WERKSMANS
ATTORNEYS

INSOLVENCY & BUSINESS RESCUE

The duty to disclose business rescue proceedings

2 June 2016 *7 min read*

On 14 April 2016, the Supreme Court of Appeal ("SCA") in the matter of *Umso Construction Proprietary Limited ("Umso") v MEC for Roads and Public Works Eastern Cape Province Responsible for the Road and Transport ("MEC Eastern Cape")* (case number 20800/2014) ZASCA 61) delivered a judgment relating to the duty of a party to disclose business rescue proceedings. The SCA concluded that the failure to disclose that the company (Tau Pele Construction Proprietary Limited ("Tau Pele")) was under business rescue during the adjudication process of the tender nullified the award of the tender to the company and ought to be set aside on that basis.

INTRODUCTION

This case was an appeal of a decision of the High Court of South Africa, Eastern Cape Local Division, Bhisho. One of the questions the SCA was called upon to decide was whether a successful bidder had a duty to disclose business rescue proceedings, within the context of a tender process.

THE RELEVANT FACTS

Tau Pele, having been awarded the tender to upgrade the gravel road between Elitheni Coal Mine and the R56 road in the Chris Hani district of Eastern Cape ("Project") on 27 May 2013, was placed under business rescue on 17 September 2012, a date after the tender advertisement (the tender was advertised on 27 July 2012) and the closure of the bids (tender closed on 8 August 2012). The tender advertisement provided that the department would only consider submissions from bidders who can satisfactorily prove that they have the necessary financial resources to undertake and complete the Project.

The business rescue proceedings were successfully implemented and completed on 21 May 2013, a date before the tender was awarded to Tau Pele. Umso, having been the unsuccessful bidder, applied for a review in terms of the Promotion of Administrative Justice Act 3 of 2000, to set aside the award to Tau Pele. Umso disclosed in its affidavit that Tau Pele was placed under business rescue during the period mentioned above and that this fact was never disclosed to the MEC Eastern Cape.

The MEC Eastern Cape supported Umso application to review and set aside the award of the tender to Tau Pele. The MEC Eastern Cape submitted that the circumstances surrounding Tau Pele's financial difficulties, and in particular the fact of business rescue, was information which ought to have been disclosed during the evaluation process.

It was argued on behalf of Tau Pele that the company had no duty to disclose that it was under business rescue from 17 September 2012 to 21 May 2013, on the grounds that the company had no legal relationship with the MEC Eastern Cape at the commencement of its business rescue and if such duty existed, it would undermine the purpose of business rescue i.e to rehabilitate a company that is financially distressed.

THE COURT A QUO'S DECISION

The court a quo set aside the tender award in favour of Tau Pele. The court held that it is reasonable to conclude that when the bids closed on 8 August 2012, Tau Pele was in the full throes of applying for business rescue, but was only able to vouch for the success of the rescue plan during or about the time that rescue was terminated. The court reasoned that –

- when Tau Pele submitted the bid for the Project, it was already financially distressed as envisaged in its application papers for the business rescue relief and followed the prescribed steps to apply for business rescue;
- even though the duty to disclose this information existed at the time of submitting its bid, the business rescue practitioner should have communicated this to the MEC Eastern Cape via correspondence at the time it commenced business rescue proceedings; and
- the MEC Eastern Cape as the investor should have been afforded the opportunity to consider Tau Pele's financial position, together with other relevant considerations before finally awarding the tender to it.

THE SCA'S JUDGEMENT

The SCA rejected the argument advanced on behalf of Tau Pele and confirmed the lower court's decision that the tender award in favour of Tau Pele fell to be side aside, on the basis that Tau Pele failed to disclose the business rescue proceedings at its commencement or at very latest when the company entered into business rescue.

The SCA strongly expressed the view that Tau Pele had a duty to disclose its business rescue proceedings to the MEC Eastern Cape (notwithstanding, the fact that it had no legal relationship with the department), at the commencement and termination of the business rescue. The SCA held the following –

- the duty to disclose the financial status of the company and prove that the company had the financial resources to undertake and complete the work as required by the tender advertisement, explicitly imposed a duty to disclose the business rescue proceedings during the adjudication process;
- the fact that the company was successfully placed under business rescue meant that the company was financially distressed before the awarding of the tender and that such fact was material and fell outside the tender conditions and as a result the company could have been disqualified from the onset;
- the failure to disclose business rescue proceedings constituted a misrepresentation of a material fact, which fact the MEC Eastern Cape relied upon in its adjudication of the tender;
- the failure to recognise the duty to disclose business rescue proceedings seriously undermined and prejudiced the tendering process; and
- there was a huge amount of public money involved in the tendering process, which required the importation of the duty to disclose business rescue proceedings.

The tender awarded in favour of Tau Pele was accordingly set aside on the basis that it failed to disclose that the company was placed under business rescue during the adjudication process of the tender.

Despite, the fact that at the time of the submission and the closure of the tender, Tau Pele was not placed under business rescue, the SCA held that Tau Pele's financial position changed materially and thus, the company bore the duty to disclose that fact.

The SCA concluded (without taking into consideration that the business rescue proceedings were successfully implemented) that at the time Tau Pele tendered for the project, it was already financially distressed. Had this fact been disclosed to the Eastern Cape, it could have been disqualified because the tender advertisement clearly stated that the MEC Eastern Cape would only consider bidders which had the financial means to undertake and complete the Project. Accordingly, it could not have been in the public interest to withhold this fact, especially where the Project was funded by the public money.

The SCA did not entertain the submission that if such duty existed, it could undermine the very purpose of business rescue, that is to rescue companies that were financially distressed.

CONCLUSION

Although the above case emphasised the duty to disclose the company's financial status (including the commencement of business rescue proceedings) and to update an interested party in the event of such financial information changing materially, it certainly poses a greater difficulty for companies that have been placed under business rescue, irrespective of whether or not the proceedings were implemented and completed successfully.

A company will not only have to disclose its current financial status, but also disclose that the company has or is to be placed under business rescue while awaiting the adjudicating committee's decision.

Download



Eric Levenstein

Head of Insolvency & Business Rescue

View Profile