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INSOLVENCY & BUSINESS RESCUE

Time to amend the Business Rescue Act?

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Business rescue was introduced into our law in May 2011. But is it time for an overhaul?

The business rescue legislation has been in place for over five years and has resulted in a plethora of judgments from the South African courts. And despite varying interpretations of the provisions of the business rescue legislation, our courts have provided well thought out judgments which has created confidence in business rescue mechanisms.

INTRODUCTION

This has resulted in an effective business rescue mechanism which provides a unique option for saving companies that were teetering on the brink of insolvency. Placing companies into liquidation, with resultant job losses, general negativity and the stigma attached to such liquidation process was never a positive outcome for the South African economy. Business rescue now provides a fresh option. And one which needs to be taken on board by all stakeholders involved in the company that is financially distressed.

In recently completing my doctoral thesis, I appraised the South African business rescue procedure to see it aligns itself with international corporate rescue regimes applicable in countries such as the United States, the United Kingdom, Australia and Canada.

All of the core features, themes and international concepts of rescue have been included in the local legislation. These include the imposition of a moratorium (breathing space) on claims to allow the company to be restructured without the impending pressure of court cases, execution against the company's assets and potential liquidation applications.

It also includes the introduction of the professional business rescue practitioner who is obligated to take control of the company (together with its board of directors). A practitioner would provide a fresh view of the company's prospects and whether or not it has a realistic prospect of trading its way out of its insolvent position.

Management and the board of directors work alongside the practitioner in achieving the goal of restructuring, allowing the company to be placed back on its feet and to re-enter the South African economy without the destruction of value and resultant job losses. As in foreign jurisdictions, South African business rescue legislation now provides the company with the opportunity to continue trading on a solvent basis, alternatively distributing a dividend to creditors that would be better than what would occur in a liquidation.

We have seen many examples where financially distressed companies have been rescued. These include Pearl Valley Golf Estate, Southgold Gold Mine, Advanced Technologies and Engineering Company, Ellerines, Moyo Restaurants and recently, Optimum Coal Mine. In many of these examples, creditors have exited from the business rescue process successfully, with business rescue dividends being paid well in excess of what creditors would have received in liquidation. This outcome remains in line with international models of successful reorganisations or rescue processes.

But there have been failures too: not every company is a candidate for business rescue. Despite the effectiveness of business rescue, the opportunity remains for changes and amendments to the legislation.

Such recommended changes include the necessity to impose upon the practitioner the need for a pre-assessment of the company's prospects of success in the business rescue process, prior to the commencement of business rescue. Such pre-assessment would allow a practitioner to provide a detailed pre-assessment report to all stakeholders, including creditors and the board of directors. This would alleviate the pressure placed on directors where only they will have to make the decision to place the company into rescue.

Such report by an independent practitioner would allow the board of directors to be placed in a far better position to determine whether or not such company should enter the business rescue process. Furthermore, it is suggested that there should be an analysis of financial distress conducted by a legal and accounting team prior to the board considering a resolution for the commencement of business rescue. Such report should be peremptory and should be prepared and submitted to the board for proper deliberation before a decision is made that the company is financially distressed and should then follow the business rescue route.

Other recommendations include proper training and formal accreditation of practitioners (in conjunction with the Commission for Intellectual Property and Companies (CIPC)). Such initiatives would go a long way in improving the standard and quality of the practitioner who is appointed to a company in business rescue. It has further been proposed that the CIPC accredits certain professions which, if a practitioner belongs to such profession, provides the practitioner with the prospect of being licensed to act as a business rescue practitioner.

Another suggested improvement is that the new legislation allow practitioners to formally interrogate directors, management, staff and any other person who can assist the practitioner in investigating the affairs of the company. This would enable quick assessment of whether the financial distress was bad management or whether there are other factors at play.

Within the current business rescue framework, it is often the case that formal dispute resolution mechanisms need to be introduced where ongoing and protracted disputes, which might hamper the success of the business rescue process, be resolved in a speedy fashion. Protracted litigation delaying the ultimate discharge of the company from its business rescue process is a frustrating prospect.

It is also recommended that the role of the CIPC should be enhanced to deal with proper scrutiny of the reasonable prospects for rescue of the company, better policing of dishonest, incompetent practitioners.

The legislation further needs to clarify the ranking of post-commencement finance. Whoever provides finance to a company in business rescue should potentially rank ahead of all other creditors (including secured creditors) so as to enable the company to continue trading and to pay expenses in the ordinary course of business. Despite certain judgments, this remains an uncertain area of the legislation.

CONCLUSION

Business rescue is here to stay. The South African government has been bold and innovative in introducing this rescue legislation and South Africans should embrace the new dispensation. Enhancements and amendments would certainly contribute to an even more effective implementation.

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