds to run the company's business under the supervision of the Master of the Supreme Court."[128]

The introduction of judicial management appears to have been driven by the need to align the South African corporate rescue framework with global practices.[129] In that vein, Maphiri observed that the retention of judicial management from 1926 until the promulgation of the Companies Act 71 of 2008,[130]may have been targeted at aligning the legal framework with other modern legal systems, particularly English law.[131] However, the exact historical foundations of the practice of judicial management in South Africa have remained uncertain.[132] To that extent, Loubser argues that, although the English Companies Act of 1908[133] contains no clear example of judicial

[125] See section 129 and 131 of the Companies Act; *The Business Rescue Practitioner of Sea Harvest Group Limited v The Commissioner of the South African Revenue Service* (1377/2018) [2019] ZAFSHC 84 (17 September 2019).
[126] Peteni "South African Business Rescue Provisions" 28. See also *Lief v Western Credit (Africa) Pty Ltd* 1966 (3) SA 344 (W).
[127] Henning "Judicial Management and Corporate Rescue in South Africa" 1992 *Tydskrif vir Regswetenskap* 91-106.
[128] Henning "Judicial Management and Corporate Rescue" 92.
[129] Loubser "Judicial Management as a Business Rescue" 140. See also Maphiri "Business Rescue Procedure" 102; *Le Roux Hotel Management (Pty) Ltd v E Rand (Pty) Ltd* [2001] 1 All SA 223 (C) at 238; Joubert "'Reasonable Possibility" Versus "Reasonable Prospect": Did Business Rescue Succeed in Creating a Better Test than Judicial Management?" 2013 *THRHR* 550, 550; Naidoo Patel and Padia "Business Rescue Practices" 1.
[130] Companies Act 71 of 2008. Hereafter the Companies Act.
[131] See Maphiri "Business Rescue Procedure" 109.
[132] See Maphiri "Business Rescue Procedure" 109.
[133] English Companies Act of 1908.

management, it may nevertheless had been the English law traditional practice of the appointment of a "receiver and manager" over the affairs of a financially ailing entities that inspired judicial management in English law and subsequently in South African law.[134]In that vein, Kloppers[135] averred that

> "South Africa shares a long commercial relationship with England, and it is beyond doubt that English law has had an important influence on South African law especially in the field of company law. Consequently, English law also influenced the South African law regarding the liquidation of companies".[136]

2.2.1. The Companies Act 46 of 1926

Judicial management was first introduced into the South African company law through the Companies Act of 1926as a means to manage and rescue financially distraught companies.[137]There was a need to manage businesses with the potential to return to a profitable state.[138]However, from its inception, the practice did not receive substantive support but was viewed as an alien doctrine likely to be a financial burden on the State.[139] The general culture of the time appears to have been that companies unable to be financially independent and sustainable were to die a natural death.[140] More so, a company that had proven to be financially incapacitated would have most likely lost the confidence of the public as well as its creditworthiness, factors that would have minimised its chances for full recovery irrespective of the availability of a rescue mechanism.[141]

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[134] See Loubser "Judicial Management as a Business Rescue" 139; Maphiri "Business Rescue Procedure" 108.
[135] Kloppers "Judicial Management - A Corporate Rescue Mechanism in Need of Reform?" 1999 *Stell LR* 417. See also Kloppers "Judicial Management Reform – Steps to Initiate a Business Rescue" 2001 *SA Merc LJ* 358.
[136] Kloppers "Judicial Management" 418.
[137] Phungula *The Evolution of an Effective Business Rescue Statutory Regime in South Africa 1926-2021* (unpublished LLD Thesis, University of KwaZulu Natal, 2021) at 3.
[138] Phungula *Evolution of Effective Business Rescue* 4.
[139] Phungula *Evolution of Effective Business Rescue* 5.
[140] Phungula *Evolution of Effective Business Rescue* 5.
[141] Henning "Judicial Management and Corporate Rescue" 92.

2.2.2. The Companies Act 61 of 1973

The Companies Act of 1973subsumed in its entirety the practice of judicial management. Section 427 of the 1973 Act provided:

> "(1) When a company by reason of mismanagement or for any other cause-
>
> (a) is unable to pay its debts or is probably unable to meet its obligations; and
>
> (b) has not become or is prevented from becoming a successful concern,
>
> and there is reasonable probability that, if it is placed under judicial management, it will be enabled to pay its debts or to meet its obligations and become a successful concern, the Court may, if it appears just and equitable, grant a judicial management order in respect of that company."

From this section, it is clear that judicial management in terms of the Companies Act of 1973 only applied to companies as defined by the Companies Act.[142]To this end, Loubser[143] argued that this limitation may have been profoundly prejudicial to non-company entities (as well as SMEs).[144]

Furthermore, section 427(1) read with section 432 of the Companies Act of 1973 underscored that, in order for a company to have been successfully placed under judicial management, there must had been a "reasonable probability"[145] that it would return to a successful concern.[146] Section 432 specifically related to a return day where a court, prior to making a final order, would had considered, among others,: the views of creditors and other company members; the provisional report of the judicial manager;

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[142] Section 1 of the Companies Act of 1973 defines a company as one which is incorporated under the Act or a company that existed immediately prior to the Act. See also Kloppers "Judicial Management" 418.
[143] Loubser "Judicial Management as a Business Rescue" 142. See also section 1 and 2 of the Companies Act of 1973.
[144] Own emphasis. See also Maphiri "Business Rescue Procedure" 109.
[145] See *Noordkaap Lewendhawe Ko-operasie Bpk v Schreuder* 1974 (3) SA 102 (A) at 110, where the court emphasized that the difference between "probable" and "possible" is material in that the latter relates to something that is less sure to happen. See also Joubert "Reasonable Possibility" 552.
[146] Section 427 (1) and section 432 of the Companies Act of 1973. See also *Noordkaap Lewendehawe Ko-op Bpk v Schreuder* 1974 (3) SA 102 (A) at 110; Henning "Judicial Management and Corporate Rescue" 92.

whether all claims had been proved; and the reports of the Master and the Registrar of the Court.[147]

This indicates that the judicial management procedure fundamentally sought to protect substantial investments and creditors' claims through a closely monitored management procedure.[148] The creditor-orientated approach was depicted in the rigorous "reasonable probability" test that creditors were to be able to recoup a greater part of their investments in the process.[149]

In *Kotze v Tulryk Bpk*,[150] the court indicated that an order placing the company in provisional judicial management was not adopted as an experimental procedure without a "reasonable probability" that the company would return as a successful concern.[151] Regarding the "just and equitable" threshold, as per section 427(1) of the Companies Act of 1973, an order for judicial management may only have been made in highly exceptional circumstances after a consideration of the need of creditors to receive a return on their investments.[152]

The South African courts bemoaned the "just and equitable" threshold in the Act.[153]In that vein, it was suggested that the threshold that a company must have been "unable" to meet its obligations in terms of section 427 (1)(a) and (b) of the Companies Act of 1973 may have be superfluous, particularly when the resuscitation of non-company entities like SMEs were under consideration.[154] This is so because it may have been uneasy to fathom the possibility of a company including an SME that is not able to honour its obligations in terms of (a) may then become a successful concern in terms of (b).[155]

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[147] Section 432 of the Companies Act of 1973.
[148] Maphiri "Business Rescue Procedure" 109.
[149] Maphiri "Business Rescue Procedure" 109.
[150] *Kotze v Tulryk Bpk*1977 (3) SA 118 (T).
[151] *Kotze v Tulryk Bpk*1977 (3) SA 118 (T) at 120. See also *Tenowitz v Tenny Investments (Pty) Ltd* 1979 (2) SA 680 (E) at 683.
[152] *Kotze v Tulryk Bpk*1977 (3) SA 118 (T) at 120. See also Loubser "Judicial Management as a Business Rescue" 147; Maphiri "Business Rescue Procedure" 109.
[153] Peteni "South African Business Rescue Provisions" 31.
[154] See Loubser "Judicial Management as a Business Rescue" 143; section 427 (1)(a) and (b).
[155] Loubser "Judicial Management as a Business Rescue" 144.

Levenstein[156] argued that judicial management was not always practicable:

> "Legal practitioners and liquidators have accepted the fact that judicial management does not work in the South African scenario. Quite simple, judicial management was a precursor for liquidation proceedings. The reason for this was clearly that there was no obligation on the part of creditors or financiers to be placed in a position where they would be bound to a judicial management process by way of a court order."

In that regard, it was argued that the reason for the failure of judicial management was probably the rigorous application of the Companies Act of 1926 brought over to the era under the Companies Act of 1973.[157]This is so because precedence and legislative mechanisms that prevailed during the Companies Act of 1926 may not have been focused on rehabilitation– more on winding-up of financially distressed companies.[158]The legislative provisions pertaining to judicial management were interpreted through the lens of winding-up, and judicial management was seen as an extraordinary measure.[159]Furthermore, it has been advanced that the traditional practice of appointing liquidators as judicial managers directly contributed to the demise of judicial management.[160] This is so because, whilst the task of judicial managers was to preserve a company as a going concern, that of liquidators was to discontinue it in an orderly manner.[161]

Section 427(2) provided the following:

> "An application to court for a judicial management order in respect of any company may be made by any of the persons who are entitled under section 346 to make an application to court for the winding-up of a company, and the provisions of section 346(4)(a) as to the application for winding-up shall mutatis mutandis apply in an application for a judicial management order".[162]

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[156] Levenstein "Business Rescue Now an Option" 6.
[157] Loubser "Judicial Management as a Business Rescue" 162.
[158] Loubser "Judicial Management as a Business Rescue" 162.
[159] Kloppers "Judicial Management" 424. See also Olver "Judicial Management- A Case for Law Reform" 1986 *THRHR* 84, 84-86.
[160] Kloppers "Judicial Management" 424. See also Olver "Judicial Management" 84-86.
[161] Kloppers "Judicial Management" 424. See also Olver "Judicial Management" 84-86.
[162] Section 1 and 2 of the Companies Act of 1973.

The section implied that the application for judicial management could be made by the company itself; any of its directors; its creditors; its members; or all of the above jointly.[163] Loubser noted that, in order for the directors of a company to avoid personal liability for company losses, they would have to exercise their discretion to apply for judicial management timeously.[164] Section 12(1) provided that the High Court had jurisdiction to hear the application.[165] Discussed elsewhere,[166] the threshold providing jurisdiction only to High Courts is very onerous on SMEs and many of them would not have been able to afford the costs associated with High Court litigation.[167]

Prior to the submission of the application to the court, a copy thereof must have been submitted to the office of the Master of the High Court in that jurisdiction.[168] Moreover, where there was a simultaneous application for winding-up, the court may have preferred liquidation where there was a reasonable belief that the conditions for judicial management would lapse.[169] Kloppers also expressed the same sentiment in that the demise of judicial management in South Africa may have been because it was not considered autonomous, but was inextricably intertwined with liquidation.[170] As indicated above, the improper appointment of liquidators as opposed to judicial managers *per se* was not amenable to the process of resuscitation of financially failing companies.[171]Also, notwithstanding that the directors of a company may have preferred business rescue over liquidation, the latter would nevertheless have prevailed where investigations revealed a lower probability of the resuscitation of the company.[172] Kloppers further argued that the traditional practice where a provisional judicial manager

[163] Section 427(2) of the Companies Act of 1973.
[164] Loubser "Judicial Management as a Business Rescue" 151. See also *Ex parte Graaff-Reinet Rollermeule (Edms) Bpk* 2000 (4) SA 670 (E).
[165] Section 12(1) of the Companies Act of 1973.
[166] See the Chapter on the Role and Challenges faced by South African SMEs.
[167] Maphiri "Business Rescue Procedure" 109; Kloppers "Judicial Management" 426.
[168] Section 427(2) read with s 346(4)(a) of the of Companies Act of 1973.
[169] Section 427(3) of the Companies Act of 1973.
[170] Kloppers "Judicial Management" 424. See also Olver "Judicial Management" 84-86.
[171] Kloppers "Judicial Management" 424. See also Olver "Judicial Management" 84-86.
[172] Kloppers "Judicial Management" 425. See also Olver "Judicial Management" 84-86.

would have applied to be appointed a final liquidator would have resulted in an anomalous conflict of interest.[173]

2.3. Business rescue

The Companies Act of 2008 was introduced in 2009 but only became operational in 2011.[174] The Act introduced a new legal framework aimed at the resuscitation of financially distressed companies with a focus on preserving them as going concerns.[175]The Companies Act was a result of the efforts of the Department of Trade and Industry to reform corporate laws.[176] The framework allows for financially distressed companies to undergo business rescue proceedings on the basis of volition or an order of the court.[177]The business rescue procedure must either restore the company to a going concern or be likely to obtain better returns for the creditors and shareholders of the company as compared to wounding up.[178]

Rushworth observes that the new legal framework represents a radical departure from the old judicial management procedure under the Companies Act of 1973.[179]On the other hand, the 180-degree transition from the creditor-friendly approach in the previous Acts to the debtor-friendly disposition in the Companies Act may present some challenges.[180]

2.3.1. Commencement by the directors of the Company

The business rescue procedure may be commenced by any interested person including the directors of the company, the shareholders, employees, and a trade union.[181]Unlike

[173] Kloppers "Judicial Management" 425. See also Olver "Judicial Management" 84-86.
[174] Burke-Le Roux and Pretorius "Business Rescue Processes" 1.
[175] Rushworth "Business Rescue Regime" 375.
[176] Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 233.
[177] Rushworth "Business Rescue Regime" 375.
[178] Section 128(1)(b) of the Companies Act. See also Rushworth "Business Rescue Regime" 376; Loubser "The Business Rescue Proceedings (Part 1)" 502.
[179] Rushworth "A Critical Analysis of the Business Rescue Regime in the Companies Act 71 of 2008" (2010) *Acta Juridica* 375, 408.
[180] Rajaram, Singh and Sewpersadh "Business Rescue: Adapt or Die" (2018) *South African Journal of Economic and Management Sciences* 1, 3.
[181] Section 129 and 131 of the Companies Act; *The Business Rescue Practitioner of Sea Harvest Group Limited v The Commissioner of the South African Revenue Service* (1377/2018) [2019] ZAFSHC 84 (17

in winding-up, the decision to place the company in business rescue only requires the decision of the board of directors.[182] It is important that the directors must believe that the company is financially distressed and that there are reasonable chances of it being rescued.[183] Financial distress entails that the company will not able to pay its debt as they become due in the next six months and that the company will become insolvent within the immediate ensuing six months.[184]In *Mvulane Holdings (Pty) Ltd v The Business Rescue Practitioner of De Beers Consolidated Mines (Pty) Ltd*,[185] the court refused to grant an order for business rescue after noting that the company was not financially distressed as it had the capacity to meet its debts as they became due.[186]

Within five business days of adopting the resolution, the directors must publish a notice directed to any "affected persons" together with the circumstances underlying the application for the business rescue.[187]More so, after adopting a resolution, the directors of the company must notify the Companies and Intellectual Property Commission (CIPC) whilst also submitting a breakdown of the company's financial position.[188]

Should the affected persons opine that the resolution is without merit, they may lodge an application to dismiss it but must provide reasons for doing so.[189] A court may not dismiss the proceedings prior to affording the directors and the business practitioner the opportunity to prove the significance and advantages of the anticipated business rescue procedure.[190] Van Zyl notes that this is one of the ways in which the Companies Act

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September 2019), the court approved the application for business rescue after considering that there was proof that it would result in better returns for shareholders, creditors and the employees of the company.
[182] Section 129(1) of the Companies Act.
[183] Section 129(1) of the Companies Act. See also Loubser "The Business Rescue Proceedings (Part 1)" 502; *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd* 2013 (4) SA 539 (SCA) para 29; *First Rand Limited v Normandie Restaurants Investments* 2016 JDR 2212 (SCA) para 14, where the court held that the determination as to whether the company is reasonably capable of being rescued is a value judgment that may consider both objective and subjective factors.
[184] Section 129(1) of the Companies Act. See also Rushworth "Business Rescue Regime" 377.
[185] *Mvulane Holdings (Pty) Ltd v The Business Rescue Practitioner of De Beers Consolidated Mines (Pty) Ltd* (1117/2019) [2020] ZAFSHC 67 (30 March 2020).
[186] *Mvulane Holdings (Pty) Ltd v The Business Rescue Practitioner of De Beers Consolidated Mines (Pty) Ltd* (1117/2019) [2020] ZAFSHC 67 (30 March 2020)
[187] Section 129(3)(a) of the Companies Act; Loubser "The Business Rescue Proceedings (Part 1)" 501.
[188] Herbst "The Legal Framework for Business Rescue" https://www.moneyweb.co.za (Date assessed: 29 March 2024).
[189] Section 130(1) of the Companies Act.
[190] Section 130(5)(a) and (b) of the Companies Act.

empowers affected persons, particularly the creditors of the company, to be involved in the process of business rescue.[191] In that vein, creditors may either be formally[192] or informally[193] involved in the decision to submit an application to court to place the company in business rescue.[194] As will be highlighted on a comparative perspective, the cram-down procedures in Singapore have undergone considerable modification so as to give the court the final say on a corporate rescue procedure.[195]

Essentially, the application for business rescue means that the directors agree to the temporal management of the entirety of the company's affairs by a qualified business rescue practitioner.[196] More so, the application presupposes the relinquishing of their powers as directors to the business practitioner, including the businesses, the properties and all related matters of the company.[197]

2.3.2. Commencement by a court order

Besides the commencement of business rescue through a resolution taken by the directors of the company, any affected person may apply to court to place the company in business rescue,[198] provided that the process has not already been commenced with by the directors.[199] The affected person must serve a copy of the application on the company, the CIPC, as well as all other affected persons.[200] In order for affected persons to place the company in business rescue, they must allege that the company is financially distressed on the premises of a cash-flow or balance-sheet test; or that it "has failed to pay an amount due in terms of an obligation under or in terms of a public

[191] Van Zyl "Business Rescue Proceedings" 9.
[192] See section 145(1)(c) of the Companies Act.
[193] See section 145(1)(d) of the Companies Act.
[194] Van Zyl "Business Rescue Proceedings" 8-9.
[195] Section 70(1)(a)-(d) of the IRDA. *Cf*Section 211H of the 2017 Act and section 70 of the IRDA Act; Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 622.
[196] Rushworth "Business Rescue Regime" 378. See also Madigoe and Pretorius "Practices Applied by Paractitioners to Achieve Management and Financial Control During Business Rescue" 2022 *Acta Commercii* 1, 2 who argue that the success of a business rescue may fundamentally depend on the managerial capabilities of the business practitioner.
[197] Rushworth "Business Rescue Regime" 378; Loubser "The Business Rescue Proceedings (Part 1)" 501.
[198] Section 131(1) of the Companies Act.
[199] Section 131 (1) of the Companies Act.
[200] Section 131 (2) of the Companies Act.

regulation, or contract, with respect to employment matters; or [that] it is otherwise just and equitable to do so for financial reasons".[201] It must also be shown that "there is a reasonable prospect for rescuing the company" as provided for in section 131(4)(a).

In that regard, it is significant to note that the application by the affected person is more extensive and goes beyond the requirements of mere liquidity.[202] To that extent, it is submitted that this differentiation between the circumstances under which affected persons and directors may apply for business rescue seem to be unfairly anomalous,[203] although directors ought to have more information on the financial state of the company than affected persons.

2.3.3. Opposing a resolution and the termination of the business rescue process

Loubser[204] criticises the ambiguity in section 130(1)(a):

> "It is unclear whether the use of this present tense in phrasing the two grounds for setting aside the resolution ('there is no reasonable...') is merely an example of bad drafting, or was intended to mean that the court may consider the situation of the company at the time of the application, rather than at the time that the resolution was taken."

More so, Loubser argues that this provision may be redundant given that section 141(2)(a) also endows the business practitioner with the power to apply for the termination of the rescue procedure when there is no prospect of rescue.[205] She criticizes the provision for its lack of clarity regarding the meaning of "equitable to do so" in section 141 in that it provides no guide as to the circumstances that would result in the failure of a business rescue plan.[206]

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[201] Section 131(4)(a) of the Companies Act. See also Marumoagae "The Rights of Affected Persons as Stakeholders During Business Rescue Proceedings in South Africa" 2018 *JCCL & P* 117, 126.
[202] Rushworth "Business Rescue Regime" 381.
[203] See Section 131(4)(a) of the Companies Act; Marumoagae "The Rights of Affected Persons" 126; Rushworth "Business Rescue Regime" 381.
[204] Loubser "The Business Rescue Proceedings (Part 1)" 505.
[205] Loubser "The Business Rescue Proceedings (Part 1)" 505; section 141(2)(a) of the Companies Act.
[206] Loubser "The Business Rescue Proceedings (Part 1)" 505.

2.3.4. The moratorium in business rescue

In South African law, as soon as the process of business rescue commences, there is a general moratorium on all the legal proceedings against the company.[207] First, this means that no legal action, including an enforcement action in relation to any property matter including the possession without from the practitioner or a court order.[208] Second, a moratorium applies with respect to any guarantee or suretyship undertake by the company which may not be enforced without an order of the court on the basis of just and equitable circumstances.[209] Third, where any third party has a right against the company that is subject to a time limit, the right is automatically suspended until such a time the rescue process continues.[210] However, the moratorium does not apply amongst others: to criminal proceedings against the company;[211] to proceedings by a regulatory framework;[212] to matters relating to property managed by a company as a trustee and;[213] to proceedings relating to a set-off initiated by the company.[214]

2.3.5. The duties of directors to cooperate with the business practitioner

As soon as the business practitioner has been appointed, the directors of the company must furnish all books and records relating to the company's affairs in their possession to the practitioner.[215] More so, the directors are required to inform the practitioner of any other books or records not in their possession.[216]The directors must provide the practitioner with a substantive statement of the affairs of the company.[217] The statement must represent the company's affairs within the preceding 12 months of the business rescue including arbitration and enforcement proceedings.[218]

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[207] Sharrock *et al Hockly's Insolvency Law* 281.
[208] Section 133(1) (a) -(b) of the Companies Act; Sharrock *et al Hockly's Insolvency Law* 281.
[209] Section 133(2) of the Companies Act; Sharrock *et al Hockly's Insolvency Law* 282.
[210] Section 133(3) of the Companies Act; Sharrock *et al Hockly's Insolvency Law* 282.
[211] Section 133(1)(d) of the Companies Act; Sharrock *et al Hockly's Insolvency Law* 282.
[212] Section 133(1)(f) of the Companies Act; Sharrock *et al Hockly's Insolvency Law* 282.
[213] Section 133(1)(e) of the Companies Act; Sharrock *et al Hockly's Insolvency Law* 282.
[214] Section 133(1)(c) of the Companies Act; Sharrock *et al Hockly's Insolvency Law* 282.
[215] Section 142(1) of the Companies Act.
[216] Section 142(2) of the Companies Act.
[217] Section 143(3) of the Companies Act.
[218] Section 142(3)(b) of the Companies Act.

2.3.6. The business rescue plan

In South African law, in terms of section 153(1)(a),"[i]f a business rescue plan has been rejected … the practitioner may (i) seek a vote of approval from the holders of voting interests to prepare and publish and revised plan; or (ii) … apply to a court to set aside the result of the vote by the holders of voting interests … on the grounds that it was inappropriate".[219]However, in terms of section 152(2), a business rescue plan "will be approved on a preliminary basis if… it was supported by the holders of more than 75% of the creditors' voting interests that were voted; and … the votes in support of the proposed plan included at least 50% of the independent creditors' voting interests, if any, that were voted".[220]

2.3.7. Post-commencement financing

In South African law, section 135(2) of the Act of 2008 provides that,"[d]uring the business rescue proceedings, the company may obtain financing".[221] The Act provides that the financing may be secured to the lender by utilizing any assert of the company to the extent that it is otherwise not encumbered.[222] Stoop and Hutchison consider two consequences of this section in South African law.[223] First, the authors argue that there is no doubt that the post-commencement creditors of the financing rank higher than other creditors.[224] Second, the authors sound concern over the requirement of asserts to which the financing will be secured.[225] It is submitted that this is a huge concern when one considers that many companies, in particular SMEs seldom have any valuable assets after the process of business rescue.[226] It is clear from this section, that South African law does not provide a definite and targeted mechanism for companies in

[219] Section 153(1)(a)(i)-(ii) of the Companies Act...
[220] Section 152(2) of the Companies Act.
[221] Section 35(2) of the Companies Act.
[222] Section 35(2)(a) of the Companies Act.
[223] Stoop and Hutchison "Post-Commencement Finance – Domiciled Resident or Uneasy Foreign Transplant" 2017 *PELJ* 1 at 5.
[224] Stoop and Hutchison "Post-Commencement Finance" 16. See also section 35(2) of the Companies Act; Calitz and Freebody "Is Post-Commencement Finance Proving to be the Thorn in the Side of Business Rescue Proceedings Under the 2008 Companies Act?" 2016 *De Jure* 265 at 272.
[225] Stoop and Hutchison "Post-Commencement Finance" 16; section 35(2) of the Companies Act.
[226] Stoop and Hutchison "Post-Commencement Finance" 16; section 35(2) of the Companies Act.

financial distress, in particular SMEs.[227] Further, it is clear that there are not targeted or effective incentives designed to encourage creditors to be interested in providing finance to companies proceeding from business rescue.[228] As will be highlighted, the South African approach will be put into context when the Singapore's approach, particularly the concept of a "super-priority" finance scheme is discussed.[229] It will be seen that as compared to South African law, a Singapore Court may authorise the debtor to raise more financing provided such financing is necessary to enable the debtor to continue as a going concern.[230]

2.4. Concluding remarks

This chapter sought among others to investigate the historical disposition of the business rescue legal framework in South African law. In that regard, it was established that the need for an effective and targeted legal framework for the resuscitation of financially distressed companies has always been a component of the South African legal framework.[231] The study established that through the process of judicial management in terms of the Companies Act of 1926 and that of the Companies Act of 1973, financially distressed companies were first given a managerial and/or financial reprieve to sustain its survival as a going concern.[232] Essentially, it was established that it may have been the English law custom of appointing a "receiver and manager" over the affairs of a financially distressed companies that may have inspired the development of judicial management in English law and subsequently in South African law.[233]

However, judicial management proved to be less successful for a number of reasons. First, the demise may had been directly because of the lack of embracement of the

[227] Stoop and Hutchison "Post-Commencement Finance" 17; section 35(2) of the Companies Act.
[228] Stoop and Hutchison "Post-Commencement Finance" 16; section 35(2) of the Companies Act.
[229] Section 211E of the 2017 Act. Cf Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 477.
[230] McCormack and Wan "Singapore's Restructuring and Insolvency Laws" 18; Cf Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 477.
[231] Levenstein "Business Rescue Now an Option" 8.
[232] Peteni "South African Business Rescue Provisions" 28. See also *Lief v Western Credit (Africa) Pty Ltd* 1966 (3) SA 344 (W).
[233] See Loubser "Judicial Management as a Business Rescue" 139; Maphiri "Business Rescue Procedure" 108; Kloppers "Judicial Management" 358.

procedure by practitioners and the State.[234] Second, it was argued its inherent shortcomings such as its prioritisation of the creditor as opposed to business resuscitation may had also been the cause of its ultimate demise.[235] Third, the limited application of judicial management in terms of the Companies Act of 1973 in that it only related to companies meant that non-company entities like many South African SMEs did not qualify by default.[236] Fourth, its requirement of "reasonable probability" as a threshold for financial assistance was not sustainable for many entities, particularly SMEs.[237] Fifth, it has been suggested that the traditional South African practice of having liquidators to subsequently act also as judicial managers may have had a direct effect on the low success of judicial management.[238]

In 2011, the Companies Act of 2008 came into effect and replaced the practice of judicial management as a means of resuscitating financially distressed companies. Whilst the underlying main objective of the business rescue procedure is to return the company to a going concern, it also seeks to get more returns for the creditors or shareholders of the company in the alternative and in contrast to immediate formal liquidation.[239]

The Act broadened the circumstances and the people endowed with the power to apply for business rescue to include the board of directors,[240] and any other affected person.[241] A "reasonable prospect" threshold test was introduced but[242] Joubert argues

[234] Loubser "Effective Corporate Rescue Procedure" 438.
[235] See Peteni "South African Business Rescue Provisions" 32; Loubser "Effective Corporate Rescue Procedure" 438.
[236] See section 427 of the 1973 Act; Kloppers "Judicial Management" 418; Loubser "Judicial Management as a Business Rescue" 142.
[237] See section 427(1) read with section 432 of the Companies Act of 1973; Maphiri "Business Rescue Procedure" 109.
[238] Kloppers "Judicial Management" 424. See also Olver "Judicial Management" 84-86.
[239] Joubert "Reasonable Possibility" 554. See also *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd* 2013 (4) SA 539 (SCA); *Swart v Beagles Run Investments 25 (Pty) Ltd* 2011 (5) SA 422 (GNP).
[240] Section 129(1) of the Companies Act.
[241] Section 131(1) of the Companies Act.
[242] Section 129(1) of the Companies Act. See also Section 427 (1) and section 432 of the 1973 Act; Loubser "The Business Rescue Proceedings (Part 1)" 502; *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd* 2013 (4) SA 539 (SCA) para 29; *First Rand Limited v Normandie Restaurants Investments* 2016 JDR 2212 (SCA) para 14, where the court held that the determination that

that the drafters of the Companies Act deliberately ignored the numerous recommendations for the adaptation of the "reasonable possibility" test as opposed to creating a "reasonable prospect" test.[243]

It is therefore clear that although there historically was and remain many challenges, the South African legal framework continually strives to create conditions suitable for the development and resuscitation of financially distressed companies. In the next chapter, the study looks into the role and the challenges faced by SMEs and establishes that the challenges are either "internal" or "external". In that respect, it will be established that whereas "internal" challenges faced by SMEs might relate to their management, control and human resources, "external" challenges relate to the constitution of concepts such as "financial distress", "reasonable prospect" amongst others insofar as they apply to business rescue mechanisms.

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the company may be reasonably rescued is a value judgment that may consider both objective and subjective factors.

[243] See Joubert "Reasonable Possibility" 553. See also section 427(1) of the Companies Act of 1973 and section 129(1) of the Companies Act.

CHAPTER 3: THE SOCIO-ECONOMIC ROLE OF, AND CHALLENGES FACED BY, SMEs IN SOUTH AFRICA

3.1. Introduction

An effective business rescue framework for South African SMEs has the propensity to alleviate employment-related and other socio-economic challenges.[244]SMEs in South Africa are a vital socio-economic engine as, for example, approximately six million SMEs were operational in 2014 with 67 percent constituting the only means of income for the SME owners.[245] Moreover, despite the wider economic impact, the failure of South African SMEs has a profound socio-moral effect on the surge of poverty and the creation of tension in ordinary households.[246]

The psychological effect of liquidation and the resultant job insecurity have been identified as having lasting effects on employees and their families, most likely having a permanent bearing on their working lives.[247] As such, the previous chapter detailed the historical legal framework designed to preserve corporate entities as going concerns as opposed to liquidating businesses in financial distress.

This chapter considers the roles of, and the challenges faced by, South African SMEs as well as the UNCITRAL recommendations on financially distressed SMEs. As mentioned above, in South Africa, SMEs are socio-economic engines responsible for the creation of employment opportunities and the reduction of poverty and inequality.[248]This chapter will argue that, despite the South African government

[244] Levenstein "The New Companies Act" 8. Maphiri "Business Rescue" 102; Jombe and Pretorius "Direct and Indirect Impact of Business Rescue on Employment" 2022 *Journal of Contemporary Management* 1, 2; Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 230.
[245] Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 231.
[246] Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 232. *Cf* Nyamunda "Financing of Small, Medium and Micro Enterprises (SMMEs) An Assessment of SADC DFIs" 2009 *Africa Growth Agenda* 6, 6.
[247] Jombe and Pretorius "Direct and Indirect Impact of Business Rescue" 10-11; Bushe "The Causes and Impact of Business Failure Among Small to Micro and Medium Enterprises in South Africa" 2019 *Africa's Public Service Delivery and Performance Review* 1, 4.
[248] Enwereji "Navigating the Hurdles: The Internal and External Challenges of Small, Medium and Micro Enterprises (SMMEs) in South Africa" 2023 *African Journal of Development Studies* 227, 228; Tala "South Africa's Lending Infrastructure: Does it Facilitate or Constrain Access to Credit Finance by Small and Medium Enterprises (SMEs)?" 2021 *Journal of Public Administration* 276, 276-277.

introducing a number of mechanisms directed toward assisting "financially distressed" businesses,[249] the legal framework nevertheless falls short of rescuing the majority of struggling SMEs.[250] More so, besides the wider socio-economic role played by SMEs in local South African communities, SMEs are also important in filing the gaps neglected by the national government.[251]

Fundamentally, the chapter will show that challenges faced by SMEs are divided into "internal" and "external" challenges.[252] Internal challenges include management, control and human resources structures, tax issues,[253] and matters related to corporate ethics; whereas external challenges relate to, among others, shortfalls in the business rescue framework, political and funding issues.[254] The next paragraphs discuss the socio-economic role of SMEs in South Africa as well as the challenges which they encounter.

3.2. The socio-economic role of South African SMEs

The scourge of unemployment has been one of the many challenges faced in the post-constitutional South African dispensation.[255]Data collected for the first part of 2024 shows that the unemployment rate stands at 45,5 percent among the ages of 15-34 years, with 32.9 percent being the national average.[256]Against the backdrop of these statistics, the increasing gap between the experienced and unexperienced young South Africans has prompted the South African government to commit to increasing learnership programmes and apprenticeships among the South African young

[249] The Small Enterprise Development Agency (SEDA) (2018); the National Small Business Act 106 of 1996; the Centre for Small Business Promotion (CSBP); the Umsobomvu Youth Fund (National Youth Development Agency) (2001), created to provide finance to SMEs run by the South African young people and the Accelerated Shared Growth Initiative for South Africa (ASGISA) (2006).
[250] Ferreira, Strydom and, Nieuwenhuizen "The Process of Business Assistance to Small and Medium Enterprises in South Africa: Preliminary Findings" 2010 *Journal of Contemporary Management* 94, 96.
[251] Hasseno, Tefera and Taylor "The Funding Model of Small and Medium Social Enterprises in KwaZulu-Natal, South Africa" 2024 *Southern African Journal of Entrepreneurship and Small Business Management* 1, 1.
[252] Enwereji "The Internal and External Challenges SMMEs" 232; Olawale and Smit "Business Environmental Influences" 1778-1780.
[253] Mukumba and Hoek "The Taxing Business of Rescuing SMMEs: Key Tax Considerations During Business Rescue" (2022) *Tax Business Rescue* 14, 14-17, on the challenges faced by business rescue practitioners in complying with tax-related matters.
[254] Enwereji "The Internal and External Challenges SMMEs" 232; Olawale and Smit "Business Environmental Influences" 1778-1780.
[255] Olawale and Smit "Business Environmental Influences" 1778.
[256] https://www.statssa.gov.za (Date accessed: 15 June 2024).

people.[257] Also, directly related to unemployment in South Africa, is the resulting challenge of poverty and inequality.[258] In that vein, the advancement, promotion and sustenance of SMEs in South Africa identify as some of the means to directly counter the rising challenge of poverty and inequality through the provision of a means of income for ordinary households.[259]

For Broembsen,[260] "chronic poverty is a descriptor for poverty that reflects a state of pervasive, unrelenting disempowerment and socio-economic vulnerability and marginality".[261] The author argues that a general change of narrative from focusing on "business rescue" to one focused on the "person" may be instrumental in the resuscitation of financially distressed SMEs.[262] This change of attitude, Broembsen argues, is significant in that it puts into perspective the practical socio-economic ramifications that result from the lack of effective SME revival mechanisms, particularly for the vulnerable amongst the society.[263]He also argues that, with the incumbent legal framework, it is doubtful whether SMEs will provide sufficient employment opportunities to meet the expected thresholds and, further, that many SMEs lack the potential to graduate to fully-fletched entities.[264]

In a similar vein, Neneh and Vanzyl[265] argue that the "growth" of SMEs in South Africa is very significant to counter the scourge of unemployment.[266] However, due to socio-economic and other hazards, many SMEs are stuck in "survival mode" without any potential to grow beyond the communal zone where they were established.[267] Saah

[257] https://www.statssa.gov.za(Date accessed: 15 June 2024); Saah "Small and Medium-Sized Enterprises on the Economic Development of South Africa" 2021 *Technium Social Sciences Journal* 549, 549.
[258] Olawale and Smit "Business Environmental Influences" 1778; Saah "Small and Medium-Sized Enterprises" 550.
[259] Olawale and Smit "Business Environmental Influences" 1778; Bushe "The Causes and Impact of Business Failure" 1.
[260] Broembsen "Informal business and poverty in South Africa: Re-thinking the paradigm" 2010 *Law, Democracy & Development* 1.
[261] Broembsen "Informal business and poverty" 2.
[262] Broembsen "Informal business and poverty" 3.
[263] Broembsen "Informal business and poverty" 3.
[264] Broembsen "Informal business and poverty" 13.
[265] Neneh and Vanzyl "Growth Intention and Its Impact on Business Growth amongst SMEs in South Africa" 2014 *Mediterranean Journal of Social Sciences* 172.
[266] Neneh and Vanzyl "Growth Intention and Its Impact" 173.
[267] Neneh and Vanzyl "Growth Intention and Its Impact" 173.

goes as far as to argue that the stagnation of SMEs in South has led to the spiralling rate of inflation and the decline of the South African Rand against international currencies such as the US Dollar and the British Pound, resulting in a spike of the cost of living.[268]

The South African government could direct its political power and focus on SMEs in order to reconfigure the distribution of economic resources, with the disadvantaged masses in mind.[269] Whilst this endeavour has the potential to create economic stability, attract foreign investments and encourage competitive business practices, it may also alleviate the scourge of violent crime and service delivery issues.[270] More so, a targeted and effective legal framework and other mechanisms designed to counter the low success rate of SMEs show promise when it comes to the preservation of countries' gross domestic product (GDP) and general economic growth.[271] Furthermore, because SMEs inherently cultivate indigenous skills development and promote work-related experience, their development and sustenance has the potential to counter the scourge of rural-urban migration in South Africa.[272]

3.3. General challenges faced by South African SMEs

Despite South Africa being identified as an economically-progressive country,[273] the growth and sustenance of SMEs generally appear to be lacking with indications that, of the new SMEs established within the Republic, the majority collapse within the first two years.[274] General insolvency-related challenges are not the only reason for failed businesses – the failure of South African SMEs appears to be premised on both "internal" and "external" factors.[275] On the one hand, funding issues, structural matters, internal deficiencies, lack of proper financial records and management irregularities account for "internal" factors and, on the other hand, the general economic challenges,

[268] Saah "Small and Medium-Sized Enterprises" 550.
[269] Peteni "South African Business Rescue Provisions" 18.
[270] Peteni "South African Business Rescue Provisions" 18-19.
[271] Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 230.
[272] Saah "Small and Medium-Sized Enterprises" 551.
[273] Tala "South Africa's Lending Infrastructure" 277.
[274] Olawale and Smit "Business Environmental Influences" 1778.
[275] Olawale and Smit "Business Environmental Influences" 1780.

inefficient regulatory frameworks, crime, corruption and ethical issues, on the other hand, account for the "external" challenges faced by SMEs.[276] In the following paragraphs, the study discusses first, the non-insolvency and then followed by the insolvency-related challenges faced by South African financially-distressed entities, with particular focus on SMEs.

Many South African SMEs generally do not have access to venture capital as a means of external financing, thus requiring the majority of them to rely on self-funding or on banks for loans and overdraft facilities as means of financial assistance.[277] This means that if SMEs do not have access to the business rescue process, they do not have access to the structured post-commencement finance options of the business rescue process.[278] According to Mbhele,[279] "venture capital" denotes private as opposed to public funding; and this form of funding capitalises on competent and competitive management for purposes of investment.[280] Also, whilst internal funding such as personal savings, borrowing from friends and relatives is premised on trust, external funding fundamentally relies on empirical merit.[281]

The inaccessibility of mainstream financial assistance seems to be premised on the fact that most SMEs generally fail to meet the formal and procedural thresholds stipulated by financial service providers.[282] The inaccessibility of bank financing for South African SMEs is as a result of many SMEs not having adequate internal and other records to evidence their financial performance such as profits and losses statements.[283] For

[276] Olawale and Smit "Business Environmental Influences" 1780.
[277] Olawale and Smit "Business Environmental Influences" 1779; Peteni "South African Business Rescue Provisions" 21; Tala "South Africa's Lending Infrastructure" 279.
[278] Ramnanum, Pillay and Rajaram "Evaluating Sources and Forms of Post-Commencement Business Rescue Finance in KwaZulu-Natal, South Arica" 2020 *Academy of Accounting and Financial Studies Journal* 1,1.
[279] Mbhele "The Study of Venture Capital Finance and Investment Behavior in Small and Medium Enterprises" 2012 *South African Journal of Economic and Management Sciences* 94.
[280] Mbhele "The Study of Venture Capital Finance and Investment" 95.
[281] Tala "South Africa's Lending Infrastructure" 280.
[282] Olawale and Smit "Business Environmental Influences" 1779.
[283] Olawale and Smit "Business Environmental Influences" 1780.

transparency purposes, financial service providers require proof of substantive financial statements and other records prior to furnishing financial assistance.[284]

Most South African SMEs fail to meet their business targets imposed by credit providers – including initiating adequate marketing, training, accessing legal services, and other growth-related opportunities.[285] More so, notwithstanding the failure by SMEs to meet the "financial record" lending criteria, most SMEs also fall short of the "property collateral" criteria by virtue of not having adequate property as security for financing purposes.[286]

The general categorisation of "natural" and "juristic" persons for purposes of loan facilities from South African banks is problematic given that SMEs can be natural or juristic persons.[287] This challenge is also evidenced in situations where the sole proprietors of SMEs are denied funding facilities by virtue of having been previously sequestrated or undergoing debt review procedures.[288]

As most South African SMEs are established and managed by their founders as directors or shareholders, or any other legal capacity, ethical lines become blurred.[289] Research has shown that the collapse of many SMEs result from the lack of values of honesty, trust, respect and fairness – all which are ethical values crucial for the survival of any business as a going concern.[290] Whilst the managing of an SME as a family concern has its economic advantages, it is equally important that ethical and professional requirements are adhered to in order to separate and identify the boundaries between business and individual.[291] Peteni raises similar sentiments in that, by virtue of being managed as family extensions, many SMEs collapse as a direct result

[284] Tala "South Africa's Lending Infrastructure" 280.
[285] Enwereji "The Internal and External Challenges SMMEs" 236; Tala "South Africa's Lending Infrastructure" 280.
[286] Tala "South Africa's Lending Infrastructure" 281. The author also argues that by virtue of their disposition, many SMEs do not qualify to the "credit-score" lending criteria which utilises past credit tendencies in determining the capacity of the debtor to honor their debt obligations.
[287] Boraine and Van Wyk "Small and Medium-Sized Enterprises (2)" 20.
[288] Boraine and Van Wyk "Small and Medium-Sized Enterprises (2)" 20.
[289] Olawale and Smit "Business Environmental Influences" 1781.
[290] Olawale and Smit "Business Environmental Influences" 1781.
[291] Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 236-7.

of the flouting of fundamental corporate governance principles and the lack of separation between the personal, moral and professional aspects of the concern.[292]

Further "internal" challenges leading to the low success rate of SMEs in South Africa include inadequate management, financial, human resources and internal control mechanisms within the SMEs.[293]Often than not, the lack of effective management and finance structures result in SMEs battling to keep up with supply and demand.[294] Financial illiteracy, inadequate financial planning, poor marketing strategies and the lack of skill and training also identifies, among others, as factors linked to the demise of SMEs in South Africa.[295]

3.4. Insolvency-related challenges

3.4.1. Overview

Boraine and Van Wyk argue that, owing to their nature and their role in the economic stabilisation of the country, the legal framework for business rescue in South Africa ought to be designed to specifically target the resuscitation of financially distressed but viable SMEs.[296] For the authors, before the choice of either the liquidation or the rescuing of financially distressed SMEs is exercised, it is important that two preliminary assessments are made.

Firstly, it must be determined what exactly an "SME" entails – to ensure that resources are directed towards rescuing only SMEs as opposed to family businesses seeking temporal reprieve.[297] Secondly, it is important that the reasons for the failure of an SME be considered – in order to direct resources towards those entities with a good chance of survival as opposed to dysfunctional business concerns.[298] In the same line, it has

[292] Peteni "South African Business Rescue Provisions" 22.
[293] Enwereji "The Internal and External Challenges SMMEs" 233; Bushe "The Causes and Impact of Business Failure" 12.
[294] Enwereji "The Internal and External Challenges SMMEs" 233; Bushe "The Causes and Impact of Business Failure" 12.
[295] Enwereji "The Internal and External Challenges SMMEs" 233; Tala "South Africa's Lending Infrastructure" 282.
[296] Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 236.
[297] Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 238.
[298] Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 238.

been suggested that, because financial assistance does not guarantee the success of the SME, it is important that the financial assistance be aligned with the nature of the SME, its business structures, the amount of time needed for the assistance to prove valuable, and the character of the owner, among others.[299]Despite the foregoing, focus must also be on revamping the finance, the marketing and the human resources as three fundamental departments with a direct role in the successful return of the entity as a profitable concern.[300] It is submitted that SME founders, including aspirant SME owners must consider these factors as part of their research initiatives before actually starting their business in order to reduce the incidences of financial distress.[301]

3.4.2. Challenges related to the business rescue process

3.4.2.1. Financial distress

The theory relating to financial distress was discussed earlier. The issues are discussed here. The definition of "financial distress" in terms of the Companies Act may have contributed to the inaccessibility of the financial rescue mechanism to SMEs.[302] The current legal framework considers "financial distress" in the limited ambit of a company's failure to honor its liabilities within the six ensuing months – the process of rescue may only be initiated within six months of commercial or factual insolvency.[303] As was argued above, this threshold is not practical and is evidenced by the substantial number of SMEs which collapse within the first year of incorporation for lack of timeous financial assistance.[304] It is suggested that the definition of "financial distress" should be revised so that it can specifically allow SMEs to seek financial reprieve at the earliest signs of distress without having to rely on the rigid statutory limitations.[305]

Moreover, in light of the fact that the current South African legal framework does not practically differentiate between "financial distress" as a "commercial insolvency test" or

[299] Ferreira, Strydom and, Nieuwenhuizen "The Process of Business Assistance" 107.
[300] Ferreira, Strydom and, Nieuwenhuizen "The Process of Business Assistance" 107.
[301] Ferreira, Strydom and, Nieuwenhuizen "The Process of Business Assistance" 107.
[302] Maphiri "Business Rescue Procedure" 113.
[303] Section 128(1)(f) of the Companies Act.
[304] Maphiri "Business Rescue Procedure" 113.
[305] Maphiri "Business Rescue Procedure" 107.

a "balance sheet test", it is suggested that an approach specifically designed for SMEs would go a long way in the rescue of financially distressed SMEs.[306]

3.4.2.2. Reasonable prospect

Closely related to "financial distress" is the requirement of "reasonable prospect" as a precursor for access to the business rescue process set out in the Companies Act.[307]Du Toit, Pretorius and Rosslyn-Smith[308] aver that, even though "reasonable prospect" does not necessarily equate to "reasonable possibility", it nevertheless requires considerations made on the strength of reliable data as opposed to speculation.[309]

There is no rigid practical threshold for the "reasonable prospect" test and companies, including SMEs, are required to furnish evidence to show the economic viability of the process – from which the court premises its case-by-case discretion.[310] The "reasonable prospect" threshold is a huge challenge for SMEs as opposed to the "possibility" or "probability" of restoring the business to its operational capacity.[311]

Smyth,[312] however, argues that the determination of financial distress is far from being too rigid or mechanical.[313] The author argues that, in order for companies to avoid being ineligible for business rescue on the premise of "financial distress", it is significant that

[306] Jones "Financial Distress – A Precursor to Business Rescue" 2018 *Without Prejudice* 9,9.
[307] See section 129(1)(b) of the Companies Act; *Swart v Beagles Run Investments (Pty) Ltd* 2011 5 SA 422 (GNP); *Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments Ltd* 2012 2 SA 423 (WCC); *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd* 2012 3 SA 273 (GSJ), 2012 2 All SA 433 (GSJ); *Koen v Wedgewood Village Golf and Country Estate (Pty) Ltd* 2011 ZAWCHC 464 para 14; O'Brien and Calitz "A Reasonable Prospect for Rescuing a Company as a Requirement for Business Rescue: a Decade Later" 2021 *TSAR* 688, 689.
[308] Du Toit, Pretorius and, Rosslyn-Smith "Small, Medium and Micro-Enterprises" Distress and Factual Evaluation of Rescue Feasibility" 2019 *Southern African Journal of Entrepreneurship and Small Business Management* 1.
[309] Du Toit, Pretorius and Rosslyn-Smith "Small, Medium and Micro-Enterprises" 3.*Cf* O'Brien and Calitz "A Reasonable Prospect for Rescuing a Company" 696, who aver that the test must be an objective one on the premise of a "reasonable businessperson". See also chapter 2 above on "reasonable prospect v reasonable probability".
[310] Du Toit, Pretorius and, Rosslyn-Smith "Small, Medium and Micro-Enterprises" 4.
[311] Du Toit, Pretorius and, Rosslyn-Smith "Small, Medium and Micro-Enterprises" 5; Maphiri "Business Rescue Procedure" 115. See also See chapter 2 above on "reasonable prospect v reasonable probability".
[312] Smyth "Detecting 'Red Flags' Early Can Help a Business Avoid Severe Financial Distress" 2012 *Professional Accountant* 26.
[313] Smyth "Detecting 'Red Flags" 26.

the business rescue procedure is adopted at the earliest sign of distress as opposed to when nothing is left to resuscitate.[314]

3.4.2.3. Costs associated with the process

According to Bradstreet, Pretorius and Mindlin,[315] the rigid South African formal costs structures is a fundamental challenge faced by SMEs intending to utilise business rescue procedure.[316] The authors argue that the rigid cost structure legal framework is a huge stumbling block on the desired objectives of business rescue and is in need of a fundamental revision.[317] Also, slightly related to the costs of the business rescue, particularly for SMEs, the authors recommend a statutory mechanism that allows business rescue practitioners to be paid in shares rather than in monetary terms.[318] It is argued that this recommendation to compensate practitioners with shares, as argued by the authors helps increase their desire to see that the entity survives by all means.[319]It is argued that this limited jurisdiction in favour of the South African High Courts in matters related to business rescue result in the majority of SMEs not to be able to access or to sustain High Courts costs scales.[320]

3.4.2.4. Conclusion of the process

The Companies Act of 2008 provides that the business rescue practitioner must file a substantial implementation as a "measure" towards the successful resuscitation of a financially distressed entity.[321] Pretorius however, argues that this statutory mechanism is not clear when it comes to the requirements for, and expectations from, rescue practitioners and this is unlikely to enable a successful business rescue procedure.[322]

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[314] Smyth "Detecting 'Red Flags" 26.
[315] Bradstreet, Pretorius and, Mindlin "The Wolf in the Sheep's Clothing- When Debtor-Friendly is Creditor-Friendly: South Africa's Business Rescue and Alternative learned From the United States' Chapter 11" 2015 *Journal of Corporate and Commercial and Commercial Law & Practice* 1.
[316] Bradstreet, Pretorius and, Mindlin "The Wolf in the Sheep's Clothing" 41.
[317] Bradstreet, Pretorius and, Mindlin "The Wolf in the Sheep's Clothing" 41. *Cf* Hasseno, Tefera and, Taylor "The Funding Model of Small" 6.
[318] Bradstreet, Pretorius and, Mindlin "The Wolf in the Sheep's Clothing" 41.
[319] Bradstreet, Pretorius and, Mindlin "The Wolf in the Sheep's Clothing" 41.
[320] Section 12(1) of the 1973 Act.
[321] Chapter 6 of the Companies Act 71 of 2008.
[322] Pretorius "Business Rescue Decision-Making: Post-Mortem Evaluation of an 'Orgy'" 2018 *South African Journal of Economic and Management Sciences* 1,1.

Pretorius further adds that the number of complaints that are lodged against practitioners reveal/ prove the intensity and the urgency need for regulatory guidelines and threshold over business practitioners.[323] In that regard, Pretorius argues that inasmuch as the actual business rescue procedures are on a "case-by-case" basis, it is nonetheless, essential that there is an effective collaboration between the business rescue educators, the regulatory bodies as well as the banks.[324] It is through this collaboration that the stakeholders of business rescue are able to collectively identify any loopholes within the framework and make practical counter-measures and recommendations in that regard.[325]

3.5. The UNCITRAL guidelines on "financially distressed" SMEs

Section 39(2) of the Constitution of the Republic of South Africa, 1996 provides that "when interpreting the Bill of Rights, a court, tribunal or forum- (a) must promote the values that underlie an open and democratic society based on human dignity, equality and freedom; (b) must consider international law; and (c) may consider foreign law". As part of international law, the United Nations Commission on International Trade Law (UNCITRAL) was designed to guide international members states in the creation of a harmonised approach in dealing with financially distressed companies.[326] The purpose of the recommendations is to provide a procedurally and substantively fair and impartial mechanism through financially distressed companies may be resuscitated.[327] What follows are the guidelines established by the UNCITRAL with relation to financially distressed companies.

Article 1[328] provides, as key objectives of a simplified insolvency regime, that

> "States should provide for a simplified insolvency regime and for that purpose consider the following key objectives:

[323] Pretorius "Business Rescue Decision-Making" 2.
[324] Pretorius "Business Rescue Decision-Making" 2.
[325] Pretorius "Business Rescue Decision-Making" 2.
[326] The UNCITRAL Recommendations on SME Insolvency https://uncitral.un.org (Date accessed: 16 June 24).
[327] The UNCITRAL Recommendations on SME Insolvency.
[328] The UNCITRAL Recommendations on SME Insolvency.

(a) Putting in place expeditious, simple, flexible and low-cost insolvency proceedings (henceforth referred to as 'simplified insolvency proceedings').

(b) Making simplified insolvency proceedings available and easily accessible to micro- and small-sized enterprises (MSEs).

(c) Promoting the MSE debtor's fresh start by enabling expedient liquidation of non-viable MSEs and reorganisation of viable MSEs through simplified insolvency proceedings.

(d) Ensuring protection of persons affected by simplified insolvency proceedings, including creditors, employees and other stakeholders (henceforth referred to as 'parties in interest') throughout simplified insolvency proceedings.

(e) Providing effective measures to facilitate participation by creditors and other parties in interest in simplified insolvency proceedings, and to address creditor disengagement.

(f) Implementing an effective sanctions regime to prevent abuse or improper use of the simplified insolvency regime and to impose appropriate penalties for misconduct.

(g) Addressing concerns over stigmatisation because of insolvency; and

(h) Where reorganisation is feasible, preserving employment and investment."

Over and above, in terms of these recommendations, member states are encouraged to ensure that all debts incurred by SMEs are consolidated in a manner that takes account the primary objective of resuscitating the SME,[329] by a specified or independent[330] body or forum.[331] Such a regime must clearly articulate the procedures, time periods and the cost effectiveness of the resuscitation initiatives,[332] as well as circumstances requiring "debtor" or "creditor" involvement.[333] More so, where the SME does not qualify for financial rescue for one or another reason, it must be informed timeously and provided with the reasons thereof and any cost or other consequences of the rejection.[334] Where there is no reasonable prospect of a resuscitation, the simplified regime must

[329] Article 3 of the UNCITRAL Recommendations on SME Insolvency.
[330] Article 8 of the UNCITRAL Recommendations on SME Insolvency.
[331] Article 6 of the UNCITRAL Recommendations on SME Insolvency.
[332] Articles 11, 12 and 13 of the UNCITRAL Recommendations on SME Insolvency.
[333] Articles 17 and 18 of the UNCITRAL Recommendations on SME Insolvency.
[334] Articles 36-39 of the UNCITRAL Recommendations on SME Insolvency.

specifically articulate the circumstances of the decision to convert the process to liquidation and the effects thereof.[335]

3.6. Concluding remarks

This chapter investigated the socio-economic role of SMEs in South Africa; and considered the challenges they face. The study established that SMEs play a vital role in providing employment opportunities to the South African local communities.[336] The study established that the unemployment rate stood at 45,5 percent, affecting mostly young people.[337] It was advanced that unemployment also has the propensity to increase poverty, inequality and tension in ordinary South Africa households.[338]

Broadly, the study established that South African SMEs face challenges such as the unavailability of external funding, structural and management woes, internal financial irregularities and political challenges.[339] The study further established that the current legal framework for distressed SMEs pose challenges as well. For example, "financial distress" and "reasonable prospect" as the thresholds for access to the business rescue process are huge barriers for SMEs seeking financial relief.[340] It was suggested that, in order for the South African SME business rescue framework to be more effective, it is important that the definition of an SMEs be specifically circumscribed and that the financial relief assistance must be considered in line with the nature of the SME, its business structures, the amount of time needed for the assistance, and the character of its founder, among others.[341]

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[335] Article 83 of the UNCITRAL Recommendations on SME Insolvency.
[336] See Enwereji "Navigating the Hurdles" 228; Tala "South Africa's Lending Infrastructure" 276-277; Levenstein "The New Companies Act" 8; Maphiri "Business Rescue" 102; Jombe and Pretorius "Direct and Indirect Impact of Business Rescue on Employment" 2; Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 230.
[337] https://www.statssa.gov.za.
[338] See Olawale and Smit "Business Environmental Influences" 1778; Bushe "The Causes and Impact of Business Failure" 1.
[339] See Olawale and Smit "Business Environmental Influences" 1780.
[340] See Section 128(1)(f) and section 129(1)(b) of the Companies Act.
[341] See Ferreira, Strydom and, Nieuwenhuizen "The Process of Business Assistance" 107; Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 236-238.

Revising the timing related to the "financial distress" requirement or the exemption of SMEs from the formal rules on financial distress may be needed.[342] The study advanced that, whereas "reasonable prospect" in terms of the Companies Act does not necessarily equate to reasonable possibility", it must consider the *ad hoc* nature of SMEs in need of relief on a case-by-case basis.[343]

The study established that, owing to its rigid formalities, the South African legal framework for lending is ordinarily inaccessible a majority of SMEs.[344] In that vein, it was advanced that banks and other private financial institutions must consider other alternatives beside the ordinary "bank records" and "collateral" lending mechanisms when dealing with SMEs.[345]

Further, the study considered the South African business rescue legal framework at the backdrop of the UNCITRAL Model Law which seeks to provide an internationally standardized approach. The study, therefore, advances that the UNCITRAL approach is very broad and flexible from which the South African approach may borrow some guidelines in dealing with financially distressed companies, particularly SMEs. It is argued that in terms of the UNCITRAL Model law, the South African approach may consider the systematic consolidation of SME debt with the fundamental objective of resuscitating the SME.[346] Furthermore, it is argued that having noted that the South African business rescue practitioner legal framework lacks solid guidelines which results in uncertainty and inconsistencies, it is argued, in line with the UNCITRAL, that an independent body or forum created and regulated by the State may alleviate those challenges. Moreover, as per the UNCITRAL guidelines, it is argued that the South African approach may consider to provide clearly articulated business rescue

[342] See Maphiri "Business Rescue Procedure" 107; Jones "Financial Distress – A Precursor to Business Rescue" 9.
[343] See Du Toit, Pretorius and, Rosslyn-Smith "Small, Medium and Micro-Enterprises" 3. See also O'Brien and Calitz "A Reasonable Prospect for Rescuing a Company" 696; Du Toit, Pretorius and, Rosslyn-Smith "Small, Medium and Micro-Enterprises" 4; Du Toit, Pretorius and, Rosslyn-Smith "Small, Medium and Micro-Enterprises" 5; Maphiri 'Business Rescue Procedure' 115.
[344] See Olawale and Smit "Business Environmental Influences" 1779; Peteni "South African Business Rescue Provisions" 21; Tala "South Africa's Lending Infrastructure" 279-280; Mbhele "The Study of Venture Capital Finance" 94-96.
[345] See Olawale and Smit "Business Environmental Influences" 1779-1780; Enwereji "The Internal and External Challenges SMMEs" 236; Tala "South Africa's Lending Infrastructure" 280.
[346] Article 3 of the UNCITRAL Recommendations on SME Insolvency.

procedures; their time periods and the cost effectiveness and; the circumstances that require “debtor” or “creditor” involvement with focus of SMEs Furthermore, it is argued that in line with the UNCITRAL guidelines, the South African legal framework must provide for simplified insolvency proceedings available and easily accessible to SMEs and also by promoting the SME debtor’s fresh start by enabling expedient liquidation of non-viable SMEs and reorganisation of viable SME through simplified insolvency proceedings.

The next chapter will discuss Singapore’s business rescue legal framework and its approach to financially distressed SMEs. The modern streamlining of corporate insolvency laws in Singapore began in 2010 with the recommendations of the Insolvency Law Review Committee (ILRC) and then the Committee to strengthen Singapore as an International Centre for Debt Restructuring (CSSICDR) in 2015 which culminated into the Companies (Amendment) Act of 2017.The UNCITRAL Model Law played a fundamental role in the structuring of Singapore’s business rescue legal framework in order to align it with global developments.

CHAPTER 4: THE BUSINESS RESCUE LEGAL FRAMEWORK IN SINGAPORE

4.1. Introduction

The previous chapters investigated the business rescue framework in South Africa. The study focused on the historical development as well as the modern mechanisms designed to resuscitate financially distressed companies. It was established that an effective business rescue framework for South African SMEs is significant in the alleviation of employment-related and other socio-economic challenges.[347] In that regard, the study established that SMEs in South Africa are a vital socio-economic engine which comprised approximately six million SMEs to have been operational in 2014 with 67 percent being the only means of income for the SME owners.[348] This chapter investigates effectiveness of the legal framework and mechanisms designed to rescue financially distressed companies in Singapore with a particular focus on SMEs. To begin with, Foo[349] describes Singapore as

> "[a] thriving global and regional emporium built on open trade and commerce – this has been the lifeblood of Singapore since its founding. As an international finance, business and trading centre, Singapore is home to a high concentration of multinational corporations, organisations and start-ups. With the rise of international and regional commerce in the past decades, businesses are often organised with regard to economic and fiscal considerations."[350]

As a former colony of England, Singapore's laws on corporate insolvency and the legal frameworks that flow from it are closely related to English law.[351] However, the modern

[347] Levenstein "The New Companies Act" 8. See also Maphiri "Business Rescue" 102; Jombe and Pretorius "Direct and Indirect Impact of Business Rescue on Employment" 2022 *Journal of Contemporary Management* 1, 2; Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 230.
[348] Boraine and Van Wyk "Small and Medium-Sized Enterprises (1)" 231.
[349] Foo "Universalism on the Ascent: Singapore's Cross-Border Insolvency Journey" 2023 *Singapore Academy of Law Journal* 593.
[350] Foo "Universalism on the Ascent" 593.
[351] Seng and Tjio "Singapore as International Debt Restructuring Center: Aspiration and Challenges" 2021 *EW Barker Centre for Law & Business Working Paper* 1, 9; Chen, Azmi and Rahman "Theories of Corporate Insolvency: A philosophical Analysis of the Corporate Rescue Mechanisms Under the Companies ACT 2016" 2021 *UUM Journal of Legal Studies* 167, 168.

streamlining of corporate insolvency laws began in 2010 with the recommendations of the Insolvency Law Review Committee (ILRC).[352] Thereafter, the Committee worked to strengthen Singapore as an International Centre for Debt Restructuring (CSSICDR) in 2015.[353] The recommendations culminated in the Companies (Amendment) Act 2017[354] which seeks to advance the country's corporate insolvency laws in line with global developments and the UNCITRAL guidelines.[355] The 2017 Amendment Act eventually led to the promulgation of the Restructuring and Dissolution Act 2018 (IRDA) which came to effect in 2020.[356] Singapore corporate insolvency law currently provides for five broad regimes: liquidation, judicial management, receivership, a Commonwealth scheme, and a hybrid scheme.[357]

The chapter will show that, whilst the traditional Singapore corporate rescue framework originated from the UK's Scheme of Arrangement around 1870, its modern form is founded in the recommendations of the ILRC, the CSSICDR and UNCITRAL. Whilst the 2017 reforms appear not to have been designed with SMEs in mind, a mandatory moratorium, a statutory mediation procedure, and other financial and tax incentives may encourage SMEs to rely on the available rescue mechanisms. Further, the study will show that the strict "cram-down" procedure has alleviated challenges related to creditor dissent in that the automatic thirty-day moratorium ensures that companies continue as going concerns despite financial distress. More so, it will be advanced that the "super-rescue" financing approach in Singapore is one of the effective and modern ways of handling financial distress, with a particular focus on SMEs.

4.2. The English law foundation of Singapore's insolvency regime

The Scheme of Arrangement (SOA) dispensation was first introduced in the UK around 1870 and was eventually introduced in Singapore.[358] This mechanism allowed a

[352] Insolvency Law Review Committee (ILRC) (2010).
[353] Committee to strengthen Singapore as an International Centre for Debt Restructuring (CSSICDR).
[354] Companies (Amendment) Act 2017 (hereafter, the 2017 Act).
[355] Seng and Tjio "International Debt Restructuring Center" 9.
[356] Insolvency, Restructuring and Dissolution Act 2018.
[357] Seng and Tjio "International Debt Restructuring Center" 10.
[358] Ang "The Race to Rescue: Evaluating the Rollout of Cross-Class Cramdowns in the UK and Singapore" 2023 *Singapore Comparative Law Review* 110, 111.

company undergoing financial distress to utilise rescue procedures whilst management retained control.[359] It will not come as a surprise that the modern corporate rescue legislative reforms in the UK and Singapore occurred within a month of each other.[360] Also, it will not be a coincidence that the frameworks of the UK and Singapore have similar references to "schemes of arrangement" although, in Singapore, the phrase is mostly associated with insolvency and related procedures.[361] The influence of English law however, began to decrease when Singapore regained its autonomy in 1962, culminating in its independence in 1965.[362]After independence, English law continued to have a huge impact on commercial matters, but Singapore began to consider developments in other jurisdictions such as the US and Canadian law.[363]

4.3. Singapore corporate rescue mechanisms and SMEs

There are strong arguments that the legal framework in Singapore was not designed to effectively resuscitate financially distressed SMEs, particularly in nationwide emergencies such as the Covid-19 pandemic.[364] This is because the mainstream legal framework is too formal and expensive to accommodate the specialised needs of SMEs.[365] Nevertheless, this chapter considers a number of suggestions essential for the survival of financially distressed SMEs in Singapore and South Africa.

First, it is essential that the Singapore government considers pre-emergency rescue procedures specifically designed to rescue SMEs.[366] The pre-emergency procedures include, amongst others, automatic statutory moratoriums against all legal actions against potential SMEs.[367] The moratorium must be able to operate outside the confines

[359] Ang "The Race to Rescue" 111.
[360] The UK's Corporate Insolvency and Governance Act 2020 (CIGA 2020) and the Singapore's Insolvency, Restructuring and Dissolution Act 2018 (IRDA 2018) both came into operation in 2020. *Cf* Ang "The Race to Rescue" 110.
[361] Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 618.
[362] Seng and Tjio "International Debt Restructuring Center" 10; Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 2023*Singapore Academy of Law Journal* 618, 618.
[363] Seng and Tjio "International Debt Restructuring Center" 10; Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 618.
[364] Gurrea-Martinez and Loh "Singapore's Legal and Economic Response" 6.
[365] Gurrea-Martinez and Loh "Singapore's Legal and Economic Response" 15.
[366] Gurrea-Martinez and Loh "Singapore's Legal and Economic Response" 15.
[367] Gurrea-Martinez and Loh "Singapore's Legal and Economic Response" 15. See further, the discussion on moratorium below.

of corporate insolvency laws and its ambit must be wide to cover all types of companies, particularly SMEs in financial distress.[368] Second, the Singapore legislature must create mechanisms that allow companies, particularly SMEs with "concentrated debt structures", to be able to collaborate and mediate with their creditors in finding solutions outside the formal rescue mechanisms.[369] Third, the Singapore government must initiate financial and other tax incentives designed to encourage both debtors and creditors to resort to insolvency mechanisms where the debtor falls in financial distress.[370]

On the other end, the 2017 reforms will benefit SMEs who seek to operate within and outside the borders of Singapore.[371] This is because IRDA provides that a foreign company, including SMEs, may become a Singapore private and domiciled company without having to set up a new company in Singapore.[372] This measure reduces operational disruption and is meant to attract foreign companies and other corporates towards Singapore's favourable tax and other regulatory laws.[373] These reforms seem to be working as evidenced by the World Banks' estimation that Singapore's corporate rescue mechanisms have the highest recovery rates approximated at 88.7 Cents to the dollar.[374]

4.4. The "cram-down procedure" in Singapore

One of the successes of the 2017 reforms was the alignment of the Singapore "cross-class cram-down" legal framework with the UNCITRAL guidelines.[375] Prior to the 2017 amendments, dissenting creditors could only be "crammed down" by a court-sanctioned scheme of arrangement order.[376] This order, however, required a three-fourth majority

[368] Gurrea-Martinez and Loh "Singapore's Legal and Economic Response" 15.
[369] Gurrea-Martinez and Loh "Singapore's Legal and Economic Response" 16.
[370] Gurrea-Martinez and Loh "Singapore's Legal and Economic Response" 16.
[371] Ooi and Tan "Singapore Company Law and the Economy: Reciprocal Influence Over 50 Years" 2019 *Asia Pacific Law Review* 14, 17.
[372] Ooi and Tan "Singapore Company Law" 17.
[373] Ooi and Tan "Singapore Company Law" 18; Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 472.
[374] Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 621.
[375] Section 211H of the 2017 Act. *Cf*Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 472.
[376] Zhu "Cross-Class Cramdowns in Singapore and Lessons from the UK" 2023 *SAcLJ* 530, 530.

of votes in each class of similar creditor rights. This threshold was difficult to reach because creditor rights are not similar so that creditors are able to collectively vote on the adoption of rescue mechanisms in times of financial distress.[377]

Further, a strict creditor-categorisation legal framework resulted in the minority creditors unreasonably holding the process to ransom and preventing a rescue scheme with a potential to benefit the majority of creditors.[378] At times, the minority creditors would resort to delaying tactics such as buying blocking stakes and increasing their numerical headcounts by assigning parts of their claims.[379] However, whilst the strict creditor-categorisation approach was endorsed in *The Royal Bank of Scotland NV v TT International Ltd*,[380] in *Wah Yuen Electrical Engineering Pty Ltd v Singapore Cables Manufacturers*,[381] the Singapore Court of Appeal intimated that it must not result in an unnecessary burden on the majority creditors.[382]

Attempts to solve the challenges related to creditor-categorisation in voting began with the Companies (Amendment) Act 2014 where the words "unless the Court orders otherwise" were before the words "majority in number".[383] This resulted in the courts assuming a statutory discretion to override any traditional voting thresholds when it was reasonable to do so.[384] Eventually, cram-down procedures were modified by section 211H of the 2017 Act and subsequently, section 70 of the IRDA.[385] In line with the 2014 Amendment, the IRDA allows the court to sanction a corporate rescue procedure where[386]

- "Creditors have voted on the debtor's proposed scheme at a scheme meeting".

[377] Zhu "Cross-Class Cramdowns in Singapore" 530.
[378] Zhu "Cross-Class Cramdowns in Singapore" 531. *Cf*Ang "The Race to Rescue" 111.
[379] Zhu "Cross-Class Cramdowns in Singapore" 531. *Cf* Ang "The Race to Rescue" 111.
[380] *The Royal Bank of Scotland NV v TT International Ltd* [2012] 2 SLR 213 para 140.
[381] *Wah Yuen Electrical Engineering Pte Ltd v Singapore Cables Manufacturers* [2003] SGCA 23.
[382] *Wah Yuen Electrical Engineering Pte Ltd v Singapore Cables Manufacturers* [2003] SGCA 23 paras [22].
[383] Section 210(3AB) of the Companies (Amendment) Act 2014.*Cf* Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 622.
[384] Section 210(3AB) of the Companies (Amendment) Act 2014. *CfRe Zipmex Pte Ltd* [2023] SGHC 88; Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 622.
[385] Section 211H of the 2017 Act and section 70 of the IRDA Act.
[386] Section 70(1)(a)-(d) of the IRDA. *Cf* Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 622.

- "Creditors meant to be bound by the scheme are placed in two or more classes of creditors for the purposes of voting on the scheme".

- "The approval thresholds (ie, relating to headcount and value) must be met in at least one class of creditors".

- "Either or both of the headcount and value requirements are not met in at least one class of creditors, being the dissenting class".

What the new cram-down reforms result in are expedited and less formal procedures for a company, including SMEs that is or is likely to fall into financial distress.[387]

Nonetheless, from an "economic viewpoint", despite its good intentions, it is submitted that the Singapore legal framework must value the rights and interests of creditors in the corporate rescue processes.[388] In that regard, the cram-down against entire dissenting classes of creditors must not be done in a discriminatory manner.[389] Also, it is essential that a creditor must receive an amount that is not less than what is estimated to be received if the business was liquidated; and the absolute priority rule must be satisfied.[390]

4.5. Singapore reforms on the moratorium

At the centre of Singapore's corporate rescue legal framework is the concept of a moratorium.[391]Section 211B(1) of the 2017 Act provides that a financially distressed company may request the court to restrain the institution of legal proceedings against it;[392]and section 211B(1)CA provides for an order preventing the taking of a resolution

[387] Chuanzhong "A Critical Evaluation of the New Cram-down" 270.
[388] Chuanzhong "A Critical Evaluation of the New Cram-down" 272.
[389] Section 211H of the 2017 Act.
[390] Section 211H of the 2017 Act. Cf Chuanzhong "A Critical Evaluation of the New Cram-down" 276 notes that the "absolute priority rule" similar to that under Chapter 11 in the US was designed to balance the rights of the creditors and other stakeholders before a decision on financial rescue is adopted.
[391] Section 96(4) of the IRDA.
[392] Section 211(B)1 of the 2017 Act.

for the winding up of the company.[393] The automatic stay of thirty days immediately applies from the date of the application to enter the proposed rescue mechanism.[394]

The automatic moratorium was adopted from the US Chapter 11 and completely contrasts with Singapore's previous dispensation and UK'S discretionary moratorium.[395] Further, the thirty-day automatic moratorium may be extended where the court opines that it is appropriate and necessary to do so.[396] It is submitted that the automatic moratorium works favourably for SMEs in financial distress by allowing them to consider financial rescue alternatives whilst having control of the company and its resources.

4.6. Judicial management in Singapore

The practice of judicial management was first introduced in Singapore in 1987 as a result of the Pan-Electric crisis in the mid-1980s and the closure of the then Stock Exchange of Singapore – this initiated a major overhaul of the corporate insolvency framework.[397] Judicial management was initially adopted from the old administration procedure of the UK which sought to give financially distressed companies a temporary reprieve whilst an exit strategy was under consideration.[398]

The 2017 corporate insolvency reforms have, however, made the procedure flexible and broad.[399] The aim of judicial management is " the survival of the company, or the whole or part of its undertaking, as a going concern"; "the approval of … a compromise or arrangement"; and "a more advantageous realisation of the company's assets or property than on a winding up".[400] The order may be made by the court if it is merely likely that the company will be unable to pay its debts – this is distinct from a probability

[393] Section 211(B)1CA of the 2017 Act.
[394] Chuanzhong "A Critical Evaluation of the New Cram-down Tool in Singapore's Restructuring Regime" 2021 *International Insolvency Review* 267, 269; Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 621.
[395] Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 622.
[396] Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 622.
[397] Chan "Schemes of Arrangement as a Corporate Rescue Mechanism: The Singapore Experience" (2009) *International Insolvency Review* 37, 37.
[398] Chan "Schemes of Arrangement" 37.
[399] McCormack and Wan "Singapore's Restructuring and Insolvency Laws" 13.
[400] Section 89(1) of the IRDA.

of this occurring.[401] The Amendment Act generally weakens the veto powers of secured creditors,[402] and the court – through a "harms test"– requires the creditors to bear the burden of proving the prejudicial effect of the order.[403]

In an effort to achieve these and other objectives, the judicial manager is given a discretionary power to plan and adopt an exit strategy post-judicial management.[404] One of the questions that a court might consider in an application is whether there is an essential "public interest" in making a final order.[405] However, in both *Re Cosmotron Electronics (Singapore) Pte Ltd*[406] and *Re Bintan Lagoon Resort Ltd*,[407] the Singapore courts refused to grant the orders on the basis of public interests. In refusing to grant the orders, the courts held that there was no sufficient public interest evidence presented in support of the applications.[408] In the *Bintan* case, the court held that the adverse conduct of the company towards its employees, customers and suppliers was not sufficient to support a public interest order.[409] The court reiterated that, in order for the application to have succeeded, the applicants must have proven that the conduct of the company was "egregious" so that it could not continue as a going concern..[410]

Further, although the post-2017 judicial management process is favoured above the previous "administration" regime, there are nonetheless arguments that it is not an effective a rehabilitative procedure:[411]

> "The effectiveness of judicial management in Singapore is questionable. In 2013, the Report of the Insolvency Law Review Committee (ILRC) noted that there are few reported success

[401] Section 227B (1) of the 2017 Act.
[402] Section 227B (5) of the 2017 Act.
[403] Section 227B (5) of the 2017 Act.
[404] Seng and Tjio "International Debt Restructuring Center" 11.
[405] Chen, Azmi and Rahman "Theories of Corporate Insolvency" 191.
[406] *Re Cosmotron Electronics (Singapore) Pte Ltd* (1989) 1 SLR(R) 121 at 127.
[407] *Re Bintan Lagoon Resort Ltd* (2005) 4 SLR(R) 336.
[408] *Re Cosmotron Electronics (Singapore) Pte Ltd* (1989) 1 SLR(R) 121 at 127; *Re Bintan Lagoon Resort Ltd* (2005) 4 SLR(R) 336.
[409] *Re Bintan Lagoon Resort Ltd* (2005) 4 SLR(R) 342.
[410] *Re Bintan Lagoon Resort Ltd* (2005) 4 SLR(R) 343.
[411] Seng and Tjio "International Debt Restructuring Center" 11.

cases where judicial management has been applied and that the majority of applications for judicial management filed in the courts have not been granted".[412]

4.7. Rescue "super-priority" financing in Singapore

The Singapore 2017 Amendment Act established a new rescue financing legal framework through a "super-priority" finance scheme that has the power to override any existing security interests or rights.[413] In the new dispensation, a Singapore Court may authorise the debtor to raise more financing provided such financing is necessary to enable the debtor to continue as a going concern.[414] Basically, what the "super-priority" financing scheme seeks to achieve is to encourage prospective lenders to rescue financially distressed companies on the strength of prioritisation.[415] This prioritisation mechanism is essential because it preserves the property and other asserts of the company so that it can remain a going concern for its business dealings.[416]

However, the courts have reiterated that before a company qualifies for the "super-priority" rescue financing, there must be evidence that the debtor had obtained prior alternative financing in order to keep the company as a going concern.[417] In the *Attilan* case, a holding company based in Singapore and listed on the Singapore Exchange, managed some media and education businesses.[418] It ensued that Phillip Asia Pacific Opportunity Fund Ltd, one of its creditors, objected to the company accessing a "super-priority" funding because of the failure by the company to show that it was entitled to the finance.[419] In rejecting the company's application, the court also found that it had failed

[412] Ooi and Tan "Singapore Company Law" 29.
[413] Section 211E of the 2017 Act. *Cf* Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 477.
[414] McCormack and Wan "Singapore's Restructuring and Insolvency Laws" 18; *Cf* Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 477.
[415] Chuanzhong "A Critical Evaluation of the New Cram-down" 270.
[416] Chuanzhong "A Critical Evaluation of the New Cram-down" 270.
[417] *Re Atillan* [2017] SGHC 283. *Cf* Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 477.
[418] *Re Atillan* [2017] SGHC 283. *Cf* Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 623.
[419] *Re Atillan* [2017] SGHC 283. Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 618.

to demonstrate that it had alternative financing mechanisms besides the "super-priority" financing.[420]

Further, it is worth noting that, because "super-priority" finance rescue was resisted in the UK, the CSSICDR looked into the US and noted that:

> "As Singapore and the regional market are new to rescue financing, the most effective way for the market to develop as quickly as possible is to leverage on the knowledge, expertise and experience of the US market in rescue financing".[421]

By adopting a flexible legal framework such as the one found in US law, the Singapore corporate insolvency laws envisaged to be regionally and globally attractive whilst also keeping their financially distraught companies afloat.[422] However, the 2017 reforms require a higher threshold in that the rescue finance would not have been obtained but for the granting of the relevant order of priority.[423]

Also, in order for a company to qualify under the new restructuring laws in Singapore, the debtors and creditors must be able to agree to a proposed plan to repay the debts of the company without going through insolvency and liquidation.[424] This process entails the adoption of significant changes in the structures and the operations of the financially distressed company.[425] The decision whether the company can be returned to profitability is an objective one made by considering all surrounding circumstances.[426] In exercising any decision related to financial distress, the Singapore Court of Appeal confirmed that the directors of the company owe a fiduciary duty to the creditors of the company more than to shareholders.[427] As such, if there is evidence to show that the

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[420] *Re Atillan* [2017] SGHC 283. Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 618.
[421] Seng and Tjio "International Debt Restructuring Center" 20-21.
[422] Seng and Tjio "International Debt Restructuring Center" 20-21.
[423] Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 477.
[424] George "Insolvency and Restructuring in Singapore" 2019*CourtUncourt* 27, 27.
[425] George "Insolvency and Restructuring in Singapore" 27.
[426] George "Insolvency and Restructuring in Singapore" 27.
[427] *Foo Kian Beng v OP3 International Pte Ltd (in liquidation)* [2024] SGCA 10- judgment dated March 28, 2024, confirming the decision of the High Court in *OP3 International Pte Ltd (in liquidation) v Foo Kian Beng* [2022] SGHC 225. *Cf* Kapur "The Social Dynamics of Corporate Insolvency Law and Workers/Employees of Distressed Companies: Comparing Select Asian Jurisdictions" 2024 *ECGI Working Paper Series in Law* 1, 27.

company may not return to making profit or that it will not be successfully rescued, a decision to sell the company or to liquidate it must be taken.[428]

The practicality of the Singapore finance rescue mechanism is questionable in some respects. First, it is doubtful whether a "super-priority" rescue finance will be successful in Singapore in practice, given that it was largely opposed in the UK.[429] Secondly, it is questionable whether the new approach truly has solid requirements for the funding to take place, such as the viability of the company or business that seeks financing.[430] Thirdly, it is questioned how potential "super-priority" lenders will deal with those companies, such as SMEs who do not have adequate assets or collateral for lending purposes.[431]

4.8. Challenges with the hybrid corporate insolvency system

The transplantation of English corporate insolvency laws into Singapore has not been without its difficulties:

> "It is well established that reforms must be sensitive to local conditions and should take account of different implementing environments. Legal concepts tend to behave differently in different countries, and the importation of a new concept may have unintended consequences for the rest of the body of law".[432]

Difficulty has arisen with regard to the sustainability and balancing of the hybrid legal system comprising of English law principles and the common law rights of creditors under the laws of Singapore.[433] First, as a legal system that has always been known for being "creditor-friendly", the 2017 reforms are more likely to tip the scales against creditors in favour of shareholders and company managers.[434] Secondly, there is strong

[428] George "Insolvency and Restructuring in Singapore" 27.
[429] McCormack and Wan "Singapore's Restructuring and Insolvency Laws" 19.
[430] McCormack and Wan "Singapore's Restructuring and Insolvency Laws" 19.
[431] McCormack and Wan "Singapore's Restructuring and Insolvency Laws" 19.
[432] Wan, Watters and McCormack "Schemes of Arrangement in Singapore: Empirical and Comparative Analyses" 2020 *American Bankruptcy Law Journa*l 463, 468.
[433] Seng and Tjio "International Debt Restructuring Center" 10.
[434] McCormack and Wan "Transplanting Chapter 11 of the US Bankruptcy Code into Singapore's Restructuring and Insolvency Laws: Opportunities and Challenges" 2019 *Journal of Corporate Law Studies* 1, 5.

suggestion that the reforms might not have been designed or targeted to effectively to rescue SMEs in financial distress.[435]

4.9. Concluding remarks

In this chapter, the Singapore legal framework in respect of corporate rescue was investigated, with a focus on SMEs. The research resulted in several observations and suggestions. First, the study established that English law has, and continues to have, a significant bearing on the corporate insolvency laws in Singapore.[436] It is argued that it was the SOA practice established in UK around 1870 that eventually found its way into Singapore and which underlies most of the modern corporate rescue mechanisms.[437] It is noted, however, that modern corporate reform in Singapore began with the recommendations of the ILRC and the CSSICDR, which resulted in the 2017 Act and the 2018 IRDA.[438]

Secondly, the study established that, because the legal framework in Singapore might be too formal and expensive,[439] it might not have been designed to effectively resuscitate financially distressed SMEs, particularly in emergencies.[440] As such, it is suggested that, in order to effectively rescue financially-distressed SMEs, the government must establish pre-emergency procedures such as automatic statutory moratoriums;[441] establish extra judiciary mediation mechanisms;[442] and consider other financial and tax incentives for debtors and creditors that successfully embark on stipulated rescue procedures .[443]

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[435] Gurrea-Martinez and Loh “Singapore's Legal and Economic Response to the Covid-19 Crisis: The Role of Insolvency Law and Corporate Workouts” 2020 *Company Lawyer* 1,6.
[436] Seng and Tjio “International Debt Restructuring Center” 9; Chen, Azmi and Rahman “Theories of Corporate Insolvency” 168.
[437] Ang “The Race to Rescue” 111.
[438] Insolvency, Restructuring and Dissolution Act 2018; Committee to strengthen Singapore as an International Centre for Debt Restructuring (CSSICDR); Companies (Amendment) Act 2017.
[439] Gurrea-Martinez and Loh “Singapore's Legal and Economic Response” 15.
[440] Gurrea-Martinez and Loh “Singapore's Legal and Economic Response” 6.
[441] Gurrea-Martinez and Loh “Singapore's Legal and Economic Response” 15.
[442] Gurrea-Martinez and Loh “Singapore's Legal and Economic Response” 16.
[443] Gurrea-Martinez and Loh “Singapore's Legal and Economic Response” 16.

Thirdly, the study established that the alignment of the 2017 reforms with the UNCITRAL guidelines has alleviated most of the challenges historically linked to deadlocks in creditor-categorisation and voting.[444] Instead of requiring a three-fourth majority vote for rescue financing, the courts now have a statutory discretion to override voting thresholds when it is reasonable to do so.[445] It is argued that this new threshold is practical and may result in the resuscitation of SMEs which might have not qualified under the old dispensation.[446] Nonetheless, it is suggested that, despite the reforms, the rights and interests of creditors must still be considered in the determination of a suitable corporate rescue procedure,[447] and that the decision must not be discriminatory.[448]

Fourthly, the study established that the practice of judicial management was first introduced in Singapore in 1987 from the then UK administration procedure,[449] when it was in the "public interest" to do so.[450] However, an applicant for judicial management must prove, amongst others, that the conduct of a company against which the order is sought must be so "egregious" to warrant a judicial management order.[451] This study argues that the current threshold in Singapore is commendable in that the order may be made where the court considers it "merely likely" that the company will be unable to pay its debts as distinct from a probability of this occurring.[452] Also, by generally weakening the powers of secured creditors and shifting the burden of proving prejudice to them, the rights of financially-distressed SMEs with weak bargaining powers are more likely safeguarded.[453]

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[444] Zhu "Cross-Class Cramdowns in Singapore" 530; Section 211H of the 2017 Act. *Cf* Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 472.
[445] Section 210(3AB) of the Companies (Amendment) Act 2014. *Cf Re Zipmex Pte Ltd* [2023] SGHC 88; Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 622; Zhu "Cross-Class Cramdowns in Singapore" 530.
[446] Section 210(3AB) of the Companies (Amendment) Act 2014. *Cf Re Zipmex Pte Ltd* [2023] SGHC 88; Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore'' 622; Zhu "Cross-Class Cramdowns in Singapore" 530.
[447] Chuanzhong "A Critical Evaluation of the New Cram-down" 272.
[448] Section 211H of the 2017 Act.
[449] Chan "Schemes of Arrangement" 37.
[450] Chen, Azmi and Rahman "Theories of Corporate Insolvency" 191.
[451] *Re Bintan Lagoon Resort Ltd* (2005) 4 SLR(R) 343.
[452] Section 227B (1) of the 2017 Act.
[453] Section 227B (5) of the 2017 Act.

Fifth, the study established that the 2017 Amendment Act created a new finance rescuing legal framework known as the "super-priority" scheme that may override any existing security rights or interests.[454] What the "super-priority" financing scheme seeks to achieve is that, on the promise of prioritisation, lenders will be more willing to rescue financially distressed companies.[455] However, for a company to qualify for the "super-priority" financing, it must show that it already had alternative financing to keep it going as a viable concern.[456]

Finally, the practicality of the rescue mechanism is questioned in some respects. First, it is asked whether this scheme will be successful in Singapore given that it faced a huge backlash in the UK.[457] Secondly, it is asked whether there are any substantive requirements as the basis of the scheme.[458] Third, it is asked whether the scheme was designed with SMEs in mind, particularly, those who do not have adequate asserts as or collateral.[459] Fourth, it is asked whether a legal system known for being "creditor-friendly", will be neglecting creditor rights in favour of shareholders.[460]

[454] Section 211E of the 2017 Act. *Cf* Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 477.
[455] Chuanzhong "A Critical Evaluation of the New Cram-down" 270.
[456] *Re Atillan* [2017] SGHC 283. *Cf* Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 477.
[457] McCormack and Wan "Singapore's Restructuring and Insolvency Laws" 19.
[458] McCormack and Wan "Singapore's Restructuring and Insolvency Laws" 19.
[459] McCormack and Wan "Singapore's Restructuring and Insolvency Laws" 19; Gurrea-Martinez and Loh "Singapore's Legal and Economic Response" 6.
[460] McCormack and Wan "Singapore's Restructuring and Insolvency Laws" 5.

CHAPTER 5: COMPARISON AND CONCLUSION

5.1. Introduction

The previous chapters dealt with the South African and the Singapore corporate rescue legal framework with focus of SMEs. In contextualising the legal problem, the chapters looked into the historical dispositions of the two legal systems in general. The role of SMEs and their socio-economic contribution in the two legal systems as well as the challenges encountered were investigated. Following on these previous chapters, the following discussion provides a general comparative overview of the main issues that have already been highlighted against the general guidelines of the UNICITRAL.

In that respect, it will be advanced that although both the South African and the Singapore have a number of individual strong points in relation with their corporate insolvency laws, they do nonetheless have a lot to consider from the UNICITRAL. In that regard, in providing a comparative general overview of the two legal systems, the study will focus on the following: the nature of the procedures and the manner of commencement; financial distress and reasonable prospect; moratorium in business rescue; the cram-down procedures and post-commencement financing. After providing a brief overview on these aspects, the study will provide recommendations in line with the gathered observations.

5.2. The nature of the procedures and the manner of commencement

In providing context to the South African business rescue legal framework, it was highlighted that, initially, financially distressed companies were assisted through the practice of judicial management under the Companies Act 46 of 1926 and the Companies Act 61 of 1973. This practice was introduced as a result of the need to manage businesses with the potential to return to a profitable state.[461] Nevertheless, the practice was not entirely successful because of among others, its inherent weaknesses and its prioritisation of the "creditor" as opposed to the resuscitation of the "business".[462]

[461] Phungula *Evolution of Effective Business Rescue* 4.
[462] Loubser "Effective Corporate Rescue Procedure" 438.

Furthermore, the practice did not receive any practical support, but was viewed as an foreign doctrine likely to be a financial burden on the State.[463] Thus, it was argued that the failure of judicial management in South Africa was because it was not considered autonomous, but was inextricably intertwined with liquidation.[464]

Following the demise of the practice of judicial management, in 2011, a new business rescue legal framework was introduced through the Companies Act 71 of 2008. Much like the previous dispensations, the Act introduced a new legal framework aimed at the resuscitation of financially distressed companies with a focus on preserving them as going concerns.[465] The Act allows companies to undergo business rescue proceedings on the basis of an order of the court,[466] or by the application by any interested person such as the directors of the company, the shareholders, employees, and a trade union.[467] In order for affected persons to place the company in business rescue, they must prove that the company is financially distressed; or that it has failed to pay some of its debts; or that it is just and equitable to do so.[468]

In South African law, in terms of section 153(1)(a), if a business rescue plan has been rejected, the practitioner may attempt to prepare and publish and revised plan or approach the court to set aside the result of the vote as inappropriate.[469]

On the part of Singapore's corporate insolvency legal framework, it was established that its strong relation to the US resulted in the streamlining of its legal framework from 2010 through the of the recommendations ILRC[470] and the CSSICDR[471] which culminated to the Act of 2017.[472]The 2017 Act provides for five broad regimes which are liquidation,

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[463] Phungula *Evolution of Effective Business Rescue* 5.
[464] Kloppers "Judicial Management" 424. See also Olver "Judicial Management" 84-86.
[465] Rushworth "Business Rescue Regime" 375.
[466] Rushworth "Business Rescue Regime" 375.
[467] Section 129 and 131 of the Companies Act; *The Business Rescue Practitioner of Sea Harvest Group Limited v The Commissioner of the South African Revenue Service* (1377/2018) [2019] ZAFSHC 84 (17 September 2019), the court approved the application for business rescue after considering that there was proof that it would result in better returns for shareholders, creditors and the employees of the company.
[468] Section 131(4)(a) of the Companies Act. See also Marumoagae "The Rights of Affected Persons as Stakeholders During Business Rescue Proceedings in South Africa" 2018 *JCCL & P* 117, 126.
[469] Section 153(1)(a)(i)-(ii) of the Companies Act.
[470] Insolvency Law Review Committee (ILRC) (2010).
[471] Committee to strengthen Singapore as an International Centre for Debt Restructuring (CSSICDR).
[472] Companies (Amendment) Act 2017 (hereafter, the 2017 Act).

judicial management, receivership, a Commonwealth scheme and a hybrid scheme.[473]Generally, although the legal framework in Singapore does have its perks, because of being too formal and expensive, it appears not effectively provide a mechanism to resuscitate SMEs.[474] In that regard, it is argued that in order to create an effective rescue approach, the Singapore government must consider pre-emergency rescue procedures specifically designed to rescue SMEs.[475] Further, it is suggested that the government must initiate financial and other tax incentives designed to encourage both debtors and creditors to resort to insolvency mechanisms where the debtor falls in financial distress.[476]

5.3. Financial distress and reasonable prospect

In South African law, section 427(1) read with section 432 of the Companies Act of 1973 underscored that, in order for a company to have been successfully placed under judicial management, there must had been a "reasonable probability"[477] that it would return to a successful concern.[478] This was confirmed in *Kotze v Tulryk Bpk*,[479] where the court said that a "reasonable probability" that the company would return as a successful concern was prerequisite in the application for judicial management.[480] It is clear that in South Africa, the "reasonable prospect" threshold operates as a huge challenge for SMEs as opposed to the "possibility" or "probability" of restoring the business to its operational capacity.[481]

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[473] Seng and Tjio "International Debt Restructuring Center" 10.
[474] Gurrea-Martinez and Loh "Singapore's Legal and Economic Response" 15.
[475] Gurrea-Martinez and Loh "Singapore's Legal and Economic Response" 15.
[476] Gurrea-Martinez and Loh "Singapore's Legal and Economic Response" 16.
[477] See *Noordkaap Lewendhawe Ko-operasie Bpk v Schreuder* 1974 (3) SA 102 (A) at 110, where the court emphasized that the difference between "probable" and "possible" is material in that the latter relates to something that is less sure to happen. See also Joubert "Reasonable Possibility" 552.
[478] Section 427 (1) and section 432 of the Companies Act of 1973. See also *Noordkaap Lewendehawe Ko-op Bpk v Schreuder* 1974 (3) SA 102 (A) at 110; Henning "Judicial Management and Corporate Rescue" 92.
[479] *Kotze v Tulryk Bpk*1977 (3) SA 118 (T).
[480] *Kotze v Tulryk Bpk*1977 (3) SA 118 (T) at 120. See also *Tenowitz v Tenny Investments (Pty) Ltd* 1979 (2) SA 680 (E) at 683.
[481] Du Toit, Pretorius and Rosslyn-Smith "Small, Medium and Micro-Enterprises" 5; Maphiri "Business Rescue Procedure" 115. See also See chapter 2 above on "reasonable prospect v reasonable probability".

Further, in terms of the 2008 Act, financial distress entails that the company will not be able to pay its debt as they become due in the next six months and that the company will become insolvent within the immediate ensuing six months. It is clear that the definition of "financial distress" in terms of the Companies Act contributes to the inaccessibility of the financial rescue mechanism to SMEs.[482] This is because "financial distress" is described in the limited ambit of a company's failure to honour its liabilities within the six ensuing months making it highly improbable for SMEs to effectively access financial rescue earlier.[483] As far as financial distress in Singapore is concerned, the order may be made where it is likely that the company will be unable to pay its debts as opposed to the probability of this occurring.[484]

5.4. Moratorium in business rescue

In South African law, as soon as the process of business rescue commences, there is a general moratorium on all the legal proceedings against the company.[485] First, this means that no legal action, including an enforcement action in relation to any property matter including the possession without from the practitioner or a court order.[486] Secondly, a moratorium applies with respect to any guarantee or suretyship undertake by the company which may not be enforced without an order of the court on the basis of just and equitable circumstances.[487] Thirdly, where any third party has a right against the company that is subject to a time limit, the right is automatically suspended until such a time the rescue process continues.[488] However, the moratorium does not apply amongst others: to criminal proceedings against the company;[489] to proceedings by a regulatory framework;[490] to matters relating to property managed by a company as a trustee and;[491] to proceedings relating to a set-off initiated by the company.[492]

[482] Maphiri "Business Rescue Procedure" 113.
[483] Section 128(1)(f) of the Companies Act.
[484] Section 227B (1) of the 2017 Act.
[485] Sharrock *et al Hockly's Insolvency Law* 281.
[486] Section 133(1) (a) -(b) of the Companies Act; Sharrock *et al Hockly's Insolvency Law* 281.
[487] Section 133(2) of the Companies Act; Sharrock *et al Hockly's Insolvency Law* 282.
[488] Section 133(3) of the Companies Act; Sharrock *et al Hockly's Insolvency Law* 282.
[489] Section 133(1)(d) of the Companies Act; Sharrock *et al Hockly's Insolvency Law* 282.
[490] Section 133(1)(f) of the Companies Act; Sharrock *et al Hockly's Insolvency Law* 282.
[491] Section 133(1)(e) of the Companies Act; Sharrock *et al Hockly's Insolvency Law* 282.

Like in South African law, one of the successes of the Singapore's corporate rescue legal framework is the concept of a moratorium where a financially distressed company may request the court to restrain the institution of legal proceedings against it[493] and by so doing prevents the taking of a resolution for the winding up of the company.[494] The automatic stay of thirty days immediately applies from the date of the application to enter the proposed rescue mechanism.[495]The automatic moratorium was adopted from the US Chapter 11 and completely contrasts with Singapore's previous dispensation and UK'S discretionary moratorium.[496] Further, the thirty-day automatic moratorium may be extended where the court opines that it is appropriate and necessary to do so.[497] It is submitted that the automatic moratorium works favourably for SMEs in financial distress by allowing them to consider financial rescue alternatives whilst having control of the company and its resources.

5.5. The cram-down procedures

In South African law, in terms of section 153(1)(a), a rejected business rescue plan may be revised plan or the result of the vote may be set aside as inappropriate.[498]However, in terms of section 152(2), a business rescue plan will be approved "if it was supported by the holders of more than 75% of the creditors' voting interests that were voted; and the votes in support of the proposed plan included at least 50% of the independent creditors' voting interests, if any, that were voted".[499]

As far as cram-down is concerned in Singapore, the 2017 reforms are commended for their endeavour to align the "cross-class cram-down" legal framework with the UNCITRAL guidelines.[500] This is because prior to the amendments, dissenting creditors

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[492] Section 133(1)(c) of the Companies Act; Sharrock *et al Hockly's Insolvency Law* 282.
[493] Section 211(B)1 of the 2017 Act and section 96(4) of the IRDA.
[494] Section 211(B)1CA of the 2017 Act.
[495] Chuanzhong "A Critical Evaluation of the New Cram-down Tool in Singapore's Restructuring Regime" 2021 *International Insolvency Review* 267, 269; Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 621.
[496] Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 622.
[497] Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 622.
[498] Section 153(1)(a)(i)-(ii) of the Companies Act.
[499] Section 152(2) of the Companies Act.
[500] Section 211H of the 2017 Act. *Cf* Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 472.

could only be "crammed down" by a court order.[501] However, because the creditor rights are not similar in class, it is often problematic for the creditors to group together for the purpose of voting.[502] This resulted in the minority creditors holding the process to ransom and preventing a rescue scheme with a potential to benefit the majority of creditors[503] though delaying tactics such as buying blocking stakes.[504] Cram-down procedures are now modified by section 211H of the 2017 Act and subsequently, section 70 of the IRDA[505] and gives the court the final say on a corporate rescue procedure.[506]

5.6. Post-commencement financing

In South African law, section 135(2) of the Act of 2008 provides that,"[d]uring the business rescue proceedings, the company may obtain financing".[507]The Act provides that the financing may be secured to the lender by utilizing any assert of the company to the extent that it is otherwise not encumbered.[508]Stoop and Hutchison consider two consequences of this section in South African law.[509] First, the authors argue that there is no doubt that the post-commencement creditors of the financing rank higher than other creditors.[510] Second, the authors sound concerned over the requirement of assets to which the financing will be secured.[511] It is submitted that this is a huge concern when one considers that many companies, in particular SMEs seldom have any valuable assets after the process of business rescue.[512] It is clear from this section, that South African law does not provide a definite and targeted mechanism for companies in

[501] Zhu "Cross-Class Cramdowns in Singapore and Lessons from the UK" 2023 *SAcLJ* 530, 530.
[502] Zhu "Cross-Class Cramdowns in Singapore" 530.
[503] Zhu "Cross-Class Cramdowns in Singapore" 531. *Cf* Ang "The Race to Rescue" 111.
[504] Zhu "Cross-Class Cramdowns in Singapore" 531. *Cf* Ang "The Race to Rescue" 111.
[505] Section 211H of the 2017 Act and section 70 of the IRDA Act.
[506] Section 70(1)(a)-(d) of the IRDA. *Cf* Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 622.
[507] Section 35(2) of the Companies Act.
[508] Section 35(2)(a) of the Companies Act.
[509] Stoop and Hutchison "Post-Commencement Finance – Domiciled Resident or Uneasy Foreign Transplant" (2017) PER/PELJ 1. 5
[510] Stoop and Hutchison "Post-Commencement Finance" 16. Cf Section 35(2) of the Companies Act; Calitz and Freebody "Is Post-Commencement Finance Proving to be the Thorn in the Side of Business Rescue Proceedings Under the 2008 Companies Act?" (2016) De Jure 265, 272.
[511] Stoop and Hutchison "Post-Commencement Finance" 16. Cf Section 35(2) of the Companies Act.
[512] Stoop and Hutchison "Post-Commencement Finance" 16. Cf Section 35(2) of the Companies Act.

financial distress, in particular SMEs.[513] Further, it is clear that there are not targeted or effective incentives designed to encourage creditors to be interested in providing finance to companies proceeding from business rescue.[514]

Regarding post-financing in Singapore, it was established that the Singapore 2017 Act established a new rescue financing legal framework through a "super-priority" finance scheme that may override any existing security interests or rights.[515]In the new dispensation, a Singapore Court may authorise the debtor to raise more financing provided such financing is necessary to enable the debtor to continue as a going concern.[516]Basically, what the "super-priority" financing scheme seeks to achieve is to encourage prospective lenders to rescue financially distressed companies on the strength of prioritisation.[517]This prioritisation mechanism is essential because it preserves the property and other assets of the company so that it can remain a going concern for its business dealings.[518]

5.7. Conclusion and recommendations

The aim of this study was to provide a comparative overview of the South African and the Singapore corporate rescue legal frameworks, with particular focus on SMEs. In that regard, it was established that whilst in South Africa, corporate rescue was initially in the form of judicial management and then corporate rescue,[519] in Singapore, the streamlining of their laws began with the of the recommendations ILRC[520] and the CSSICDR[521] which culminated to the Act of 2017.[522] Both legal systems provide for

[513] Stoop and Hutchison "Post-Commencement Finance" 17. Cf Section 35(2) of the Companies Act.
[514] Stoop and Hutchison "Post-Commencement Finance" 16. Cf Section 35(2) of the Companies Act.
[515] Section 211E of the 2017 Act. Cf Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 477.
[516] McCormack and Wan "Singapore's Restructuring and Insolvency Laws" 18; Cf Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 477.
[517] Chuanzhong "A Critical Evaluation of the New Cram-down" 270.
[518] Chuanzhong "A Critical Evaluation of the New Cram-down" 270.
[519] Companies Acts 71 of 2008; 61 of 1973 and 46 of 1926.
[520] Insolvency Law Review Committee (ILRC) (2010); Companies Acts 71 of 2008; 61 of 1973 and 46 of 1926.
[521] Committee to strengthen Singapore as an International Centre for Debt Restructuring (CSSICDR).
[522] Companies (Amendment) Act 2017 (hereafter, the 2017 Act).

regimes such as liquidation, judicial management, receivership, a Commonwealth scheme and a hybrid scheme.[523]

Further, the study established that both the South African and the Singapore legal frameworks have an effective moratorium system which complies with the UNCITRAL guidelines. In South African law, as soon as the process of business rescue commences, there is a general moratorium on all the legal proceedings against the company.[524] First, this means that no legal action, including an enforcement action in relation to any property matter including the possession without from the practitioner or a court order.[525]

In South Singapore, a company may request the court to restrain the institution of legal proceedings against it,[526] which prevents the taking of a resolution for the winding up of the company.[527] The automatic stay of thirty days immediately applies from the date of the application to enter the proposed rescue mechanism.[528] It is submitted that the approach on moratorium in the two legal systems is very commendable in terms with the resuscitation objectives of the UNCITRAL.[529]

Furthermore, it was established that whilst in South Africa, post-commencement rescue finance is regulated in terms of section 135(2), in Singapore, it is regulated in terms of the 2017 Act through a "super-priority" finance scheme that may override any existing security interests or rights.[530] whilst in South Africa, the financing may be secured to the lender by utilizing any asset of the company to the extent that it is otherwise not encumbered,[531] in Singapore, the Court may authorise the debtor to raise more

[523] Seng and Tjio "International Debt Restructuring Center" 10.
[524] Sharrock *et al Hockly's Insolvency Law* 281.
[525] Section 133(1) (a) -(b) of the Companies Act; Sharrock *et al Hockly's Insolvency Law* 281.
[526] Section 211(B)1 of the 2017 Act and section 96(4) of the IRDA.
[527] Section 211(B)1CA of the 2017 Act.
[528] Chuanzhong "A Critical Evaluation of the New Cram-down Tool in Singapore's Restructuring Regime" 2021 *International Insolvency Review* 267, 269; Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 621.
[529] Article 6, 8, 11, 12 and 13 of the UNCITRAL Recommendations on SME Insolvency.
[530] Section 211E of the 2017 Act. Cf Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 477.
[531] Section 35(2)(a) of the Companies Act.

financing provided such financing is necessary to enable the debtor to continue as a going concern.[532]

In summary, it is submitted that although both the South Africa and Singapore do have legal frameworks designed for post-commencement finance, nonetheless the two legal systems may benefit profoundly from the UNICITRAL.[533] In that regard, the UNICITRAL is clear and unwavering that for the purpose of post-commencement finance:

> "The insolvency law should facilitate and provide incentives for post-commencement finance to be obtained by the insolvency representative where the insolvency representative determines it to be necessary for the continued operation or survival of the business of the debtor or the preservation or enhancement of the value of the estate. The insolvency law may require the court to authorize or creditors to consent to the provision of post-commencement finance".[534]

What follows next are the recommendations of the study.

The focus of this study was to consider both the South African and the Singapore's business rescue legal frameworks at the backdrop of the UNCITRAL Model Law which seeks to provide an internationally standardized approach. In that regard, the study concludes that both legal systems have recommendable structures, they may nonetheless be improved by the UNCITRAL guidelines.

In that regard, it is recommended, first that both legal systems are clearly in need of a consolidated system of SME debt restructuring with the fundamental objective of resuscitating companies, particularly SMEs.[535] Essentially, the study established that both the South African and the Singapore legal frameworks show signs of being too rigid, too formal and too expensive to effectively provide a mechanism to resuscitate SMEs.[536] With particular respect to South Africa, it was established that because only

[532] McCormack and Wan "Singapore's Restructuring and Insolvency Laws" 18; Cf Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 477.
[533] Calitz and Freebody "s Post-Commencement Finance" 282.
[534] UNCITRAL Legislative Guide on Insolvency Law (2005) 113.
[535] Article 3 of the UNCITRAL Recommendations on SME Insolvency.
[536] Gurrea-Martinez and Loh "Singapore's Legal and Economic Response" 15; Maphiri "Business Rescue Procedure" 109; Kloppers "Judicial Management" 426.

High Courts have jurisdiction in matters related to insolvency, this clearly does not operate in favour of SMEs both in terms of access the costs associated with High Court litigation.[537]

Second, the study established that although the South African and the Singapore legal frameworks do have their individual strong points, they are both generally not entirely fully compliant with the UNCITRAL guidelines on corporate insolvency. As such, it is recommended that in line with the UNCITRAL both legal systems must ensure that all debts incurred by SMEs are consolidated in a manner that takes account the primary objective of resuscitating them,[538] by a specified or independent[539] body or forum.[540] Such a regime must clearly provide the procedures, time periods and the cost effectiveness of the resuscitation initiatives,[541] as well as circumstances requiring "debtor" or "creditor" involvement.[542]

Third, it is submitted that both in line with the UNCITRAL both the South African legal framework must provide for simplified insolvency proceedings available and easily accessible to SMEs and also by promoting the SME debtor's fresh start by enabling expedient liquidation of non-viable SMEs and reorganisation of viable SME through simplified insolvency proceedings.[543]

Fourth, it is recommended that South Africa has a lot to learn from the Singapore "cram down" rules. In terms of South African law, if a business rescue plan has been rejected, the practitioner may apply to court to set aside the result of the vote by the holders of voting interests on the grounds that it was inappropriate.[544] This is a stark contrast with

[537] Maphiri "Business Rescue Procedure" 109; Kloppers "Judicial Management" 426.
[538] Article 3 of the UNCITRAL Recommendations on SME Insolvency.
[539] Article 8 of the UNCITRAL Recommendations on SME Insolvency.
[540] Article 6 of the UNCITRAL Recommendations on SME Insolvency.
[541] Articles 11, 12 and 13 of the UNCITRAL Recommendations on SME Insolvency.
[542] Articles 17 and 18 of the UNCITRAL Recommendations on SME Insolvency.
[543] Article 6, 8, 11, 12 and 13 of the UNCITRAL Recommendations on SME Insolvency
[544] Section 153(1)(a)(i)-(ii) of the Companies Act.

the Singapore's approach which clearly gives the court power over the dissenting creditors.[545]

Fifth, it is recommended that South Africa has a lot to learn from the Singapore "super-financing" mechanism. Rather than section 135(2), which provides that "[d]uring the business rescue proceedings, the company may obtain financing",[546] the Singapore 2017 Act makes for a "super-priority" finance scheme that may override any existing security interests or rights.[547] This legislative framework in line with the UNCITRAL significantly ensures that the property and other asserts of the company, particularly an SME can remain a going concern for its business operations.[548]

[545] Section 70(1) (a) -(d) of the IRDA read with Section 211H of the 2017.*Cf* Watters and Omar "The Evolution of Cross-Border Insolvency in Singapore" 622.
[546] Section 35(2) of the Companies Act. Cf Stoop and Hutchison "Post-Commencement Finance" 16. Calitz and Freebody "Post-Commencement Finance" 265.
[547] Section 211E of the 2017 Act. Cf Wan, Watters and McCormack "Schemes of Arrangement in Singapore" 477; Cf Stoop and Hutchison "Post-Commencement Finance" 16. Calitz and Freebody "Post-Commencement Finance" 265.
[548] Chuanzhong "A Critical Evaluation of the New Cram-down" 270.

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