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# CORPORATE & COMMERCIAL ALERT

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### Impact of business rescue and creditors compromise on contractual arrangements

Business rescue proceedings and arrangements or compromises with creditors under the Companies Act 71 of 2008 (Companies Act) are, by their very nature, contentious proceedings which may result in the dissatisfaction of some participating parties.

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## Impact of business rescue and creditors compromise on contractual arrangements

Pursuant to the conclusion of the Buy-Back Agreement, Highveld Syndication began experiencing financial difficulties and in 2010, the group of companies which Highveld Syndication formed part of were placed under business rescue.

**Business rescue proceedings and arrangements or compromises with creditors under the Companies Act 71 of 2008 (Companies Act) are, by their very nature, contentious proceedings which may result in the dissatisfaction of some participating parties.**

The case of *Zephan (Pty) Ltd & others v Noormahomed* (1303/18) [2019] ZASCA 162 (29 November 2019) (*Zephan v Noormahomed*) explores the effect of business rescue proceedings in terms of section 128 of the Companies Act and arrangements or compromises with creditors in terms of section 155 of the Companies Act on share buy-back agreements similar to the share buy-back agreement concerned in the case. We have used this case to study the impact of business rescue proceedings or arrangements with creditors on contractual arrangements to which the company undergoing either one of these processes is not party to, but which affect securities held in it.

*Zephan v Noormahomed* revolved around a share buy-back agreement entered into between Zephan Proprietary Limited (Zephan) and Suraiya Begun Noormahomed (Suraiya) in terms of which Zephan sold 3,000 shares in Highveld Syndication Proprietary Limited (Highveld

Syndication), which shares Zephan had acquired for a purchase price of R3 million, to Suraiya and agreed to purchase the same shares from Suraiya after a period of 5 years for a pre-agreed purchase price of R6 million (Buy-Back Agreement).

Pursuant to the conclusion of the Buy-Back Agreement, Highveld Syndication began experiencing financial difficulties and in 2010, the group of companies which Highveld Syndication formed part of were placed under business rescue. After it became clear that it was necessary to restructure the debts of Highveld Syndication so as to yield a better return for its creditors than any return that would have resulted from liquidation, the company proceeded to enter into a court sanctioned arrangement with its creditors in terms of section 155 of the Companies Act, which included the adoption of a plan to restructure the debts of Highveld Syndication and entailed receipt by Suraiya of interest payments from a related company, Orthotouch Limited (Orthotouch) (section 155 Arrangement).

Upon expiry of a period of five years from conclusion of the Buy-Back Agreement, Suraiya demanded that Zephan comply with its undertaking to purchase the shares in Highveld Syndication in accordance with the terms of the Buy-Back Agreement.

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## Impact of business rescue and creditors compromise on contractual arrangements...continued

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The question before the SCA was whether the section 155 Arrangement and Suraiya's receipt of interest payments from Orthotouch had novated Suraiya's rights under the Buy-Back Agreement.

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After the Defendant had accordingly failed to fulfil its obligations under the Buy-Back Agreement, Suraiya elected to approach the High Court of South Africa, Pretoria (High Court) to enforce the terms of the Buy-Back Agreement and accordingly obtained judgment by default, which was followed by an application for rescission of the default judgment by Zephan.

In the High Court, and subsequently the Supreme Court of Appeal (SCA), Zephan argued that Suraiya's rights under the Buy-Back Agreement had been novated through Suraiya voting in favour of the section 155 Arrangement and by receiving interest payments from Orthotouch. In turn, Suraiya argued that the section 155 Arrangement and her receipt of interest payments from Orthotouch did not affect her rights in terms of the Buy-Back Agreement.

The question before the SCA was whether the section 155 Arrangement and Suraiya's receipt of interest payments from Orthotouch had novated Suraiya's rights under the Buy-Back Agreement.

The SCA held that there was an irrevocable undertaking by Zephan to purchase the shares of Suraiya as agreed in terms of the Buy-Back Agreement. It was noted by the SCA that the undertaking of Zephan in terms of the Buy-Back Agreement was independent and insulated from the affairs of Highveld Syndication.

The SCA proceeded to refer to the judgment of *Zephan (Pty) Ltd & others v De Lange* (1068/2015) [2006] ZASCA 195 [2 December 2016] (*Zephan v De Lange*) which dealt with a similar issue where the question before the SCA was whether the adoption of a business rescue plan had rendered a share buy-back agreement unenforceable. The SCA in *Zephan v De Lange* held as follows:

*"The business rescue plan relates only to the restructuring of the business of the HS companies and not the appellants. When the HS companies went into business rescue the appellants were the primary carriers of the obligation to buy back Mrs De Lange's shares. The fact that the HS companies might have been in business rescue was irrelevant to the appellants' discharge of their obligations under the buy-back agreement. Neither was the fact that she had accepted payments of the reduced annual interest. Such interest was never part of the buy-back agreement. There could be no basis for a finding that Mrs De Lange had compromised her rights under the buy-back agreement."*

## Impact of business rescue and creditors compromise on contractual arrangements...*continued*

The lesson in this regard is a clear affirmation to the effect that no rights or obligations under an agreement similar to the Buy-Back Agreement may be relinquished by either business rescue proceedings nor an arrangement or compromise with creditors

The SCA in *Zephan v Noormahomed* found that Zephan's reasoning to the effect that the section 155 Arrangement and Suraiya's receipt of interest payments from Orthotouch had novated Suraiya's rights under the Buy-Back Agreement was misconceived. The SCA accordingly held that the rights and obligations in terms of the Buy-Back Agreement had been unaffected and, in the same manner as the High Court, ordered Zephan to purchase Suraiya's shares as agreed.

### Conclusion

Through *Zephan v Noormahomed* and *Zephan v De Lange* our courts have provided an unequivocal statement on the relevance of business rescue proceedings and arrangements or compromises with creditors in terms of section 155 of the Companies Act on contractual arrangements similar to the ones we have observed in *Zephan v Noormahomed* and *Zephan v De Lange*.

The lesson in this regard is a clear affirmation to the effect that no rights or obligations under an agreement similar to the Buy-Back Agreement may be relinquished by either business rescue proceedings nor an arrangement or compromise with creditors in terms of section 155 of the Companies Act, unless such is expressly contained in the agreement. An agreement with similar arrangements as those of the Buy-Back Agreement concluded between parties and relating to a company which subsequently commences business rescue proceedings or enters into an arrangement or compromise with its creditors may not be affected by such proceedings or arrangements or by either party's participation in these proceedings unless clearly expressed and agreed to.

*Mondli Sithole and Nonhla Mchunu*

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