DISPUTE RESOLUTION

BUSINESS RESCUE, RESTRUCTURING & INSOLVENCY

NEWSLETTER

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CDH
CLIFFE DEKKER HOFMEYR

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Business Rescue,
Restructuring &
Insolvency

In what feels like a lifetime of a year of 2020, we find ourselves in October and at a stage where we can unbelievably say that there are only 78 days until Christmas.

As we reflect on this past year, we recognise that this may have been the most extraordinary year we will have had endured in our lifetime. And while we think that the only milestones we achieved this year was either packing on a few extra "*lockdown*" pounds, or on the other side of the spectrum, running a marathon in your garden, we have to appreciate that we have not been alone in this ordeal, and we can take comfort in knowing that come December, you may not be the only one considering going to the beach fully clothed.

On a more serious note, in recognising that we have all been affected by the extraordinary events of this year, we have seen many legislative and regulatory changes to accommodate and guide those who have found themselves in a worse off state as a result thereof.

We have seen a surge in business rescues and liquidation proceedings and as such, the CIPC and the courts have reacted accordingly. We have seen the CIPC provide for a suspension of their rights in terms of section 22 of the Companies Act, whereby they agreed to hold back on the issuing of notices in terms of section 22 in the case of a company which is temporarily insolvent and still carrying on business, where such temporary insolvency can be attributed to the effects of the COVID-19 pandemic.

Earlier this year, the CIPC drew up a Business Rescue Continuing Professional Development Policy which aimed to ensure that Business Rescue Practitioners (BRP) are aware of their responsibilities when applying to be a BRP and the future requirements to be considered. The policy focuses specifically on the roles, responsibilities, policy requirements, reporting period, monitoring and reinstatement expected of BRPs. With the surge in business rescues we have seen to date, and will continue to see in the next year, the policy is of vital importance as it will ensure that when BRPs are appointed, they are properly accredited and fully aware of their responsibilities in their capacity.

In this edition of our Insolvency Newsletter we will be looking at the case of *Chavonnes Badenhorst St Clair Cooper N.O and Another v Kurt Robert Knoop N.O and 6 Others* where we note how the courts have reacted to the effects of the COVID-19 pandemic and the subsequent liquidation and business rescue proceedings which have been brought before them. In this case we note the court's hesitation to flippantly grant an order interdicting the business rescue process from continuing and that the courts have tended to lean towards the side of assisting the distressed companies as far as possible. This has highlighted that a party bringing a liquidation application would have to be confident on their grounds for an application and ensure that a proper case is made out for a liquidation order to be granted.

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Sometimes you just gotta stick to the (business rescue) plan...

The primary rationale behind the introduction of the new business rescue procedure was to afford financially distressed companies the opportunity to restructure their affairs, with the purpose of enhancing their prospects of survival to the general benefit of stakeholders and the economy at large. In theory, one might assume that facilitating the continued existence of a financially distressed company, with the central aim of enhancing its prospects of survival, would be an end worth securing for all stakeholders, however, this is not the case.

What may prove beneficial to the stakeholders as a whole, does not invariably align with the individual interests of a creditor. That said, section 152(4) of the Companies Act 71 of 2008 (Companies Act) provides that once the duly published business rescue plan is voted on and subsequently adopted, it is binding on the company, each of its creditors and every holder of its securities, irrespective of whether such persons voted in favour of the plan.

Disgruntled creditors who are not in favour of a business rescue process may wish to bring a liquidation application against the company in business rescue, in order to vindicate their rights and interests for the recovery of the indebtedness owing to them.

This was the position in the recent case of *Chavonnes Badenhorst St Clair Cooper N.O and Another v Kurt Robert Knoop N.O and 6 Others*, where the aim of the application was to obtain an interdict against the section 151 creditors meeting until the winding-up application had been dealt with, given the adverse consequences that would result from the adoption and subsequent implementation of the business rescue plan.

The facts of the case and the important legal principles stemming from the judgment are discussed hereunder.

The facts

On 19 February 2018, Optimum Coal Mine (Pty) Ltd (OCM) was placed under business rescue. Pursuant to section 150(5) of the Companies Act, the appointed business rescue practitioners (BRPs) resolved to publish a revised business rescue plan (plan) on 11 September 2020. The BRPs sought to convene a meeting, the main purpose of which would be to put the plan to a vote as contemplated in section 151 of the Companies Act. Accordingly, the BRPs proposed that the meeting be held on 28 September 2020.

Prior to the publication of the plan, the liquidators of one of OCM's creditors, Westdawn Investments (Pty) Ltd (Westdawn), opposed the business rescue process proceeding in the ordinary course. In line with their opposition, on

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9 December 2019, they instituted an application for the provisional winding-up (liquidation application) of OCM, which would, in effect, have terminated the business rescue process if OCM was subsequently liquidated. In July 2020, the liquidation application was, however, still pending as the matter had only been set down for hearing on 24 November 2020. Alive to the possibility that the BRPs might publish the plan, Westdawn launched an urgent application for the liquidation application to be heard on 11 August 2020.

In a similar vein to their opposing counterpart, the BRPs opposed the urgent application, intimating that they would not publish a revised plan by the end of July, nor convene a meeting in early August for the purposes of putting the plan to a vote. Consequently, Westdawn withdrew the urgent application from the roll, and on 8 September 2020 the liquidation application was set down for hearing in the final week of November 2020. On 11 September 2020, three days after the liquidation application date had been secured, the BRPs published the revised plan, which in turn, precipitated the urgent application before the court.

Preliminary point- issue of non-joinder

Prior to dealing with the merits of the matter, the court disposed of several preliminary points raised by the BRPs, one of which bears consideration.

The BRPs raised the defence of non-joinder, on the basis that, Westdawn had not joined all the creditors as parties to the proceedings. In this regard, the kernel of their contention was that once the plan had been published, all of the creditors acquired a vested right to vote on the plan at the creditors meeting scheduled for 28 September 2020. This right, so the argument went, was sufficient to constitute a legal interest in the subject matter of litigation which may be prejudicially affected by the outcome of the proceedings – thus necessitating joinder.

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The court remarked that, although creditors acquire a variety of statutory rights upon the commencement of business rescue proceedings, the Companies Act did not necessitate joinder in all legal proceedings that potentially impact these rights. In this regard, the court pointed to the provisions of section 145 of the Companies Act, which read as follows:

> *"145(1) Each creditor is entitled to –*
>
> *(a) Notice of each court proceeding, decision, meeting or other relevant event concerning the business rescue proceedings;*
>
> *(b) Participate in any court proceedings arising during the business rescue process..."*

The court held that the provisions merely gave creditors the right to be apprised of the proceedings and the option to join, should they elect to do so, as opposed to making joinder a necessary procedural step. However, the court cautioned that section 145(1) did not supersede the common law on joinder, and that certain instances might, in fact, require joining all of the creditors as parties to the respective proceedings. That said, the court was not persuaded that the matter before it was one such instance.

The court however remarked that, once a business rescue plan has actually been adopted, all creditors must be joined in the application to have the business rescue plan set aside. In this regard, the court referred to the case of *Absa Bank v Naude 2016* (6) SA 540 (SCA) in which the SCA found that joinder is necessary in circumstances where a business rescue plan has been adopted, given that non-joinder would result in the position of creditors being prejudicially affected.

The court stated that once a business rescue plan is adopted, creditors acquire legal rights under it. These rights are directly related to the satisfaction of their claims against the company: they are substantive rights for the satisfaction of their claims, albeit that those claims may be compromised under the plan. The court indicated that the right to vote on a business rescue plan is different. It is a statutory right to participate in a process. It is inherently a right of a procedural nature, albeit that once a business plan is adopted by the exercise of the vote, more substantive rights flow from the plan.

Merits of the application – interdict sought against the BRPs

The court thought it necessary to consider the provisions pertinent to (i) the preparation of the plan; (ii) the BRPs' scheduling of the meeting; and (iii) the adoption and subsequent implementation of the plan. Section 150 placed an obligation on the BRPs to prepare the plan. In terms of section 151, the BRPs are then enjoined to *"convene and preside over a meeting of creditors and any other holders of a voting interest called for the purpose of considering the plan"* within 10 business days after its publication.

Thereafter, the BRPs must notify all affected persons within 5 business days of the date scheduled for the meeting. More importantly, in terms of section 152(4) once the plan is adopted it *"is binding on the company... [and] each of the creditors... whether or not such a person was present at the meeting [or] voted in favour of the adoption of the plan"*.

Notwithstanding the possibility of the meeting yielding a variety of outcomes, Westdawn contended that its adoption was, in fact, a foregone conclusion, hence the relief sought. Although not couched in clear and precise terms, the substance of what Westdawn sought, in terms of relief, was to obtain an interdict against the BRPs holding the meeting until the liquidation application had been heard.

The basis of Westdawn's case was that the BRPs had abused their powers by publishing the plan. It contended that the impetus behind the BRPs publishing the plan was not to discharge their statutory obligations, but rather, to prevent or obstruct the pending liquidation application. In this regard, Westdawn averred that the BRPs had acted with *"malicious forethought"* in instituting the mechanisms of section 151.

The court intimated that, Westdawn like any other applicant, would have to satisfy the trite requirements for interdictory relief. Although trite, the requirements bear repeating. An applicant must establish: (i) a *prima facie* right; (ii) a well-grounded apprehension of irreparable harm if the interdict is not granted and the ultimate relief is granted; (iii) a balance of convenience in their favour; and (iv) the absence of any other satisfactory remedy. The court stated that the requirements should not be considered in isolation, but rather, concurrently in order to determine whether interdictory relief ought to be granted.

Westdawn contended that its rights, as an aggrieved creditor, were undermined by the ostensibly untoward conduct of the BRPs who, according to Westdawn, sought to *"bolster the claims of the major creditors and... sideline the rights of the remaining creditors"*. As a result, unless the court rescinded the published plan, or alternatively, delayed the meeting until after the liquidation application, Westdawn's rights would be thwarted.

The court noted that Westdawn had not averred that they possessed a right to delay the vote, rather, they pegged their hopes on the alleged abuse of power by the BRPs. In this regard, the court found that the allegations proffered by Westdawn were ill-grounded. For example, Westdawn alleged that the BRPs had failed to canvass and consult on the plan with all the creditors before its publication, however, correspondence attached to the filed affidavits clearly showed that the BRPs made valiant attempts to consult with Westdawn on the development of the plans. As a result, the court concluded that Westdawn had failed to establish a *prima facie* right.

Westdawn further contended that it would suffer irreparable harm if the creditors meeting proceeded as scheduled, because the outcome, in its estimation, was a foregone conclusion. According to Westdawn, this would have a materially adverse effect on its pending liquidation application. To this end, Westdawn argued

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that it would be forced to join over 400 persons to the liquidation proceedings if the plan was adopted. Moreover, Westdawn argued that the balance of convenience was tipped in its favour, given that there was no urgency in putting the plan before the creditors. To corroborate this point, Westdawn stated that the plan contained several suspensive conditions that would, in effect, delay its adoption for at least 18 months. This notwithstanding, upon the implementation of the plan (Effective Implementation Date), Westdawn would lose its claim against OCM together with its locus standi in the liquidation application as a consequence thereof.

Once again, the court found that the justifications advanced by Westdawn were factually unfounded. For example, the BRPs submitted that the Effective Implementation Date depended solely on the suspensive conditions being fulfilled. To this end, they argued that the suspensive conditions would not be fulfilled with any haste, as they were subject to certain regulatory approvals. To allay Westdawn's ostensible apprehension of irreparable harm, the BRPs went as far as providing an undertaking to Westdawn and the court that they would, *inter alia*, (i) not challenge Westdawn's status as a creditor; and (ii) ensure that the suspensive conditions were not fulfilled or waived by the date of the liquidation application.

The court held that the undertakings effectively thwarted any prospect of Westdawn suffering irreparable harm. It further held that, when considering where the balance of convenience lies, due regard must be given to "*the interests of the general body of creditors, and... the public interest, in ensuring that the business rescue process is not unnecessarily impaired*". The court concluded that there was no sound justification for halting the business rescue process, given that it could run concurrently with the liquidation application. As a result, the balance of convenience tipped in favour of putting the plan to the vote. Consequently, the application was dismissed.

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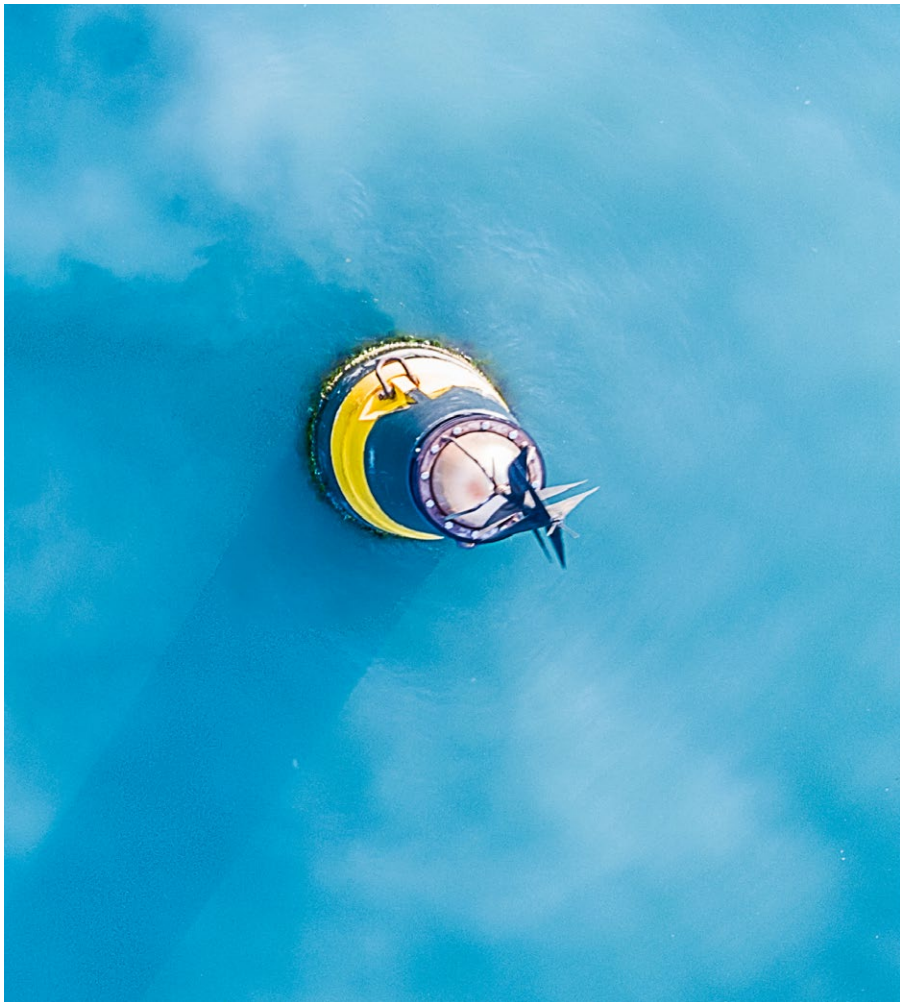

Conclusion

Regarding the issue of non-joinder, it is important to note that although creditors acquire various statutory rights once business rescue proceedings have commenced, the Companies Act does not require that they be formally joined as parties in all legal proceedings which may impact on their statutory rights. In terms of section 145(1) of the Companies Act, creditors are entitled to notice of proceedings. It is then for a creditor to decide whether they wish to formally join the proceedings.

Where the relief sought is simply to delay the exercise of a vote on a plan, this would not ordinarily require the formal joinder of all creditors. However, if the plan was already adopted, the creditors would need to be formally joined as parties to the proceeding, as they have vested rights for the satisfaction of their claims under the proposed business rescue plan.

In terms of the issue of establishing a *prima facie* right, applicants must take heed of the fact that they cannot merely rely on the alleged abuse of power by the BRPs of a company in business rescue, they need to go further and substantiate the allegations with the necessary facts.

Lastly, the judgment demonstrates that courts are generally 'bending over backwards' to assist companies in business rescue. Many judgments handed down during the course of this year in the midst of the COVID-19 pandemic reflect that our courts will assist companies in business rescue to the extent possible (and legal) and will further guide the way in allowing a company to fully harness the procedural and substantive protections of Chapter 6 of the Companies Act, even when there is a pending liquidation application.

For example, the judge in this case stated that: *"[i]t is important to bear in mind that all creditors have an interest in the business rescue process taking its course. The statutory scheme places obligations on BRPs to guide that process forward. The scheme does not give some creditors the right to stall the vote on a business rescue plan because of a pending, competing winding-up application."*

It is therefore important for applicants who wish to bring liquidation proceedings against a company in business rescue, to bring the application at the right time and to make sure that a proper case for liquidation has been made out. It is particularly important for an applicant not to delay bringing the liquidation application should there indeed be no reasonable prospect of rescuing the company. For example, if it is abundantly clear from the first meeting of creditors that the company is hopelessly insolvent and there are no reasonable prospects of rescuing the company, the applicant should consider bringing the liquidation application immediately and not waiting until the publication or the adoption of the plan, as this is where the issues as set out in the above judgment start arising.

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BBBEE STATUS: LEVEL TWO CONTRIBUTOR
Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

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