

# “BUSINESS RESCUE PROCEEDINGS”

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## Rehabilitation Tool

Section 128 (1) (b) of the Companies Act 71 of 2008 (the “Companies Act”) defines business rescue as “*proceedings to facilitate the rehabilitation of a company that is financially distressed*”, this is done by restructuring its affairs, business, debt, property and other liabilities including equity.

## Introduction to Business Rescue

The vast number of companies in financial distress is on the rise in South Africa and this has led to the introduction of Business Rescue as regulated by Chapter 6 of the Companies Act. Such relief was a much needed alternative to liquidation proceedings, as no alternative existed prior to the introduction of Business Rescue in relation to distressed companies. Despite Business Rescue being a necessitous instrument it is still fairly new to our Law and as such certain aspects remain contentious, and will most likely find resolution in Court. Business Rescue commences by the passing of a resolution by the Board of the company and subsequently appointing a Business Rescue Practitioner (“BRP”).

## Payment Moratorium

Section 133 of the Companies Act places a moratorium on all legal proceedings which are imminent prior to the company filing for Business Rescue, save where the court or BRP grants consent to institute any legal proceedings. Section 133 safeguards the company from any legal proceedings and other related costs, it also enables the company to expand on its operations and improve on its finances. The aim of the moratorium is to offer breathing space to a BRP thus enabling them to investigate the business affairs of the distressed company, it provides them with sufficient time to consult with the Directors, Employees and Creditors and develop a Business Rescue Plan for the financially distressed company.

## Delay Tactic?

A concern which has arisen on several occasions in respect of Business Rescue is that there is a firm belief that this process is used as a delay tactic by various companies. The use of this regime as a delay tactic enables companies to move the company assets and as a result the company creditors have no recourse against the company for debts owed to the creditors.

Certain companies have also utilized Business Rescue as a means of obtaining a temporary respite from creditors thereby abusing such regime, nevertheless the Companies Act provides certain procedural requirements in order to combat the abuse displayed by companies in this regard.

## Advantages of Business Rescue

Apart from all the contentious issues displayed above in relation to Business Rescue there are advantages which are indicated below:

- Creditors can make a greater return on the outstanding debts considering that the aim is to place creditors in a more favourable situation;
- In the event that the Business Rescue is successful, the company is able to operate on a solvent basis however, this is applicable only if the business creditors have agreed to write off a certain portion of the company’s debt;
- It allows not only for the preservation of the company employees, but it also limits employment losses.
- It allows for the preservation of certain assets of the company;
- the BRP may suspend any agreement or provision contained in an agreement to which the company was a party to, be it entirely, partially or conditionally however, this specifically excludes employment contracts; and
- It is a process that promotes the continued existence of a financially distressed but nevertheless sustainable company.

## Disadvantages

Disadvantages always presents itself; the following have been indicated as disadvantages in utilizing the Business Rescue regime:

- The company undergoing Business Rescue would be susceptible to negative publicity;
- Financial institutions become reluctant in granting distressed companies finance, in certain instances there is a suspension of facilities by the financial institutions; and

- Business Rescue may not be viable for each and every company that is financially distressed, in the event that the prospect for rescuing the company is low there is no need to institute Business Rescue. Various factors play a role in determining the viability, one of the key factors is whether there is an overwhelming amount of debt in which case the better option for the Creditors and Shareholders would be liquidation.

### **Liquidation and Business Rescue**

Liquidation proceedings involves the process of shutting down a company and subsequently disposing of its assets, the proceeds are then utilized to pay the creditors in terms of a legal order of preference and settle the company's debts. The main focus of Business Rescue is to assist financially distressed companies return to its profitability and save the business as a going concern; in addition it aids in facilitating the settlement of various claims against the business however, in some cases where this is not feasible i.e. where the company has an overwhelming amount of debt then a more advantageous option would be liquidation.

In respect of initiation of both Liquidation Proceedings and Business Rescue Proceedings both can be initiated by way of an application to the court by creditors and other affected parties or voluntarily by the board of directors adopting a resolution.

In the case of a liquidated company the creditors suffer as their returns are far less than that of a company which has instituted Business Rescue Proceedings. Nonetheless liquidations furnished creditors with more certainty in respect of the status of claims as opposed to Business Rescue.

The objective of Business Rescue is to maximize the likelihood of the company continuing in existence on a solvent basis and to acquire a better return for the company's employees, creditors and shareholders as opposed to the result that would be obtained from liquidating the company.

In the event that the Board of Directors adopt a resolution to voluntarily commence with Business Rescue Proceedings it is prohibited from adopting a resolution to commence with Liquidation Proceedings however, in the event that business rescue proceedings have already commenced and the court is of the view that rehabilitation is highly unlikely, the court may then order that the company rather be liquidated.

### **Business Rescue Plan**

Section 150 of the Companies act sets out the framework with which the Business Rescue Plan must comply with. The purpose of setting out this framework is to ensure that the Business Rescue Plan contains sufficient detail for all affected persons to make an informed decision on whether or not the Business Rescue Plan is viable. As the Business Rescue Plan must be set out in 3 (three) parts:

#### • **Part A Background**

- List of material assets and an indication of which assets were held as security by creditors at commencement of Business Rescue Proceedings;
- List of creditors to the company and each creditors rank in relation to other creditors (preferent, secured, unsecured, concurrent) and an indication of which creditors need prove their claims;
- Probable dividend to creditors if the company were to be liquidated;
- Complete list of holders of company securities;
- Copy of the written agreement concerning the BRP's remuneration; and
- A statement whether the Business Rescue Plan includes a proposal made informally by a creditor of the company.

#### • **Part B- Proposals**

- The nature and duration of any moratorium for which the business rescue plan makes provision;
- The extent to which the company is to be released from the payment of its debts, and the extent to which any debt is proposed to be converted to equity in the company, or another company;
- The ongoing role of the company, and the treatment of any existing agreements;
- The property of the company that is to be available to pay creditors' claims in terms of the business rescue plan;
- The order of preference in which the proceeds of property will be applied to pay creditors if the business rescue plan is adopted;
- The benefits of adopting the business rescue plan as opposed to the benefits that would be received by creditors if the company were to be placed in liquidation; and
- The effect that the business rescue plan will have on the holders of each class of the company's issued securities.

#### • **Part C- Assumptions and Conditions**

- The nature and duration of any moratorium for which the business rescue plan makes provision;
- The extent to which the company is to be released from the payment of its debts, and the extent to which any debt is proposed to be converted to equity in the company, or another company;

- o The ongoing role of the company, and the treatment of any existing agreements;
- o The property of the company that is to be available to pay creditors' claims in terms of the business rescue plan;
- o The order of preference in which the proceeds of property will be applied to pay creditors if the business rescue plan is adopted;
- o The benefits of adopting the business rescue plan as opposed to the benefits that would be received by creditors if the company were to be placed in liquidation; and
- o The effect that the business rescue plan will have on the holders of each class of the company's issued securities

### **Conclusion**

Caution should be exercised when considering Business Rescue Proceedings as such regime is not a means of avoiding debt but rather providing a distressed company with a "second chance" by providing a company with an opportunity to trade its way out of the financial predicament it holds with the aid of a BRP.

Not all financially distressed companies can be rescued by this regime and various factors need to be considered prior to making a decision, as such the decision to embark on Business Rescue should ultimately be a realistic one.