CAN A CREDITOR HAVE BUSINESS RESCUE PROCEEDINGS CONVERTED INTO LIQUIDATION PROCEEDINGS?

There can be no denying that one of the hardest hitting consequences of COVID-19 will be on business throughout South Africa, big or small, particularly following the lockdown put in place by the South African government, effective from midnight, 27 March 2020.

Many businesses will suffer financially, with revenues predicted to drop sharply until such time as the virus is contained, restrictions are uplifted and life returns back to normal. This could well spell disaster for many businesses, with few alternatives but to commence business rescue proceedings.

Businesses need to be alive to the fact that, notwithstanding that business rescue proceedings may have commenced, until such time as a business rescue plan has been adopted, section 130(1) of the New Companies Act (the "Act") allows an affected party (i.e. a creditor) to apply to court for a court order setting aside the business rescue proceedings and placing the business into liquidation.

A creditor can apply to set aside the business rescue on the following grounds: – (1) No reasonable basis exists for believing that the company is financially distressed; (2) no reasonable prospect exists for rescuing the company; or (3) the company failed to comply with the procedural requirements in section 129 of the Act when commencing with the business rescue proceedings.

In addition to the above, when considering an application to set aside business rescue proceedings, a court may do so on any of the grounds above, or if the court considers it just and equitable to do so (Section 130(5)(a) of the Act).

Most importantly, section 130(5)(c) of the Act also enables a court to then, after setting aside the business rescue, place the company under liquidation.

Whilst these provisions allow for a creditor to have business rescue proceedings converted into liquidation proceedings, from recent case law, it appears that the approach adopted by courts is that, unless compelling reasons are provided, business rescue is preferred to liquidation. Courts favour affording the business rescue practitioner an opportunity to get the business rescue ‘off the ground’ and be given a chance to save the company given the drastic measures which follow a liquidation (such as job loss).

Accordingly, companies and their directors are well advised to ensure that, should they believe business rescue to be the only means to avoid liquidation of the financially distressed company, the company comply unerringly with the requirements of section 129 of the Act and secure ample evidence that it is in the best interest of the company, its business, its staff and all other parties depending upon it, including its creditors, that the company be afforded the opportunity to return to profitability.

If such evidence can be adduced, it would appear, on the basis of current precedent, that our courts will come to the assistance of the company and the business rescue practitioner in order to avoid one or more creditors taking the business out of business rescue and placing it into liquidation.

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