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AUD009 EXPLORING VARIOUS BUSINESS RESCUE PRACTICES IN SOUTH AFRICA

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ABSTRACT:
Business rescue proceedings attempt to rehabilitate businesses that are in financial distress and provide them with an alternative to liquidation (Companies Act No. 71 of 2008). Despite its importance, there is a seemingly low rate of success of the current business rescue regime (at just 13.6% as at June 2015 and 15% as at 30 June 2016 (Companies and Intellectual Property Commission, 2016). This article seeks to build on our current understanding of some of the key issues that may be hindering the current rate of success of business rescue practices and thereby aims to assist practicing accountants (in their capacity as business rescue practitioners). This will allow them to better perform their duties and also gives corporates in need of rescue a fighting chance.

Through the use of qualitative interviews, this study provides detail on five key insights to business rescue practices in South Africa, namely: the effect of the change in the regime (from judicial management to business rescue), the effect of financial distress and the possibility of voluntary applications for business rescue, the effect of inconsistent court judgements on business rescue proceedings, the congruence of the South African business rescue regime with that of other jurisdictions and lastly the effect of creditors and the ability to source funding in business rescue proceedings.

Key words:
Business Rescue; Success; Rescue; Companies Act; South Africa; Rescue practice.

INTRODUCTION, SIGNIFICANCE AND BACKGROUND:

Business rescue proceedings attempt to rehabilitate businesses that are in financial distress and provide them with an alternative to liquidation (Companies Act No. 71 of 2008). Successful business rescue proceedings are in the interests of South African society; the successful rescue of financially distressed companies will limit job losses and this is extremely relevant in South Africa where unemployment figures are high (Loubser, 2010). Loubser (2010) also explains that a increasing number of South Africans hold shares in listed companies indirectly and that individual shareholding has increased in South Africa. In particular, 95% of the shareholders in South Africa's publicly traded, broad-based black economic empowerment (BBBEE) share-purchase schemes are individuals (van Zyl, 2015). This emphasises the fact that companies are part of the community and that their failure will impact the community, placing greater importance on their rescue (if needed).

There are two requirements for the use of business rescue provisions: the company must be 'financially distressed', and there must be a reasonable prospect of rescuing the company (Companies Act No. 71 of 2008). 'Financial distress' refers to the appearance that the company will not be able to pay its debts as they fall due in the following six months or that the company will become insolvent in the following six months (Companies Act No. 71 of 2008). Business rescue can be entered voluntarily by the company, or applied for by creditors, shareholders and employees (Companies Act No. 71 of 2008). The Association of Chartered Certified Accountants states:

> "The primary objective with business rescue provisions is to save the company as a going concern. If this is not possible, then the secondary object or goal is to restructure the company in such a way that shareholders and creditors will still get a return on their investments, which is better than the return that they would have received should the company be liquidated." (ACCA, 2014)

Judicial management, which is often viewed as a precursor to liquidation, was used prior to the implementation of business rescue, for a similar purpose (Levenstein, 2008; Naidoo, Patel & Padia, 2016). The business rescue provisions introduced in 2008 ensured the correlation of South African company law with international provisions for corporate turnarounds (Levenstein, 2008) and aimed to address the shortcomings inherent in judicial management (Loubser, 2010; Naidoo, et al., 2016). Despite the provisions made in the Act to rehabilitate businesses, business rescue proceedings do not always succeed in rehabilitating the company as reflected by the current low rate of success (the Commission, 2014; the Commission, 2015). (It is noted that this rate of success is measured on the basis of a successful implementation of the business rescue plan constituting success.) The Minister of Trade and Industry acknowledges that the regime has several shortcomings such as "sanctions applied to business [rescue] practitioners and the regulation of their activities" (the Commission, 2014, p. 6).

The purpose of this paper is to elicit key insights on the current practice of business rescue to understand the regime better, through the use of the views elicited from experienced business rescue practitioners, and thereby improve on its success. The study is explorative in nature with key focus areas being: the effect of the change in the regime (from judicial management to business rescue), the effect of financial distress and the possibility of voluntary applications for business rescue, the effect of inconsistent court judgements, the congruence of the South African business rescue regime with that of other jurisdictions and

lastly the effect of creditors and the ability to source funding in business rescue proceedings. Business rescue provisions were inserted into the Companies Act (2008) in order to improve on the previous regime – judicial management – which was not considered to be very successful. Business rescue has a greater chance of success when the warning signs of financial distress are acted upon. Court judgements have an important role to play in the development and clarification of legislation and thus have the ability to influence the impact of the regime. There are similar corporate rescue regimes internationally which have some similar characteristics and which may provide further guidance. Lastly, the availability of funding and the support of creditors may have a key role to play in business rescues and the overall success of the regime. These key factors are examined.

LITERATURE REVIEW:

1. Judicial management:

The business rescue regime legislated in the Companies Act No. 71 of 2008 replaces judicial management which has been perceived by the market as a step toward liquidation (Levenstein, 2008). Under the Companies Act of 1973, a company which was financially distressed and could not meet its obligations had two alternatives to liquidation: judicial management or reaching a compromise with creditors (Claasens, 2012). Judicial management thus served as a formal corporate rescue procedure, although it was not seen to be an effective means of rescuing companies in financial distress because of its low rate of success and instances of abuse. Judicial management was also only available to companies and not to close corporations (Lamprecht, 2008), and was also considered to be "cumbersome and was not accessible enough" (Alberts, 2004, p. 81). Further, it was considered to be a "special and extraordinary privilege that should be granted only in very special circumstances" (Loubser, 2008, p. 373). Bradstreet (2011) explains that of the companies that made use of the judicial management provisions, less than 20% avoided being wound up (i.e. an 80% failure rate) after being placed into judicial management.

Claasens (2012) cites that this failure arose due to the high level of probability of success required for the rescue proceedings to be initiated and the requirement that the company wholly settles its debt with its creditors, as part of the judicial management proceedings. Thus, judicial management could only be invoked if the company was already insolvent (The Centre for Advanced Corporate and Insolvency Law, 2004; Lamprecht, 2008). There was also a great level of court involvement which was "self-defeating" (Rajak & Henning, 1999, p. 268) which also made it unsuitable for smaller businesses (Rajak & Henning, 1999; Lamprecht, 2008). Further, there was an onerous burden of proof placed on the applicant (for judicial management) to show that it is probable that the company will be rescued (as opposed to the possibility of being rescued) (Lamprecht, 2008).

The Centre for Advanced Corporate and Insolvency Law (2004) quotes Harmer (1997) as saying that a business rescue regime has a better chance of achieving the intended objective if the insolvency provisions are debtor-friendly. Judicial management also had a negative impact on the credit rating of the company and made it difficult for the company to obtain financial assistance (Claasens, 2012) with which to rehabilitate itself. Due to the low success rate under judicial management, creditors would often resort to "cutting their losses" (Bradstreet, 2011, p. 356) through supporting the immediate liquidation of the company.

The business rescue provisions legislated in the Companies Act attempt to improve on and address the above flaws of judicial management. The current business rescue regime recognises the value of the entity as a going concern and considers all affected parties (not only the interests of the creditors) (Bradstreet, 2011). Furthermore, business rescue provisions in the Companies Act can be applied when the company is financially distressed and need not be invoked only when the company is already insolvent (Companies Act No. 71 of 2008). The business rescue provisions in the Companies Act bring about several improvements and address some of the flaws inherent in judicial management - whether business rescue provisions suitably compensate for the inadequacies in judicial management is what this study partly endeavours to explore by interviewing South African practitioners and obtaining their views in this regard.

2. Financial distress and voluntary business rescue:

For business rescue to succeed, it is imperative that prompt action and decisions are taken (Finch, 2005). Olivier (2014) states that delaying the process of requesting assistance when needed is the worst thing a business can do. It is, therefore, imperative to recognise the warning signs and ask for help earlier (Olivier, 2014). Warning signs exist in several different categories, including management, finances, operations, strategy and banking (Pretorius & Holtzhauzen, 2013). An earlier start of a rescue procedure increases the chances of its success (Loubser, 2010).

The board of a company may delay in initiating business rescue because of its belief that there is not a reasonable prospect of rescuing the company, or it believes it can continue and trade its way back to good financial health or it may wish to reward itself (the members of the board) (Loubser, 2010). This reward would come in the form of stripping some of the assets of the entity before it is closed down (Loubser, 2010). In both: the case of attempting to trade the company out of financial distress or attempting to strip the company's assets for personal benefit, the directors may want to keep this information away from creditors to enhance their own ability to achieve their goal (Loubser, 2010). An entrance into business rescue would require informing creditors and this action will, therefore, be avoided.

The Companies Act does, however, provide that if the requirements for voluntary entrance into business rescue are met and the directors decide not to place the company into business rescue proceedings, a notice must still be issued to affected persons disclosing this fact (Companies Act No. 71 of 2008). Finch (2005) and Loubser (2010) both note, however, that the onerous requirements for notifications to be sent may act as a deterrent because this is a costly exercise. This paper will thus explore whether there are any practical issues that are standing in the way of the success of the regime at present which can contribute to the above literature.

3. Court judgements:

As an alternative to entering into business rescue voluntarily, a shareholder, creditor, trade union representing employees of the company or employees not represented by the trade union (an "affected person") can apply to the court at any time for an order to place the company in business rescue (Companies Act No. 71 of 2008). Upon application, the court has discretion either to dismiss the application or to place the company under business rescue (Claasens, 2012). Claasens further states that, if there is a "reasonable possibility" of being rescued (2012, p. 11), the court should place the company under business rescue.

The lack of a specialist court has been blamed for the lack of success of business rescue as the lack thereof has resulted in contradictory judgements (Ensor, 2014). This refers to the fact that not all judgements are made in support/in precedent with other judgements previously made. This impedes the success of business rescue as it leaves practitioners with uncertainty about what are acceptable actions in the context of business rescue. Certain provisions in the Companies Act seem to lack clarity, such as the meaning of "reasonable prospect." Case law would ordinarily clarify this meaning but the conflicting judgements in this area do not allow for the establishment of clear criteria (Ensor, 2014). This paper partly aims to explore the importance and effect of court judgements (both quantitatively and qualitatively) on the business rescue process.

4. International provisions:

Although South Africa was one of the first countries to introduce a form of corporate rescue through judicial management, prior to the Companies Act No. 71 of 2008, it lagged behind other countries in terms of its business rescue regime (The Centre for Advanced Corporate and Insolvency Law, 2004). This was due to a few progressions in other corporate rescue regimes abroad that South Africa did not keep abreast of (as judicial management had not changed substantially since its enactment) (Kloppers, 1999). The trend in other modern corporate rescue regimes was to rescue the company and the business carried on by it (Bradstreet, 2011), while judicial management in South Africa was perceived simply to precede liquidation (Levenstein, 2008), which would not allow such a rescue to take place. It seemed that business rescue regimes worldwide were popular and judicial management was traditionally perceived as unsuccessful (The Centre for Advanced Corporate and Insolvency Law, 2004). That is, judicial management was seen as an extraordinary measure, while other jurisdictions saw business rescue as a necessary and natural predecessor for insolvency (The Centre for Advanced Corporate and Insolvency Law, 2004).

In establishing its own business rescue regime, South Africa had the opportunity to learn from those of the United States of America (U.S.A.), Germany, Canada, the United Kingdom (U.K.) and Australia (Claasens, 2012; Cawood, 2014) because these countries had already instituted such practices.

In the U.S.A., the goal of filing a *Chapter 11 petition* for corporate rescue (as opposed to filing for liquidation under Chapter 7) is to become profitable (U.S. Securities and Exchange Commission, 2009). This is similar to one of the objectives of the Companies Act in terms of business rescue – to rehabilitate the company. However, the U.S.A.'s corporate rescue regime allows the company itself an opportunity to propose a rescue plan within 120 days of a petition being filed (Pont & Griggs, 1995). This allows the board to propose a rescue regime and does not call for the appointment of an external person (such as a business rescue practitioner). This is because it is believed that the board has the "requisite hands-on knowledge of a company's immediate state of affairs" (Finch, 2005, p. 391) and may be better able to develop a feasible rescue plan than an external person who is not familiar with the business.

Further, the 120 days allowed by U.S.A. legislation (Pont & Griggs, 1995) to develop a rescue plan is significantly longer than the 25 days currently allowed by South African legislation (Companies Act No. 71 of 2008). The additional time may allow for a more comprehensive investigation and the preparation of a better, more feasible plan. In

turnaround situations, there is often dependence on financial reports, which are often inadequate and are found to be “after the fact” (Pretorius & Holtzhauzen, 2013, p. 468).

Unlike the corporate rescue regime in the U.S.A., the German business rescue regime does not provide for a debtor in possession (where the company itself has an opportunity to rescue itself and is in control of its own affairs) and does not place priority on reorganisations (Loubser, 2010). German law provides that rescue should only be an option if the value of the business as a going concern exceeds the liquidation value (Loubser, 2010) and there is no difference in the procedure, under German law, regardless of whether it is expected that the company be liquidated or rescued (Loubser, 2010). The Canadian business rescue regime on the other hand has three main goals (similarly to those of the U.S.A., Australia and the U.K.) – the impact on all stakeholders should be beneficial and an economically viable company should emerge from the rescue or there should be a better return for creditors than that achieved under liquidation (Conradie & Lamprecht, 2015). The latter two objectives are similar to those of the South African business rescue regime.

The U.K.’s corporate rescue provisions are similar to that of South Africa and aim to preserve the continuation of the business as a going concern and to preserve some jobs as a result (Loubser, 2010). The U.K.’s Insolvency Act provides that financially distressed companies will have an administrator appointed to assist and that this administrator will have a wide range of management powers (Loubser, 2010). Administration is only available if a company satisfies two conditions: the company is or is likely to be unable to pay its debts and administration is reasonably likely to satisfy the intended objective of administration proceedings (Loubser, 2010). The intended objective of administration proceedings is to rescue the company as a going concern and, if this is not possible, to achieve a better return for creditors than that which would have been achieved had the company been wound up (Loubser, 2010).

Administration grants the company a moratorium on the enforcement of claims and repossession of security (Armour, 2004). This is in line with the South African business rescue regime. It was however found that the main cause of financial difficulty for the companies that entered into the U.K.’s corporate rescue procedure was poor management and poor economic conditions and that the breathing space afforded by the moratorium has a significant effect (Pandit, Cook, Milman, & Chittenden, 2000).

The Australian approach was guided by the approach of the U.K. and the U.S.A. (Routledge & Gadenne, 2004). The objective of the Australian corporate rescue regime is to maximise the possibility of the company continuing or, if this is not possible, to provide a better return than immediate winding up (Anderson, 2001). Australia’s business rescue provisions call for the appointment of an independent, external ‘company administrator’ who is appointed by the board of directors (Pont & Griggs, 1995). This is similar to the appointment of the business rescue practitioner under the current South African regime. However, in contrast to South Africa, the company administrator must also be qualified as a liquidator (Anderson, 2001). When the company administrator is appointed and the company effectively enters into voluntary administration, there is a short moratorium on the enforcement of debts against the company but there are certain exceptions[12] (there are no exceptions of this

[12] These exceptions apply when the holder of a charge over the whole or substantial amount of company assets acts before or during the decision period and enforces that charge; when a secured creditor holding a charge has assumed possession or control over that property or has made arrangements for its sale; when a secured creditor holds a charge over perishable property; and when, prior to the

nature to the moratorium in the South African business rescue regime) (Museta, 2011). This regime, however, accepts that rescue need not necessarily rule out liquidation but should provide a better return to creditors than winding up (liquidation) (Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami) (Pty) Ltd (609/2012) [2013] ZASCA 68, 27 May 2013).

The provisions for business rescue inserted into the Companies Act bring South African company law in line with international provisions for corporate turnarounds (Levenstein, 2008). However, it is important that a business rescue regime is specifically tailored for the economic and social conditions of a country (Claasens, 2012), which may/ may not be the case for South Africa and is what this paper partly aims to explore.

5. Creditors and funding:

Olivier (2014) states that not every business is a candidate for business rescue and that business rescue will only succeed if shareholders are willing to provide some form of working capital. A lack of available funding could seriously impede the success of business rescue as, without it, the company is unable to sustain its operations (Thomas, 2014). The delivery of any notice stating that the company is in financial distress could severely impede the ability of the company to secure funding and could potentially result in the cancellation of credit facilities and in demands by suppliers to be paid immediately (Loubser, 2010). Vriesendorp & Gramatikov (2010) cite that a large majority of insolvency practitioners find that it is more difficult to find funding for companies that are in financial distress, especially when the company needs the funding most (when it is in financial distress).

Finch (2005) points out that in times of financial distress, banks (and other creditors) can demand certain terms and these terms may give them the ability to influence the strategy of the company. New funding from shareholders also increases the equity these shareholders hold in the company and will allow these shareholders greater control over the company (Finch, 2005). Despite this, the fact that the Companies Act provides post-commencement financiers with superior priority may make it easier for the company to obtain funding (Companies Act No. 71 of 2008). Finch (2005) points out that a flaw in the U.K. Corporate rescue regime is that it does not place the superior priority status on post-commencement financiers. However, despite this and the recognition by the World Bank and UNCITRAL[13] that post-commencement financing is of importance, South Africa seems to lack significant available post-commencement finance (du Preez, 2012). There is also a lack of understanding by creditors of the business rescue process, which may greatly hinder their ability to participate meaningfully in business rescue (le Roux & Duncan, 2013). The importance of the commitment by creditors and shareholders, particularly in their role as providers of finance, is an area that is explored by this research paper.

METHODOLOGY[14]:

The results in this paper are formulated based on the insights and experiences of business rescue practitioners (with more than ten years of experience) using interviews. Thus, this paper is qualitative and exploratory in nature. The literature reviewed pointed out some of the potential shortcomings of the regime from which themes were developed, which then

appointment of the administrator, owners or lessors of property used by or in possession of the company enforce a right to take possession of that property (Museta, 2011).

[13] United Nations Commission of International Trade Law

[14] The methodology has been adapted from Naidoo et al. (2016)

formed the basis for an interview agenda. The transcripts from these interviews were coded (with reference to common themes) in order to formulate results. The results presented in the next section are, in certain cases, described by quoting the words of the interviewee. However, interviewees are not identified in order to protect their confidentiality.

Business rescue practitioners have been selected as constituents of the population as they were anticipated to have the most pertinent insight for the study, as they facilitate business rescue proceedings in South Africa (Companies Act No. 71 of 2008). From the 85 experienced and senior registered business rescue practitioners based in Gauteng (as at 31 March 2014), a total sample of thirteen were selected (Chen, Danbolt & Holland, 2014; O'Dwyer, Owen & Unerman, 2011; Rowley, 2012) from the Companies and Intellectual Properties Commission's (CIPC) database, as data saturation was expected to occur at this point. Interviews were conducted in Gauteng between June 2015 and November 2015. Interviewees comprised business rescue practitioner of different experiences (based on information available from the CIPC (the Commission, 2015): interviewees comprised six practitioners from an accounting background, one member of the Institute of Directors, two business consultants, two attorneys, one financial advisor and one other professional.

Due to the use of purposive sampling, interviews were deemed to be the most appropriate method. The use of the standardised interview agenda allowed for comparisons between responses of different participants to be made. In addition, the research was performed using semi-structured interviews, which allowed interviewees to talk freely about the topic, which, in turn, allowed for a deeper understanding of the interviewees' practice and perceptions of business rescue (Holland, 1998).

Data gathering and examination made use of an iterative process of interview responses being analysed in terms of the literature and responses of other participants (Willig, 2008). The authors alternated between evaluating interview data and reviewing literature based on the emerging themes (Willig, 2008). The data was processed using a methodical set of procedures to derive results (O'Dwyer, et al., 2011).

The transcripts of the interviews were analysed through a formal process of data reduction and data verification (O'Dwyer, et al., 2011). In order to facilitate data reduction and establish key themes (O'Dwyer, et al., 2011), a detailed reading of transcripts and rereading of the literature was undertaken. Themes were then individually coded to assist with analysis (Rowley, 2012). Consideration of any apparent inconsistencies within a specific transcript or between interviewees was also completed (O'Dwyer, et al., 2011). In addition, the responses were considered in conjunction with the literature to identify resemblances and dissimilarities. Once theoretical saturation occurred, concepts were then developed from the coded data.

To ensure that the findings of the research are more reliable, interviewees were asked to make any additions/corrections to interview transcripts (Leedy & Omrod, 2013). External validity was also established through a peer review process wherein the classification and coding was assessed (Rowley, 2012).

RESEARCH FINDINGS:

1. Judicial management:

When asked about judicial management, twelve of the thirteen participants believed that judicial management was not an appropriate and effective corporate rescue procedure, while one did not provide a clear answer. Many participants remarked that there were very few cases of judicial management achieving success. These views iterate that the current business rescue regime is an improvement on its predecessor. A participant stated that it was simply "a waste of everyone's time". Another commented that it was "tainted too early" and was "perceived to be a step prior to liquidation". Accordingly, judicial management required paying all debts in full and, under this regime, the company would have to "find a way to live with all the shackles on going forward". This shows that this regime was not debtor-focused. One participant used the analogy of a glass of water to explain:

> "Judicial management looks at saving the glass (the vessel; the juristic person), [whilst] business rescue says saves the water"

Another participant pointed out that judicial management was the "first of its kind" and was likely effective in its aims initially but "didn't keep pace with the changing business environment". This reiterates that although South Africa was initially at the forefront of corporate rescue, it lagged other countries for a while after the enactment of judicial management. One participant noted that judicial managers were liquidators and approached their duties with the intention to liquidate. This highlights the lack of debtor friendliness of this regime. It was also stated that judicial management was an "organised liquidation" and a process which "allowed an abusive approach".

Overall, all participants agreed that business rescue was more beneficial than judicial management and a variety of reasons were provided. The 'flexibility' provided by business rescue (as an advantage over judicial management) was common to many of the responses. One participant explained this 'flexibility' as the business rescue regime being more tailored and being applicable to both small and large companies. This shows that business rescue is aimed to be more wide-reaching and accessible than judicial management. The immediate protection (from claims of creditors) offered to companies under business rescue was also considered to be a reason why business rescue is more advantageous than judicial management.

Another reason was that business rescue proceedings seem to be more user-friendly and easier than judicial management, which was "legally top heavy" and not "focused on commercially rehabilitating a company". However, the fact that the practitioner is an agent of the court and can bind people to a plan is a reason that business rescue is preferable to judicial management. This allows for change to be effected efficiently. Lastly, it was noted that business rescue (and the protection it offers the company) affords the company, management team and practitioner an opportunity to look inwards, while, judicial management compelled the company to have an external focus (forcing the company to focus on the claims of creditors and other claimants). This reflects the business rescue regime's focus on rehabilitation and rescue of the company as the main objective.

2. Financial distress and voluntary business rescue:

The majority of participants felt that the assessment of six months for the consideration of whether the company is in financial distress is adequate. Only one participant disagreed with this and felt that, in the specific circumstances in South Africa, the time allocated was inadequate. One of the participants who felt that six months was adequate, stated that this period was often too long and that this period should not be longer because it required looking forward and trying to anticipate the circumstances the company may face in the future. Some practitioners observed that, practically, boards do not make such an assessment and, if they did, there would be greater rates of success for business rescue as the process would start sooner and the practitioner "would have more options available". It was also noted that boards do not act on indications of financial distress and "live in denial" and that the requirement that the company notify its creditors as to why it has not entered into business rescue when it is in financial distress has never been adhered to. This shows that, despite the intentions of the Companies Act and the provisions put in place to meet the objectives, it is (in part) these practical issues that are standing in the way of the success of the regime.

When asked why directors might delay applying for a voluntary business rescue, practitioners cited many reasons: some practitioners remarked that the management, who had driven the company into financial distress, felt they had the ability to rescue it from this distress. Others cited that management may be uninformed, uneducated or "don't know unless the lawyer mentions it". This shows that management lack appropriate knowledge and this may be an obstacle to the success of the regime at times. This may be a result of a lack of awareness, which if increased, will enhance the success rate. A greater awareness of the availability of business rescue to companies may increase the number of cases of successful business rescue. Practitioners also explained that management may delay the initiation of business rescue because it is not in their interests to lose control and be governed by a practitioner.

Another practitioner pointed out that filing for business rescue may trigger personal liabilities for members of management, particularly those who had signed surety. Other practitioners noted that management may be in denial or may be fearful of the unknown. The potential negative effect on management's reputation and potential negative publicity was also cited by some practitioners as a potential reason which indicates the perception that the company would be tainted forever. A practitioner, however, commented that stigmatisation was a result of lack of knowledge, while another explained that there is still a culture of business rescue being akin to liquidation and that it was still seen in a negative light. In this regard, another practitioner suggested that education would be helpful in rectifying the problem.

A few practitioners explained that, if companies came into business rescue earlier, it would be easier and would lead to a greater chance of saving these companies. One practitioner commented that business rescue "may have the unintended consequence of getting companies to work on problems earlier", which, considering an earlier start to a rescue increasing its chances of success, will improve the rate of success of the regime.

3. Court judgements:

Consistent court judgements as a factor influencing the success of business rescue were generally considered to be of importance by practitioners. One practitioner stated, as a

reason, that “you have to know all the rules”. Another practitioner commented that there are “too few” court judgements and that there would be a significant influence “but there isn’t enough precedent”.

Generally, practitioners felt that there have been some good judgements and some bad ones, where some provide clarity and some have negative influences. Courts clear up the grey areas which arise as a result of the legislation being difficult to interpret. The view of one practitioner was that the court itself had not correctly interpreted the consideration of the requirement that the business rescue should not leave creditors worse off than liquidation, while another practitioner observed that different courts have reached different conclusions (regarding the interpretation of the Act) and that this has created uncertainty. However, one practitioner explained that, despite some judgements currently having a detrimental effect, as time goes by, there will be more consistent judgements. This will help to “shape and form otherwise ambiguous or conflicting aspects”.

It is believed that court judgements are already becoming “more robust” and that some of these judgements have been “a big help”. However, another practitioner noted that the judgements had not had a huge influence to date but that there would be increasing influence of legal precedent going forward. One practitioner explained that the Companies Act “envisages dedicated business rescue courts and that hasn’t happened”. However, another practitioner expressed the view that the courts are currently supportive of business rescue and they do a “good job of preventing unfounded attempts”. This shows the importance and effect of court judgements and the expectation that they will play an increasing role in the business rescue regime.

4. International provisions:

Practitioners did not consider the alignment of South African business rescue provisions with provisions of other jurisdictions to be of high importance. This suggests that the cohesion between South African business rescue provisions and international provisions has a minimal bearing on the success of the regime.

When asked whether a rescue regime that allows management to develop the plan without the appointment of a practitioner (such as is the case in the U.S.A.) will function effectively in South Africa, some practitioners pointed out that this depended on the company and its management, while one practitioner said that this will not function effectively in South Africa. One practitioner (who believed the effective functioning of such a regime is dependent on the quality of management) stated that “if you make that a blanket-availability in South Africa, it will fail”. A few practitioners felt that it will not function effectively because management are sometimes the problem, while one stated that “there has to be an external perspective because management is so sucked into the business”. It was also stated that “generally, the same people that got the business into trouble are seldom the people to get it out of trouble.”

Some practitioners commented on the current corporate rescue regime in the U.S.A. citing that the U.S.A courts “only allow the company [itself] to resolve its issues until the creditors complain”, while another explained that it is “difficult for management to develop a plan without an external, independent perspective” and that, in the U.S.A., the external perspective comes from the court. This shows that there was generally little support for a regime that allows management to develop the business rescue plan. One practitioner

pointed out that it may be a misconception to think that management develop the plan themselves and said that they actually outsource this at great expense.

5. Creditors and funding:

The majority of participants stated that, in their experience, creditors were generally willing to accept a business rescue plan and cooperate with its implementation. Only one participant felt that this was not the case. This participant stated that the practitioner has to prove to the creditors that the business rescue can work and that the practitioner must work with them to win them over. Another participant specified that creditors with no security and creditors who were not reinsured were willing, while banks that have credit guarantees are generally less willing. A different participant who had experienced willingness by creditors to cooperate, also explained that there was "a lot of negotiation" and believed that the only way to encourage creditor cooperation is "through education and making them a part of the process".

Creditors generally seem to be supportive of business rescue. One other participant pointed out the difference in behaviour of different creditors. This participant stated that creditors with security are "inclined to liquidate and cut their losses" but that trade creditors and employees were "more willing to speculate because they have nothing to lose". Creditors are believed to be more cooperative when there is communication and transparency. Another practitioner also emphasised the importance of the relationship of trust between the practitioner and creditors.

Some practitioners noted that while funding is important, it is rarely available from shareholders. Participants pointed out the lack of the post-commencement funding market in South Africa. One interviewee stated that "distressed companies can't find money for good reason. Our capital markets are too thin. We are not creative enough in our working capital structure." In the experience of the participants of this paper, it was established that there is a difficulty in obtaining funding during and after the business rescue because the business being rescued is "perceived as a huge risk for funders" because of its financial distress and potential inability for the lender to recover all funds and because there is a lack of a post-commencement finance market in South Africa. A participant stated that "finding post-commencement funding is a key determinant of success". One interviewee commented that "the U.S.A. has a very deep market and South Africans should study this market".

The problem created by the difficulty and delay in obtaining funding was summarised by a participant who stated that "by the time you get the funding, you might sit with a dead patient". It was also stated that obtaining funding is easier where there are assets which can be used as security. If a company were to go into business rescue without consultation, all funding would dry up and security-ships would be triggered. This would be because of the perception of additional risk, due to the lack of involvement and understanding by creditors. Other financing solutions could be explored but, while it may be easier to obtain funding after business rescue, the company may still be "tainted forever". Funding thus has a key role to play in the success of the rescue, although is difficult to obtain.

CONCLUSION:

Given the important role that a well-functioning business rescue regime plays in a healthy economy, the state of the South African economy currently (low growth and high

unemployment) and the current low level of success (as identified by the CIPC), this paper has highlighted that it is absolutely imperative, now more than ever before, to understand some of the key issues that may be hindering the current rate of success of business rescue practices in South Africa. Further, it is vital that we understand the key issues that may be encumbering the current rate of success of the regime, to provide companies in need of rescue a fighting chance. This paper has provided key insight into the practice of business rescue from the point of view of practitioners and has thereby provided an understanding of some of the shortcomings in the current practice, which can then be used as areas for potential improvement in this regard.

There are several practical issues impeding the success of the current business rescue regime which need to be explored. This paper shows that while business rescue seems to be an improvement on its precursor, judicial management, there are practical issues that may impede its ability to succeed. The first item considered by this paper was that companies, through their directors, do not always apply (voluntarily) for business rescue timeously and at the first sign of distress. An earlier start to the rescue would improve its chances of success. This paper has also shown that, for business rescue to succeed, it is imperative that the warning signs of financial distress are recognised and that these are acted upon promptly. The lack of prompt action currently may be an obstruction to the regime.

Court judgements have an important role to play in business rescue but seemingly this paper establishes that inconsistent court judgements have hindered the regime. The need for a dedicated, specialist court for business rescue may address this current hindrance and would facilitate a sound legal precedent in business rescue cases going forward. Interestingly, it is also found that the cohesion between the South African business rescue provisions and the provisions of corporate rescue regimes in other jurisdictions are not considered to be important by practitioners (and are thus not considered to be a limitation to the regime). However, when probed, practitioners cited that the provisions of other regimes would not function effectively in South Africa due to the lack of this specialist court needed.

Lastly, there seems to be a lack of availability of post-commencement financing in South Africa, which, despite the superior priority given to post-commencement financiers by the Act, makes it difficult for a distressed company to find the financing it needs to rescue itself. Funding is imperative to the success of a corporate rescue and the lack thereof is a significant stumbling block for any business rescue. The findings also establish that creditors are generally supportive of business rescue plans when they are involved in the process. While times of distress may allow creditors to make additional demands, the availability of financing is imperative to the success of the rescue.

FURTHER RESEARCH:

This paper is limited to the success of the South African business regime, as legislated by the Companies Act and practitioners involved in facilitating this process. While many studies have been undertaken comparing the South African business rescue regime to corporate rescue regimes of other jurisdictions, this study (and those studies) could be expanded to include the views of practitioners from these other jurisdictions, in light of the differences noted between the various regimes. Comparisons could also be made of practical difficulties faced in different jurisdictions and an analysis can be undertaken to evaluate whether certain

difficulties are more prevalent in developing countries. This paper is further limited to business rescue proceedings that have commenced before 30 June 2015. A future study could be conducted to evaluate whether the difficulties and issues identified above (as impediments to the current business rescue regime) persist as the regime matures, especially as the post-commencement funding market in South Africa is given a chance to develop. Lastly, this paper also does not extensively examine the difference between business rescue and liquidation. The ability of the company to choose business rescue or liquidation when it is in financial distress could be examined further by future research, as well as the impact of business rescue in different industries.

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APPENDIX 1: INTERVIEW AGENDA

The following is a list of the questions that were asked of practitioners participating in the study. Participants were informed of the purpose of the study at the start of each interview and were informed that they did not need to answer questions they did not wish to answer.

Short questions

Please answer with Yes/No and elaborate wherever possible.

1. The objective of business rescue is to rehabilitate businesses that are in financial distress. Do you believe that these proceedings in fact meet this intended objective?
2. Do you think that the assessment of six months for the consideration of whether the company is in 'financial distress' is adequate?
3. In your experience, has business rescue truly adequately balanced the rights and interests of all stakeholders?
4. In your opinion, is the power granted to employees and a single shareholder too great?
5. Do you think that business rescues are generally successful?
6. Do you think that judicial management was an appropriate and effective corporate rescue procedure?
7. Without business rescue, do you believe there would be unnecessary liquidations?
8. In your experience, have creditors generally been willing to accept a business rescue plan and cooperate with its implementation?
9. The Companies Act (2008) only allows 25 days for the development of a business rescue plan. Do you think that there should be a longer period available in which to develop a business rescue plan?

Ranking question

10. Please rank each of the following factors influencing the success of business rescue proceedings on a scale of 1 to 5 (where 1 is barely influential and 5 is highly influential):

Potentially influencing factor	Rank from 1 – 5
Experience of the practitioner in conducting business rescue proceedings	
Qualification of the practitioner as the director of business rescue proceedings	
Relationship of trust between practitioner and management as a means of facilitating actions aimed at rescuing the company	
A comprehensive business rescue plan which will be used to rescue the company	
Creative strategies through which to rescue the business	
Funding from shareholders to support the company and assist with its rehabilitation	

Consistent court judgements on matters relating to business rescue	
Ability to source external funding (other than from shareholders) to be used to rehabilitate the company	
Cohesion between South African business rescue provisions and international provisions	
An extended time for the preparation of a business rescue plan	
Support of trade unions and employees in developing a business rescue plan	

Longer answer questions

11. What, in your opinion, constitutes success as far as business rescue proceedings are concerned?

12. Comparing the current business rescue regime to judicial management, which one do you think is more beneficial and why?

13. What are your views on the preparation of a business rescue plan?

14. In your experience, what are some of the difficulties you have come across in developing business rescue plans?

15. How does the relationship between the practitioner and management affect the prospects of the company's rescue?

16. Do you think that business rescue practitioners are generally adequately qualified to conduct business rescue proceedings? If not, are there any requirements you would like to have introduced into the criteria for qualifying as a business rescue practitioner?

17. What influence have court judgements on matters relating to business rescue had on the success of the regime?

18. Do you expect the success rate of business rescue proceedings to improve? What motivates this opinion?

19. In your experience, how easily have companies placed under business rescue been able to obtain funding, during or after the business rescue proceedings?

20. In your opinion, why might directors of a company delay applying for voluntary business rescue?

21. Certain other jurisdictions allow management to develop a rescue plan without appointing a practitioner. In your opinion, would this practice function effectively in South Africa? Please elaborate.