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A black and white photograph of a man in a suit and tie, holding a briefcase, standing on a rocky cliff overlooking the ocean. The sky is overcast.

LEGAL CONSEQUENCES – THE GENERAL MORATORIUM ON LEGAL PROCEEDINGS AND THE PROTECTION OF PROPERTY INTERESTS

05



Presented by

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Overview of the timelines in business rescue

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General moratorium on legal proceedings – section 133

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Exceptions to the moratorium

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Overview of the timelines in business rescue

- Directors' duties (section 142(1)(2)) –
 - The directors are required to provide the Business Rescue Practitioner with all books and records of the company as soon as practicable after the commencement of business rescue.
 - Statement of affairs to Business Rescue Practitioner within 5 business days of the commencement of business rescue.
- Business Rescue Practitioner (section 140(1A)) –
 - As soon as possible after appointment, Business Rescue Practitioner must inform all regulatory authorities of the commencement of Business Rescue.
- Creditors & employees' meetings (sections 147(1) and 148(1)) –
 - Within 10 business days of being appointed, the Business Rescue Practitioner must give notice of, convene and preside over separate meetings of the creditors and employees of the company.
- Meeting to consider the plan (section 151(1)(2)) –
 - Within 10 business days after publishing a business rescue plan, the Business Rescue Practitioner must convene and preside over a meeting of creditors and any other holders of a voting interest, for the purpose of considering the plan.
 - At least 5 business days before the meeting, the practitioner must deliver a notice of the meeting to all affected persons, setting out the date, time, and place of the meeting, the agenda, and a summary of the rights of the affected persons to participate and vote at the meeting.



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Moratorium on legal proceedings

- Prevents legal proceedings and enforcement actions from being instituted or proceeded with, against the company or in respect of property belonging to the company or lawfully in its possession
- Designed to provide the company with "breathing space" while the business rescue practitioner attempts to rescue the company through the preparation and implementation of the business rescue plan
- Without this element, a creditor would be able to enforce its rights during the process or apply for the liquidation of the company
- **Section 133(1) of the Companies Act**
- During business rescue proceedings, no legal proceeding against the company, including enforcement action, or in relation to any property belonging to the company, or lawfully in its possession may be commenced in any forum **except** –
 - with the written consent of the practitioner,
 - with the leave of the court and in accordance with any terms the court considers suitable,
 - as a set-off against any claim made by the company in any legal proceedings, irrespective of whether those proceedings commenced before or after the business rescue proceedings began,
 - criminal proceedings against the company or any of its directors or officers.



Moratorium – Section 133

Merchant West Working Capital Solutions (Pty) Ltd v Advanced Technologies and Engineering Company (Pty) Ltd and Another [2016] JOL 36732 (GSJ)

- The meaning of "legal proceedings" must be given its ordinary every day meaning"
- "legal proceedings" construed widely and includes arbitration proceedings

Chetty t/a Nationwide Electrical v Hart NO and another 2015 (6) SA 424 (SCA)

- Facts: arbitration hearing involving a contractual dispute relating to a building contract. Arbitrator made an award against Chetty in favour of the Company in business rescue. Chetty applied to the court a quo to nullify proceedings on basis that at the time of the award she was unaware that the company was in BR, which resulted in her failure to seek consent from Business Rescue Practitioner to continue with the arbitration
- Court a quo: legal proceedings as contemplated in s133 referred to court proceedings only and not to arbitrations
- SCA Held – arbitration proceedings are indeed legal proceedings for purposes of s133(1). Purpose of moratorium is to give Business Rescue Practitioner breathing space to get the company's financial affairs in order
- Legal proceedings to be construed widely – arbitrations like court proceedings involve a diversion of resources including time and money that may hinder the effectiveness of BR proceedings



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Exceptions to the Moratorium – S 133(1)(a)-(f)

1. With the written consent of the practitioner
2. With the leave of the court – must be well motivated (Redpath Mining South Africa (Pty) Ltd v Marsden NO & Others (18486/2013) [2013] ZAGPJHC 148 (14 June 2013))
3. As a set-off against any claim made by the company in legal proceedings, irrespective of when the proceedings commence
4. Criminal proceedings against the company/directors/officers
5. Proceedings concerning any property or right over which the company exercises the powers of a trustee
6. Proceedings by a regulatory authority in the execution of its duties after written notification to the practitioner



Exceptions to the Moratorium – S 133(1)(a)-(f)

Moodley v On Digital Media & Others 2014 (6) SA 279 (GJ) (11 July 2014)

- Moratorium does not apply to proceedings to set aside the business rescue plan and to interdict the implementation of the business rescue.
- Confirmation that Section 133(1) is not an absolute bar to legal proceedings against a company in business rescue

Arendse and Others v Van der Merwe NO and Another 2016 (6) SA 490 (GJ)

- Senior Executives (Applicants) were employed by Ellerine Furnishers Proprietary Limited and concluded Performance Incentive Scheme Agreements
- Applicants brought an application to institute legal proceedings against Ellerine Furnishers, African Bank Investments Proprietary Limited and Ellerine Holdings Limited to realise the debt owed in terms of the agreements
- Each of the defendants denied liability
- Case became moot as business rescue proceedings came to an end, but the court held in terms of section 133(1) that the moratorium on legal proceedings is not an absolute bar against legal proceedings
- The court has a wide discretion to grant leave to proceed based on the interests of justice
- All the applicants need show is that one or the other of the defendants is legally liable and that there is a prima facie case made out
- It must be noted that the business rescue procedure cannot be used by companies to avoid their obligations by taking improper advantage of the moratorium against legal proceedings provided for under section 133(1)



Exceptions to the Moratorium – S 133(1)(a)-(f)

Gormley v West City Precinct Properties (Pty) Ltd and Another, Anglo Irish Bank Corporation Ltd v West City Precinct Properties (Pty) Ltd and Another (19075/11, 15584/11) [2012] ZAWCHC 33 (18 April 2012)

- Application for business rescue based solely on achieving a moratorium against legal proceedings being brought by the largest creditor and to achieve a better return for creditors
- Company owed the Bank R219 million in terms of a loan agreement
- Court held that the company was not financially distressed and in any event the business rescue plan would be rejected by the bank as the creditor with the most voting rights
- Therefore, business rescue cannot be used as a means of staying obligations



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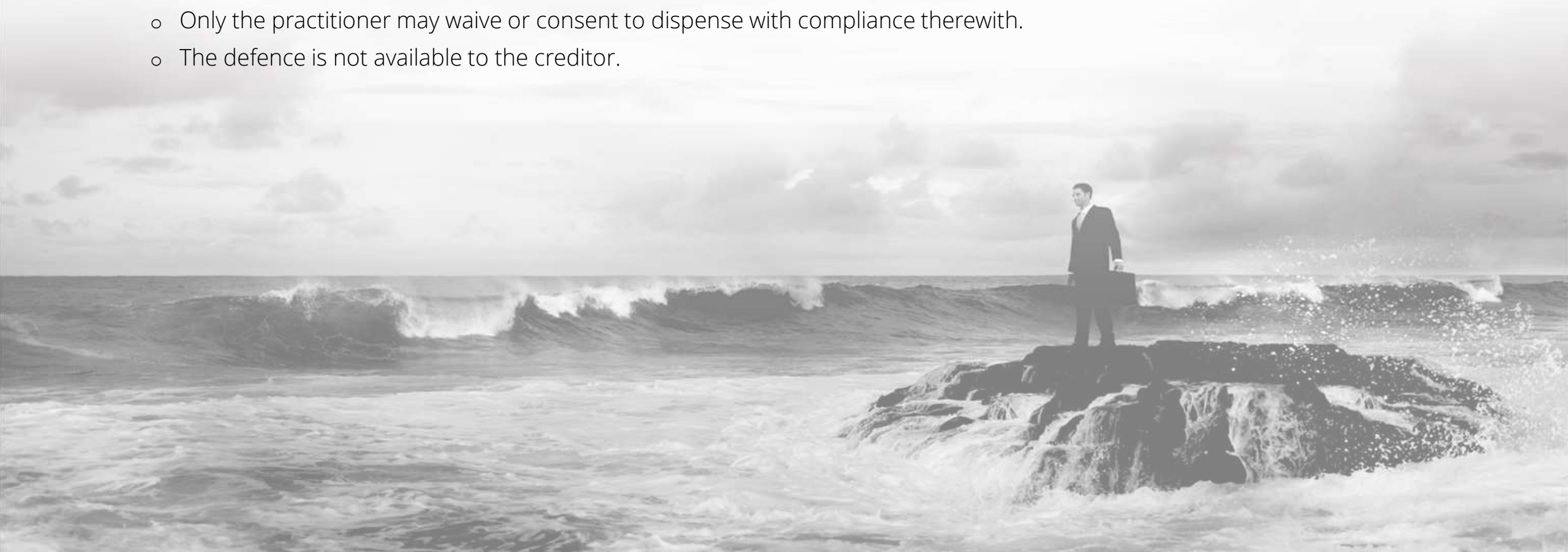
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Benefit of the Moratorium

Investec Bank Ltd v Bruyns 2012 (5) SA 430 (WCC)

- The statutory moratorium as a personal privilege or benefit in favour of the company.
- Therefore:
 - Only the practitioner may seek its protection.
 - Only the practitioner may waive or consent to dispense with compliance therewith.
 - The defence is not available to the creditor.



Stay on Legal Proceedings

Madodza (Pty) Ltd v Absa Bank Limited & Others [2012] ZAGPHHC 165 (15 August 2012)

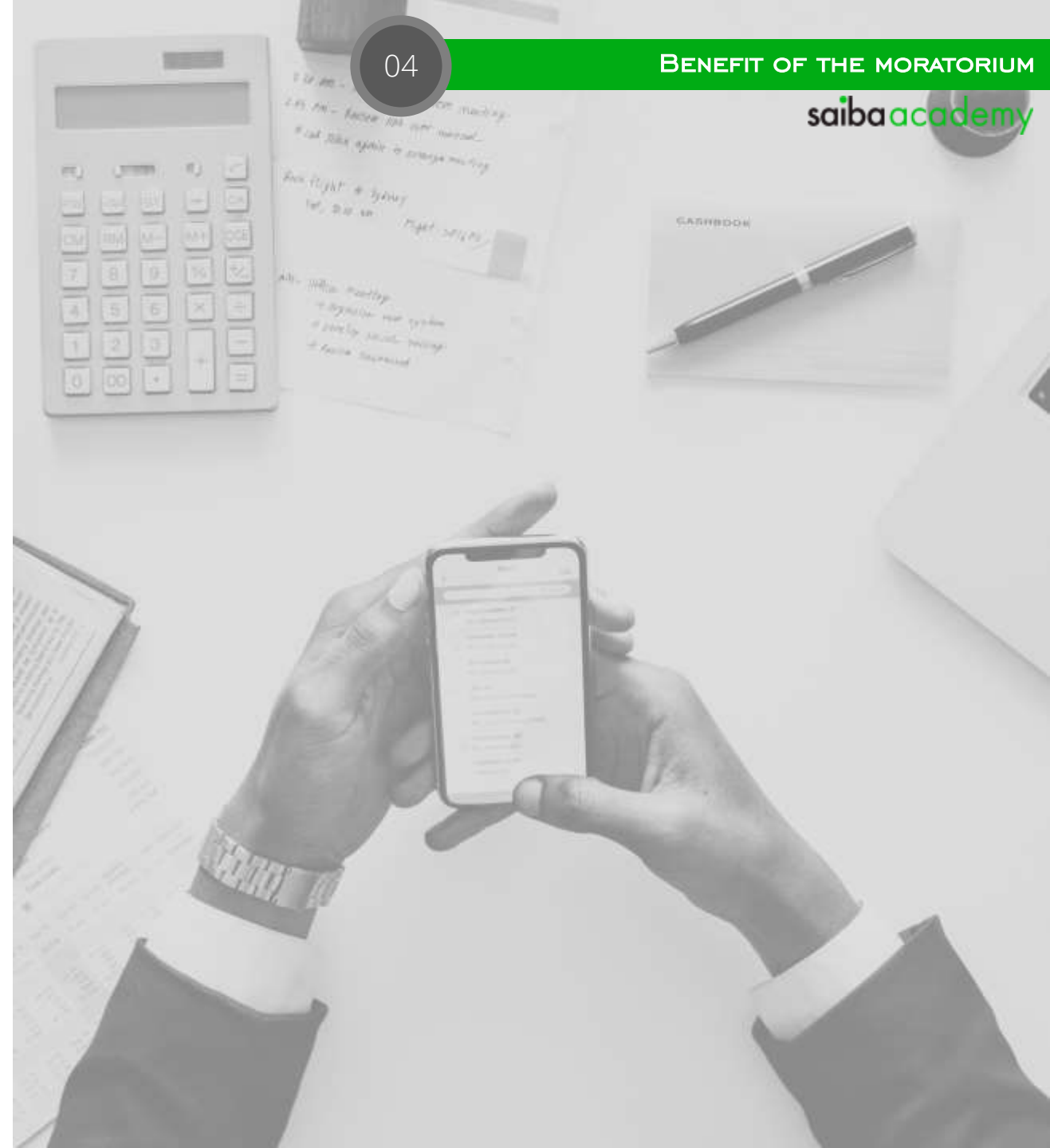
- Final court orders for the attachment of vehicles were issued prior to the commencement of business rescue
- The orders fell outside the s133 moratorium on enforcement proceedings
- The court ordered the return of the vehicles on the basis that the vehicles did not constitute property of the company nor property lawfully within the possession of the company in business rescue



Stay on Legal Proceedings

Cloete Murray NO & Another v FirstRand Bank Limited t/a Wesbank 2015 (3) SA 438 (SCA)

- Held –
 - Enforcement action refers to the enforcement of obligations under the generic heading of “legal proceedings” in section 133 of the Companies Act.
 - FirstRand was entitled to cancel the instalment agreement as cancellation does not constitute “enforcement action” as it does not constitute enforcement by way of legal proceedings.
- It is submitted that perfection of a general notarial bond is enforcement action as it requires leave of the court to repossess the property in the absence of the consent of the mortgagee
- Moratorium on legal proceedings would then apply after commencement of business rescue proceedings



Stay on Legal Proceedings

Moodley v On Digital Media & Others 2014 (6) SA 279 (GJ) (11 July 2014)

- Facts: an application was brought to set aside the adopted business rescue plans. The question before the court was whether the moratorium in section 133 applied to proceedings relating to the development or adoption or implementation of a business rescue plan
- Question: was leave of the court or the consent of the practitioner required for the institution of legal proceedings?
- Held – the purpose of s133(1) is to prohibit the commencement or continuation of any legal proceedings against a company in business rescue. The moratorium is not concerned with the development, adoption and implementation of the business rescue plan but rather with the temporary stay of legal proceedings against a company in business rescue
- No need for affected parties to seek leave from the practitioner or the court when instituting legal proceedings relating to the business rescue plan



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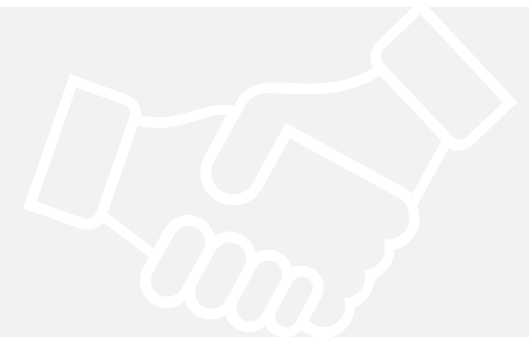
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Sureties and Guarantees by the Company

- Surety –
 - obligation is accessory to the principal obligation
 - depends on the wording in the document – has one agreed to be specifically liable for the principal obligation
- Guarantee –
 - liable independently (not accessory to the principal obligation)
- Surety or guarantee given by a company that is in business rescue -
 - section 133(2) - during business rescue proceedings, a guarantee or surety by a company (that is in business rescue) in favour of any other person may not be enforced by any person against the company except with the leave of the court and in accordance with any terms that the court considers just and equitable
 - Business Rescue Practitioner is not empowered to consent to enforcement against the company of claims based on guarantees and suretyships (section 133(2))
 - Instead, creditors should submit a claim for the value of the surety or guarantee in the business rescue proceedings



Sureties by Third Parties

Investec Bank Ltd v Bruyns 2012 (5) SA 430 (WCC) (Rogers AJ)

- Considered the meaning of section 133 and the status of a surety and guarantee provided by the company, or by another person or entity in favour of the company, during business rescue
- Held –
 - section 133(2) prohibits a third party from enforcing a suretyship or guarantee, provided by the company, against the company, during business rescue
 - practitioner cannot consent to the enforcement of a suretyship or guarantee against the company, it can only be granted with leave by the court
 - the statutory moratorium that arises for the benefit of a company does not automatically arise for the benefit of a (third party) surety on the basis that the statutory moratorium is a personal defence that arises for the benefit of the principal debtor (ie the distressed company) and has no effect on the existence of the debt



Sureties by Third Parties

Investec Bank Ltd v Bruyns 2012 (5) SA 430 (WCC)

- Rogers AJ
 - a business rescue plan may provide for the company to be released in whole or in part from its debts
 - if the Business Rescue Practitioner puts forward a plan with such a feature and if it is approved and implemented in accordance with its terms and conditions, an affected creditor may lose the right to enforce his claim (whether in whole or in part)
 - if all of these events were to occur, a surety for the company would not be liable to the creditor for more than so much of the claim as survives the implementation of the business rescue plan



Sureties by Third Parties

Business Partners Limited v Tsakiroglou and Others 2016 (4) SA 390 (WCC)

- Company owing the principle debt went into business rescue and the third party applied for a sequestration order in respect of the surety's estate
- On the return date, the surety brought a counter-application and argued that the moratorium against legal proceedings in section 133 of the Companies Act was unconstitutional as it applied to companies in business rescue but did not extend to sureties.
- The surety argued that the rights of dignity, equality and property had been compromised under the Constitution of the Republic of South Africa, 1996 if the surety were to be held liable.

Business Partners Limited v Tsakiroglou and Others 2016 (4) SA 390 (WCC) – Constitutional challenge on appeal

- Held – Based on the *Investec* judgment, the moratorium on legal proceedings is a personal defence to the company placed in business rescue
- Therefore there is no discrimination in terms of section 9 of the Constitution between the company as a juristic person and the surety as a natural person



Sureties by Third Parties

DH Brothers Industries Pty Ltd v Gribnitz N.O. & Others 2014 (1) SA 103 (KZP)

- Application to set aside the business rescue of the company based on the grounds, inter alia, that it was just and equitable to do so.
- Directors of the company also stood as surety for its debts but as a result of the business rescue plan, the applicants were subject to a compulsory cession of 76% of their claim which in turn extinguished their ability to claim from the sureties
- Held – section 154(1) provides that a creditor who has acceded to the discharge of its debt (in whole or in part) will lose the right to enforce it
- Therefore considering section 152(4) makes a business rescue plan binding on non-consenting creditors and section 154(2) provides that a pre-business rescue debt can only be enforced to the extent provided for in the plan, then any business rescue plan that goes beyond a voluntary discharge of the debt is not competent
- Otherwise a creditor would be deprived of its claim and by extension, its claim against a surety even if it did not vote for this scenario



Sureties by Third Parties

Artio Investments Proprietary Limited v Absa Bank Limited & Others (7562/2014) [2014] ZAGPPHC 689 (8 September 2014) – Extinguishing of debt – sureties are also exempt

- Applicant ran a shopping centre but eventually went into business rescue with ABSA as its largest creditor in terms of which the shareholders stood surety
- Absa brought an application for winding-up.
- Made an offer of R24 million to ABSA which was only 25% of the total amount owed to ABSA
- Held – there were no exceptional circumstances that would justify not granting a winding up order given that were ABSA to accept the applicant's offer, it would not be able to claim the surplus from the sureties



Sureties by Third Parties

Blignaut v Stalcor Proprietary Limited 2014 (6) SA 398 (FB) – moratorium under business rescue is a personal defence to a company

- Applicant stood as surety for a company that was placed in business rescue.
- In opposition to a writ of execution brought by the company's creditor against him, the applicant argued that the adoption of a business rescue plan which wrote off 75% of the debt was a statutory compromise and that as such the creditors could not satisfy their claim through the suretyship
- Held – business rescue is a personal defence specific to the company and cannot be relied on by the surety



Sureties

Absa Bank Limited v Du Toit and others (7311/13) [2013] ZAWCHC 194 (13 December 2013)

- It was application for summary judgment against sureties
- The business rescue plan of the company provided that –
 - the amounts made available for payments to creditor in terms of this business rescue plan were paid in full and final settlement of any and all claims of the creditors
 - such settlement was not intended to affect any rights that any creditor may have against any third party who bound itself as surety
 - Held – by virtue of sections 154(1) and (2) ... provision could be made in the business rescue plan that the principal debt not be extinguished ... which by implication would mean the retention of the principal creditor's right of recourse against the surety



Sureties

African Banking Corporation of Botswana Limited v Kariba Furniture Manufacturers (Pty) Ltd 2013 (6) SA 471 (GNP)

“There is no express provision contained in Chapter 6 of the Act which provides that the adoption of a business rescue plan will deprive creditors of the company in business rescue, of their rights as against sureties for the debts of the company in business rescue. The effect of such a provision, in my view, would be drastic as it would deprive a creditor of its rights as against a third party (surety) simply by virtue of the adoption of a business rescue plan for the debtor. If the legislature intended that the adoption of a business rescue plan would have such a far-reaching consequence, the legislature would have expressly provided for this consequence”



Sureties by Third Parties

- General principle –
 - if the principal debt is discharged, the accessory obligation of the surety is discharged unless the suretyship provides otherwise
 - applies to a compromise or release pursuant to a statute regardless of whether or not the creditor himself supported the compromise or release
- If a business rescue plan provides for a release of the principal debtor and if the right against a surety is not preserved in the plan, the right against the surety is discharged



Sureties by Third Parties

- Practical approach –
 - ensure that suretyships are drafted so as to ensure that they remain extant notwithstanding any compromise of the principal debt
 - ensure that the business rescue plan preserves the creditor's right to pursue the surety
- If a legal proceedings are brought against a surety during business rescue, the moratorium against legal proceedings is not a defence for a surety
- However, after the business rescue plan is adopted, the principal debt may be extinguished in terms of section 154(2) thereby extinguishing the sureties obligations



Discharge of debts and claims

- Section 154(1) provides that a business rescue plan “**may**” provide that a creditor will lose the right to enforce the relevant debt or part of it; and
- If a business rescue plan has been approved and implemented in accordance with Chapter 6, then no creditor will in terms of section 154(2) be entitled to enforce any debt owed by the company, “**except to the extent provided for in the business rescue plan.**”
- This means:
 - the Act expressly envisages that a business rescue plan may include a release (discharge) of the company from its debts
 - It is a defence *in rem* ... but, hold on...



Sureties and Guarantees

New Port Finance Company (Pty) Ltd and Another v Nedbank Limited (30/2014) [2014] ZASCA 210; [2015] 2 All SA 1 (SCA); 2016 (5) SA 503 (SCA) (1 December 2014)

- Wallis in the SCA said that -
 - Section 154 “is capable of the construction that it deals only with the ability to sue the principal debtor and not with the existence of the debt itself. If that is the case then the liability of the surety would be unaffected by the business rescue, unless the plan itself made specific provision for the situation of sureties”



A clearer picture

- A deed of suretyship may be crafted to protect a creditor's rights against sureties
- In its absence, if the plan provides for "full and final settlement", then
 - the common law position will be applicable (no provision similar to section 155(9); and
 - a defence in rem will arise and a surety will be able to resist a claim;
- Section 154(2), on the other hand, merely provides a personal defence that ensures to the benefit of the distressed company



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Protection of Property Interest

- In terms of **section 134(1)**, during business rescue the company may dispose, or agree to dispose of property only if -
 1. it is in the ordinary course of business; or
 2. it is a bona fide transaction at arm's length for fair value approved in advance and in writing by the practitioner; or
 3. In a transaction completed within, and undertaken as part of the implementation of, a business rescue plan
- Any third-party who through an agreement concluded prior to commencing business rescue is in lawful possession of any property owned by the company may continue to exercise any rights in respect of that property in accordance with the agreement
- No person may exercise any right in respect of any property in the lawful possession of the company irrespective of whether the property is owned by the company



Protection of Property Interest

- **Section 134(3)** - if during business rescue, the company wishes to dispose of property over which another person has security or title interest, the company must –
 - obtain the prior consent of the security holder unless the proceeds would be sufficient to fully discharge the indebtedness that the security or title interest protects; and
 - promptly –
 - ❖ pay the sale proceeds to the security holder up to the amount of the company's indebtedness to that person/entity; or
 - ❖ provide security for the amount of those proceeds to the reasonable satisfaction of the security holder
- **Section 136(2A)(c)** – if a business rescue practitioner suspends a provision of an agreement relating to security granted by the company, that provision nevertheless continues to apply for the purpose of section 134 (i.e. the property interest and security rights remain intact for disposal purposes)

Protection of Property Interest

- Therefore -
 - Property owners remain protected – their property cannot be prejudicially dealt with by the Business Rescue Practitioner.
 - Bondholders – will either receive the full value of their claim from a sale of the underlying property, or if not, the property can only be sold with the bondholder's consent.
 - If the Business Rescue Practitioner suspends any provision of an agreement related to security, the suspension does not apply for purposes of section 134
 - ❖ That is - the consent of the security holder is required unless a sale or realisation of the security will discharge the full claim of the creditor.
 - ❖ Example – the rights of a bondholder and landlord (perfected tacit hypothec) regarding the disposal of the asset securing a claim, would not be affected by a suspension.

Protection of Property Interest

National Union of Metalworkers of SA and others v VR Laser Services (Pty) Ltd and others [2020] 2 All SA 536 (GJ)

- Held: Section 134 deals with a creditor's security which was obtained prior to the commencement of the business rescue proceedings
- provides for the protection of the security
- specifies the manner in which the encumbered asset is to be disposed of by business rescue practitioners
- Remuneration due to employees post commencement of business rescue proceedings does not place them in preference to pre-business rescue proceedings secured creditors



Landlord's Tacit Hypothec

Landlord's hypothec -

- a right enjoyed by a landlord in respect of arrear rental over movable property brought into or upon the leased premises
- operates for as long as rental is owing – when payment of the arrear rental is made, the landlord must return the movables to the tenant
- although a landlord's hypothec arises immediately when a tenant falls into arrears with rental, it is of little effect unless it has been perfected –
 - the landlord must obtain an order of court and attach the assets; or
 - obtain an interdict preventing the tenant from removing the movables on the property
- Importantly – general view is that a landlord must "perfect" before the commencement of business rescue proceedings to be a secured creditor, otherwise caught by the moratorium on legal proceedings and enforcement actions



Landlord's Tacit Hypothec

Perfect before business rescue or liquidation – secured creditor

- Without perfection - enjoys a preference only in respect of a liquidation (section 85(2) of the Insolvency Act) – not in respect of a business rescue
- Preference in a liquidation is limited to –
 - three months if the rent is payable monthly or at shorter intervals;
 - six months if the rent is payable at intervals exceeding one month but not exceeding three months;
 - nine months if the rent is payable at intervals exceeding three months but not exceeding six months; or
 - 15 months in any other case
- For any arrear rental owing for a period longer than 3, 6, 9 or 15 months respectively, the landlord will have a concurrent claim

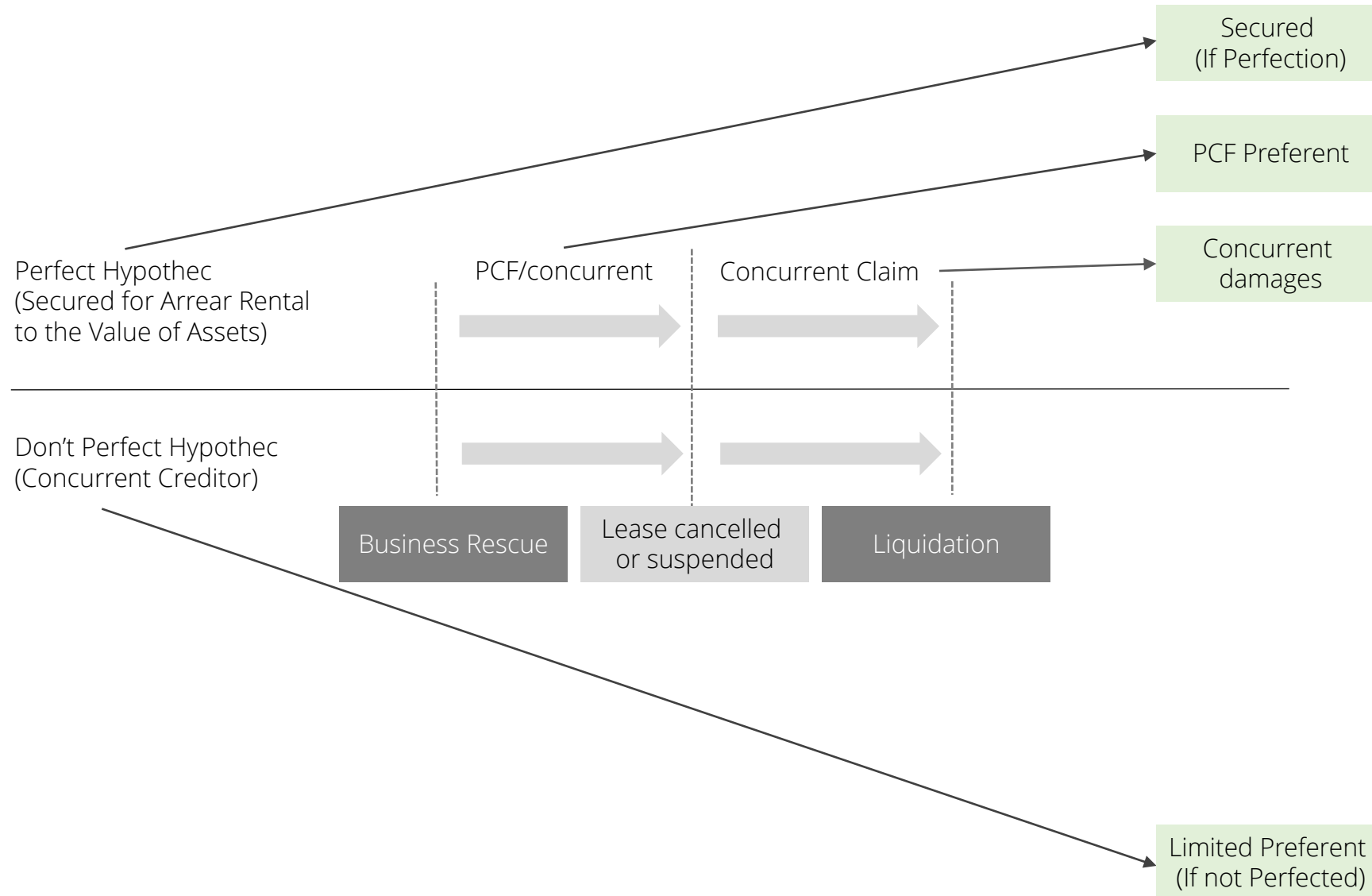


Summary

- A lease which –
 - remains operative - PCF (i.e. provision of services during business rescue) if agreed with the Business Rescue Practitioner
 - remains operative – if not agreed with the Business Rescue Practitioner, arrear rental gives rise to a concurrent claim
 - is cancelled – gives rise to a concurrent claim for damages
 - suspended – fully or partially, gives rise to a concurrent claim for damages
- Claim for damages is controversial - if the lease provisions are suspended, the landlord moves from a PCF creditor to a concurrent creditor – claim for damages may or may not be compromised in terms of the plan
- A landlord who –
 - perfects his hypothec prior to business rescue will be a secured creditor (consideration to be given to previously registered special notarial bonds and perfected general notarial bonds)
 - does not perfect his hypothec before business rescue, will be concurrent creditor



Timeline



General Notarial Bonds

- Holder of a general notarial bond is not a secured creditor but a preferent creditor
- Mere fact that a notarial bond has been agreed on and registered does not in itself authorise the bondholder to take possession of the property. Instead, a perfecting clause to that effect has to be incorporated into the notarial bond agreement
- Perfecting clause is effectively an agreement to constitute a pledge, thereby entitling the bondholder to take possession of the property with the mortgagor's consent or in the absence of consent, by an order of Court
- Holder of a general notarial bond would need to "perfect" the bond (on application to court) before a liquidation or business rescue in order for the bond to have any effect
- Whilst the movable property over which a special notarial bond is registered is specifically excluded from the landlord's tacit hypothec, the same is not true of a general notarial bond



Special Notarial Bonds

- Scope of the landlord's hypothec has been limited by section 2 of the Security by Means of Movable Property Act 57 of 1993 (i.e. special notarial bond)
- Provides that a landlord's hypothec cannot exist over movable property if -
- property which, while hypothecated by a special notarial bond mentioned in section 1(1) of the Act is in the possession of a person other than the mortgagee, unless the landlord's hypothec was perfected before the notarial bond was registered; or
- the property is subject to an instalment agreement defined in section 1 of the National Credit Act 34 of 2005.
- If a special notarial bond is registered before a landlord "perfects" his hypothec, the special notarial bond will trump the landlord's hypothec

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