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BUSINESS RESCUE, RESTRUCTURING & INSOLVENCY

NEWSLETTER

DISPUTE RESOLUTION

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Since the introduction of business rescue proceedings into South African law in 2011, many companies have jumped at the opportunity to “rescue” their businesses. Business rescue quickly became the favoured approach for companies who found themselves in dire financial straits – allowing them one last shot at economic redemption before the liquidation hangman comes knocking at their door.



INCORPORATING
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Despite us ceremoniously throwing away our masks to mark the possible end of COVID-19 for good, it seems like our economy is certainly in for a bumpy ride post-COVID. The start of July saw the fall of the temporary R1.50 reduction in the general fuel levy from Government and a steep petrol price hike with record-high petrol prices. The nation has also been plunged into new stages of darkness with Stage 6 loadshedding being utilised by Eskom in an attempt to protect the nation's grid in light of labour action and to combat further capacity constraints. Despite the tough times we are facing, we remain cautiously optimistic and hold onto the South African spirit of resilience. We, as the CDH Business Rescue, Restructuring and Insolvency Sector, welcome the challenge to assist our clients in these trying times.

In recent times, much has been discussed regarding the granting of the provisional winding-up order of Comair. The business rescue practitioners (BRPs) concluded that business rescue proceedings had failed and filed for the provisional liquidation of the airline. All affected parties have until 26 July 2022 to oppose the granting of a final liquidation order. Attention will certainly be tuned into the proceedings at the Johannesburg High Court on 26 July.

Despite Comair's misfortune, it appears the airline industry has risen to the occasion to meet demand as South Africans adapt to the easing of COVID-19 restrictions, which will hopefully boost the tourism and travel industry despite another airline entity possibly facing the clipping of its wings.

In other news, JSE-listed Huge Group is buying Virgin Mobile South Africa, now trading as Tethys Mobile. Tethys has been in business rescue since September 2020. Huge Group has pledged a cash injection into Tethys that will preserve jobs and aid the entity in its switch from providing consumer mobile services to providing software and technology platform services. For the cinema fans, Ster-Kinekor's BRP has stated that there are still reasonable prospects of rescuing the cinema operator. An amended business rescue plan has been implemented with further financial gain in the release of blockbuster movies such as Jurassic World, Dr Strange and Tom Cruise's 36-year-later return to the Top Gun franchise in 2022's highest-grossing film Top Gun: Maverick.

Many companies would prefer to hold onto the hope that there is a light at the end of the tunnel and opt for business rescue proceedings where possible. However, it is important to realise that the choice between the two is not one that can be made willy-nilly and business rescue is not an option that is available in all circumstances. In our latest newsletter, we explore the conversion of business rescue proceedings into liquidation proceedings with an analysis of the difference between both by Lucinde Rhoodie and Kara Meiring.

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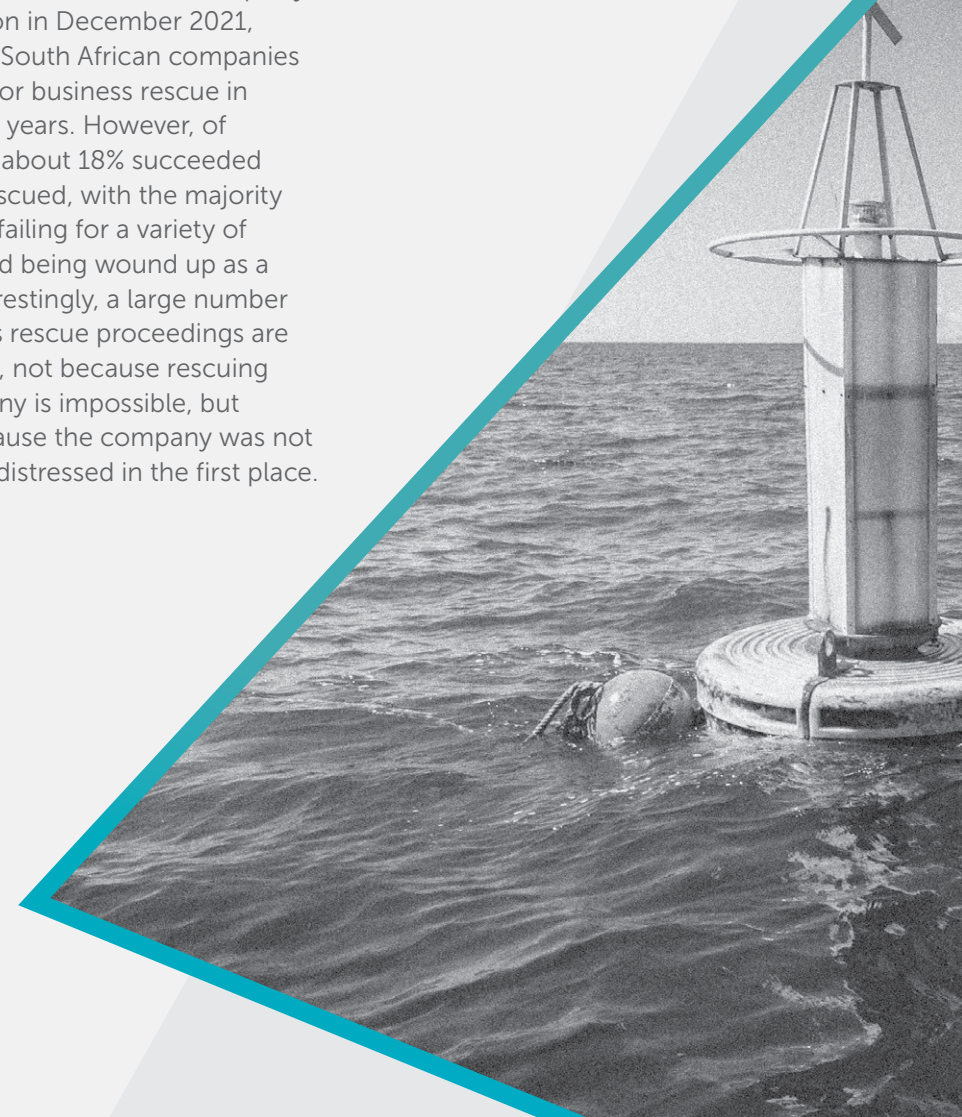
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From one foot in the grave, to buried: Converting business rescue proceedings into liquidation

Since the introduction of business rescue proceedings into South African law in 2011, many companies have jumped at the opportunity to “*rescue*” their businesses. Business rescue quickly became the favoured approach for companies who found themselves in dire financial straits – allowing them one last shot at economic redemption before the liquidation hangman comes knocking at their door.

According to a report published by the Companies and Intellectual Property Commission in December 2021, over 4,215 South African companies have filed for business rescue in the past 10 years. However, of those only about 18% succeeded in being rescued, with the majority eventually failing for a variety of reasons and being wound up as a result. Interestingly, a large number of business rescue proceedings are terminated, not because rescuing the company is impossible, but rather because the company was not financially distressed in the first place.



From one foot in the grave, to buried: Converting business rescue proceedings into liquidation

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BUSINESS RESCUE VERSUS LIQUIDATION: WHAT'S THE DIFFERENCE?

When a company becomes financially distressed, it is not always obvious whether the business rescue or liquidation route should be followed. Many companies would prefer to hold on to the hope that there is a light at the end of the tunnel, and would therefore opt for business rescue proceedings where possible. However, it is important to realise that the choice between the two cannot be

made willy-nilly and business rescue is not an option that is available in all circumstances. Instead, the purpose and process for each option needs to be considered and the context surrounding the company's financial distress has to be taken into account in order to determine which one is the better choice. Directors must always be aware of the obligation placed on them in terms of section 129(7) of the Companies Act 71 of 2008 (Companies Act), which provides that if the board of directors has reasonable grounds to believe that a company is financially distressed, but the board has not adopted a resolution to place it in business rescue, the board must deliver a written notice to each affected person, setting out why it regards the company to be financially distressed and its reasons for not adopting a resolution placing the company under business rescue. Failure by the board to comply with the provisions of this section may attract liability for the directors.

Business rescue proceedings are aimed at either "*rescuing*" a company (i.e. ensuring that the company gets back to being commercially solvent and continuing its business activities) or to ensure a better return for the creditors than in a liquidation scenario. Business rescue is defined in section 128(1)(b) of the Companies Act, as a procedure "*to facilitate the rehabilitation of a company that is financially distressed*". The key here is that the company must actually be capable of being rescued and there must ideally be some prospect of continued commercial activities. Some money, as opposed to no money, is perhaps an easy rule of thumb.

In contrast, liquidation is the process whereby both solvent and insolvent companies are wound-up, either voluntarily or as a result of a court order. The effect of liquidation proceedings is essentially the opposite of business rescue, in that the company ceases to operate and its legal existence is terminated, along with any and all of its obligations or liabilities.



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MOVING FROM BUSINESS RESCUE TO LIQUIDATION

Of the companies that filed for business rescue over the last 10 years, at least 511 of them ended up collapsing into liquidation (this does not include an additional 310 business rescues that were declared invalid from the outset and may have ended up in liquidation as well). The conversion of business rescue proceedings into liquidation proceedings is not something that is done lightly, as it inevitably means that a company has lost its last hope of being saved and can have devastating consequences for employees, directors and shareholders alike.

It is ultimately the business rescue practitioner who initiates the process of converting business rescue proceedings into liquidation proceedings, if they are of the view that there is no reasonable prospect of the company being rescued. Section 141(2) of the Companies Act requires business rescue practitioners, if they conclude that the company

is incapable of being rescued at any point during the business rescue proceedings, to (i) inform the court, the company and all affected persons and (ii) apply to the court for an order discontinuing the business rescue proceedings and placing the company into liquidation. Once a business rescue practitioner applies for a liquidation order, it is likely that the court will be inclined to grant such an order, especially given that the business rescue practitioner would have an in-depth understanding of the company's financial position and would not bring such an application if there was still some prospect of the company being rescued. Our courts have also taken an obiter view that in certain instances the court has the power to intervene in business rescue proceedings and order the winding up of the company, such as in circumstances where the business rescue practitioner has been shown to have committed material errors in its running of the business rescue proceedings.

CONCLUSION

The hope for all companies who file for business rescue is that they will eventually be rescued. Similarly, business rescue practitioners commence their role with the ultimate goal of saving a distressed company. However, the Companies Act places an obligation on them to admit defeat when there is truly no prospect of rescuing the company. A failure to do so (i.e. to notify the court and apply for liquidation), or to resign as practitioner, is a breach of the duties provided for in the Companies Act and therefore leaves the practitioner with no choice but to terminate the business rescue and commence liquidation.

**LUCINDE RHOODIE
AND KARA MEIRING**



OUR TEAM

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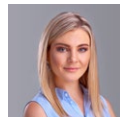
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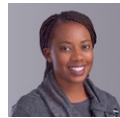
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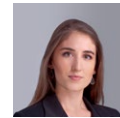
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Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

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