



**A CRITICAL REVIEW OF THE NEW ZIMBABWEAN CORPORATE
RESCUE LAW**

BY

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TABLE OF CONTENTS

Abstract	5
Dedication	6
Acknowledgements	7
CHAPTER 1: INTRODUCTION	
1.0. Introduction	8
1.1. Background to the Study	8
1.2. Theoretical Framework	9
1.3. Literature Review	11
1.4. Research Questions	13
1.5. Objectives of the Study	15
1.6. Research Methodology	15
1.7. Delimitation of the Study	16
1.8. Limitations	16
CHAPTER 2: CORPORATE DISTRESS AS A TRIGGER TO RESCUE	
2.0. Introduction	18
2.1. Background	18
2.2.1. What is Corporate Rescue?	18
2.1.2. The Rise of the Rescue Culture	19
2.1.13. Corporate Rescue in the Insolvency Act, 2018	21
2.2 Corporate Distress as a Trigger to Rescue	23
2.2.1. What is Corporate Distress?	25
2.2.2. Timing of Rescue	25
2.3. Entry Routes into Rescue Proceedings	26
2.3.1. Voluntary Commencement of Rescue Proceedings	27
a) The Company Resolution	27
b) Debtor Friendly Process	28
c) Some Checks and Balances	29
d) Residual Court Interference	30
2.3.2. Compulsory Commencement of Rescue Proceedings	31
a) The Court Application	31
b) Conditions to be Satisfied	32
2.4. Duration of Corporate Rescue Proceedings	34
2.5. Conclusion	36
CHAPTER 3: THE GENERAL MORATORIUM AND CREDITORS' RIGHTS	
3.0. Introduction	38

3.1. The General Moratorium on Legal Proceedings	38
a) The General Moratorium	38
b) Significance of the Moratorium	40
c) Lifting of the Moratorium	41
d) Exceptions to the Moratorium	44
3.2. Protection of Property Interests	46
3.3. Moratorium on Contracts	49
3.4. Rights of Creditors	50
a) Right to Participate in Proceedings	50
b) Independent Creditors	51
c) Creditors' Voting Rights	52
d) Creditors' Committees	53
3.5. Post Commencement Finance	54
3.5.1. Significance of Post Commencement Finance	55
3.5.2. Statutory Super Priority Under the Insolvency Act	56
3.6. Conclusion	58

CHAPTER 4: THE RIGHTS OF EMPLOYEES, SHAREHOLDERS AND DIRECTORS

4.0. Introduction	59
4.1. Rights of Employees	59
4.1.1. Effect of Rescue on Employees and Employees' Contracts	60
4.1.2. Preferential Claim Status of Remuneration	61
4.1.3. Procedural Rights	62
4.1.4. Employees Representative Committees	64
4.2. Rights of Shareholders and Directors	65
4.2.1. Legal Effect of Rescue on Shareholders and Directors	65
4.2.2. Management Displacement	66
4.2.3. Procedural Rights	67
4.3. Conclusion	68

CHAPTER 5: THE POWERS, DUTIES AND QUALIFICATION OF THE CORPORATE RESCUE PRACTITIONER

5.0. Introduction	69
5.1. Appointment and Qualification of a Practitioner	69
a) Appointment of Practitioners	69
b) Qualification of Practitioners	70
5.2. Regulation of Practitioners	72
5.3. Removal from Office of a Practitioner	73
5.4. Powers and Duties of a Practitioner	74
5.5. Investigating the Affairs of the Company	77
5.6. Remuneration of the Practitioner	79
5.7. Conclusion	80

CHAPTER 6: THE CORPORATE RESCUE PLAN	
6.0. Introduction	81
6.1. Development of the Corporate Rescue Plan	81
6.2. Consideration of the Corporate Rescue Plan	85
6.3. Effect of the Approval of the Corporate Rescue Plan	90
6.4. Conclusion	91
 CHAPTER 7: CONCLUSION	
7.0. Introduction	93
7.1. Restating the Purpose of the Research	93
7.2. Summary of the Arguments of the Study	94
7.3. Summary of the Conclusions of the Study	94
7.4. Recommendations	99
7.5. Overall Conclusion	100
 BIBLIOGRAPHY	
Core Texts	101
Articles	102
Law Reform Reports	102
Online Articles	102

ABSTRACT

This work critically reviews the new law in Zimbabwe on Corporate Rescue as provided for in the Insolvency Act [*Chapter 6: 07*]. Zimbabwe has had a Corporate Rescue regime in the Companies Act [*Chapter 24:03*] in form of Judicial Management as first provided for in the 1951 Companies Act and further developed over the years. This concept was borrowed from the South African Companies Act of 1925. Although historically both the South African and Zimbabwean Company Laws have been based on English Company Law, this concept of judicial management was alien to English Law. The revision of our Insolvency Law in the last few years led to the enactment of a new consolidated Insolvency Law that also provides for the modern concept of corporate rescue while the new Companies and Other Business Entities Act [*Chapter 24: 31*] which came into effect on 18 February 2020 no longer provides for corporate insolvency. We seek to unpack the new law on this subject measuring it against normative theories on Corporate Rescue. In other words, we will look at the philosophy behind the “rescue culture” and endeavour to see if the new law helps facilitate companies achieve the intended goals of Corporate Rescue. Key features of Corporate Rescue Law will be analysed in detail.

DEDICATION

I dedicate this work to my wife Bridget and my three children, Ropafadzo, Mufaro and Munashe whom I robbed of quality family time in order to undertake my Masters studies. When I told my sons that I was enrolling for the LLM Programme, they said, “We want good grades from there, just as you demand of us”. I wish the little ones well as they progress with their education. And to my daughter Ropafadzo, I hope you will realise your dream of becoming a leading human rights lawyer.

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CHAPTER 1

INTRODUCTION

1.0 INTRODUCTION

Corporate debt and corporate failure are subjects that have been of interest to law makers because of the importance of corporations to the day to day life of any modern society. This has influenced society to come up with laws that seek to help rehabilitate struggling companies or companies in distress rather than just processing failure in the form of liquidations. This has come to be known as the “rescue culture”. This is the subject of our discussion in this work as we seek to review the new law on corporate rescue in Zimbabwe to see if it promotes the rehabilitation of distressed companies.

1.1 BACKGROUND TO THE STUDY

Zimbabwe enacted a new Insolvency Act [Chapter 6: 07] passed in 2018 seeking to consolidate all insolvency laws in the country. With these changes came the concept of modern Corporate Rescue which has replaced the old judicial management regime. This concept seems to be imported from South Africa’s corporate rescue/ business rescue regime and as we shall see throughout this work, there are a series of identical and near identical provisions on the subject in the South African Companies Act, 2008 and the Zimbabwean Insolvency Act, 2018. The said business rescue procedures in the South African law are modelled along the English and American statutes indicated above¹. The rise of the “rescue culture” globally may be traced to the United States’ 1970s Chapter 11 Corporate Rescue procedures in the Bankruptcy Code of 1978. In England, it was only after the Cork Report of 1982 that Parliament enacted the 1986 Insolvency Act which provided for administration receivership and other related procedures.

¹ F H Cassim ed, *Contemporary Company Law*, 2nd Edition, Juta & Company, 2012. 864

1.2 THEORETICAL FRAMEWORK

No one theory can explain insolvency in general and corporate rescue in particular. How a legal system deals with companies in distress or insolvency in general has considerable influence on attracting investors to make investments in that particular jurisdiction. So important is this subject that the United Nations set up a commission to craft recommendations on model insolvency laws and these also deal with corporate restructuring². But what is the reason why there has been that shift towards rescue? As will be seen in the definition adopted by the legislature in the next chapter, rescue is meant to facilitate corporate **“rehabilitation”** which may be understood to mean returning something to its original state. That has not been, until recently, the historically accepted goal of insolvency law. Liquidation has been the ultimate result of corporate failure. R. Goode puts it aptly when he says that, **“it would be worrying”** if all insolvency would lead to liquidation because **“a company may be financially distressed yet have a viable business that is worth preserving, but liquidation is not a procedure that is well designed to achieve that”**³. It is clear that he was reading from the Cork script which said,

“We believe that a concern for the livelihood and well-being of those dependent upon an enterprise which may be the lifeblood of a whole town or even a region is a legitimate factor to which a modern law of insolvency must have regard. The chain reaction consequences upon any given failure can potentially be so disastrous to creditors, employees and the community that must not be overlooked”.⁴

However, some philosophies that have informed insolvency law for a long time would not be sympathetic to the above views on insolvency. T. H. Jackson’s creditor’s bargain

² See the United Nations Commission on International Trade Law (UNCITRAL) Legislative Guidelines, 2004

³ K Zwieten, *Goode on Principles of Corporate Insolvency Law*, 5th Edition, Sweet & Maxwell, 2018. 39

⁴ K Cork *Insolvency Law and Practice, Report of the Review Committee*, 1982, Cmnd. 8558 (The Cork Report)

theory of insolvency law views insolvency as a collective debt collection process for creditors and as a response to the common pool problem. This theory would be in conflict with the idea of keeping companies in business (something going beyond protecting the interests of creditors) as an independent goal of insolvency law⁵. This theory places creditor interests ahead of any other interests in the face of any insolvency. However, this theory was narrow and other theorists began to advance theories that look at the interests beyond those of creditors to include social and distributional goals, public as well as private interests, and to consider values such as expertise, fairness and accountability.

As noted above, in England it was the Cork Committee that laid the foundation for the rescue culture as they advanced the need to preserve businesses worth saving as commercial enterprises for reasons other than simply advancing the interests of creditors. In the United States however, the Bankruptcy Code of 1978 had already introduced the so called Chapter 11 rescue procedures that emphasised the reorganization of companies. As we shall see throughout this research, the American rescue procedures are different in many ways from the English version of rescue, yet there is a common thread running through them; that businesses should be saved as an alternative to liquidation in the face of an insolvency.

The fact that an insolvency affects constituents beyond creditors is recognized by the Insolvency Act [Chapter 6:07] when it defines what it terms “affected persons” in the context of an insolvency. These are shareholders, creditors and employees (who may be represented by a trade union if there is one to which they belong) of the company to be rescued. It is noteworthy that the list is a closed one and deliberately excludes any other person who may want to claim rights against the insolvent. This is significant because theorists who advance the more communitarian visions of insolvency law have been criticised for advancing theories that may result in indeterminate lists of those affected

⁵ See also D G Baird, “*The Uneasy Case for Corporate Reorganizations*” (1986) 15 *Journal for Legal Studies* 127

by an insolvency. It is opined that indeed a corporate insolvency may affect more than just the listed persons but keeping the list open ended results in an uncertain law. We will end by quoting a South African judge, Binns-Ward J⁶ who had this to say about the rise of the rescue culture;

“It is clear that the legislature has recognised that the liquidation of companies more frequently than not occasions significant collateral damage, both economically and socially, with attendant destruction of wealth and livelihoods. It is obvious that it is in the public interest that the incidence of such adverse socio-economic consequences should be avoided where reasonably possible. Business rescue is intended to serve that public interest by providing a remedy directed at avoiding the deleterious consequences of liquidations in cases in which there is a reasonable prospect of salvaging the business of a company in financial distress, or of securing a better return to creditors than would probably be achieved in an immediate liquidation”.

1.3 LITERATURE REVIEW

Our jurisdiction lags behind in terms of in-depth literature (in form of publications) on corporate rescue and insolvency in general. The situation is compounded by the fact that this concept of corporate rescue as understood in contemporary legal discourse is new to Zimbabwe. However, there has been a lot of literature from abroad especially from common law jurisdictions of South Africa, England and the United States, and the former two jurisdictions share some common legal history with us. Most available and relevant literature centres on corporate rescue as a legal concept. Some writers on the concept like A. Belcher⁷ adopt a multi-disciplinary paradigm arguing that this subject can only be adequately addressed without the blinkers of legal scholarship. It therefore follows that such authors’ definition of corporate rescue tends to be very wide in order to include informal rescue procedures. While accepting the relevance of non-legal interventions in

⁶ In the case of *Koen and Another v Wedgewood Village Golf & Country Estate (Pty) Ltd and Others* 2012 (2) SA 378 (WCC)

⁷ A Belcher, *Corporate Rescue*, Sweet & Maxwell, 1997

addressing corporate failure, this research deliberately leaves those interventions to other disciplines and focuses on formal or legal rescue.

More literature on this subject which helps in a study of this nature has been mostly by authors that deal with the normative theories of corporate rescue law in addition to simply studying the law as it is. English scholars like V. Finch and D. Milman⁸ and American scholars such as T. H. Jackson⁹ and D. Korobkin¹⁰ deal a bit more with the philosophy behind the law on the subject than the traditional study of the law as it is. Other scholars like R. Goode¹¹ discuss more on the law as it is and its historical context. Most South African scholars like F. H. Cassim¹² give insight into the law of South Africa whose provisions in many cases are identical to our law. Reference is also made to the Cork Report¹³ which had so much influence on modern English Insolvency Law from which our law borrows a lot. Some comparative literature on the subject was also quite helpful especially that on the Anglo-American perspective of the law.¹⁴

The research touches on the outgoing judicial management regime in the Companies Act [Chapter 24:03] and as such case law on this subject on any relevant matter will be discussed. There has probably been little or no significant case law so far in Zimbabwe on Corporate Rescue since this is still a new concept and most litigants were still relying on judicial management as provided for in the Companies Act. References will be made to several judicial decisions from law reports not only in Zimbabwe, but from South Africa, England and the United States. Several published and unpublished articles on the subject were also a major component of the literature relied on in this research.

⁸ V Finch & D Milman, *Corporate Insolvency Law*, 3rd Edition, Cambridge University Press, 2017

⁹ T H Jackson, *Bankruptcy, Non-Bankruptcy Entitlements, and the Creditors' Bargain*, Yale Law Journal, 1982

¹⁰ D R Korobkin, *Rehabilitating Values: A Jurisprudence of Bankruptcy*, (1991) 91 Columbia Law Review

¹¹ Zwieten (n. 3 above)

¹² Cassim, (n.1 above)

¹³ The Cork Report (n. 4 above)

¹⁴ For example, G. McCormack, *Corporate Rescue Law – An Anglo-American Perspective*, Edward Elgar Publishing Limited, 2008

1.4 RESEARCH QUESTIONS

Contemporary discourse on the subject of corporate rescue has focused on what the role of the law should be in insolvency. The traditional theory of creditor wealth maximization and creditor's bargain¹⁵ emphasises that insolvency is and should be a collective debt collection mechanism which should at its core protect and advance the interests of creditors. The end result of any insolvency regime should be to maximise returns for creditors. The interests of other groups other than creditors are not important. However, this theory has been criticised in favour of other theories that focus on preserving economically viable businesses that are facing financial distress hence the concept of corporate of business rescue¹⁶. This concept requires a delicate balance of competing interests of the various interested parties like creditors (whether secured, preferential or concurrent), employees, shareholders, managers, customer, suppliers and the community at large. The other relevant question that arises is on the ultimate goal for corporate rescue which is to "rehabilitate"¹⁷ financially distressed companies or businesses. It is difficult to accept that law on its own can achieve this goal and that is why the subject of corporate rescue is a multi-disciplinary subject¹⁸. No model of corporate rescue law can be said to be better than the other in achieving corporate rehabilitation and much also depends on a country's own economic circumstances.

The research will answer the following questions:

1. What is the philosophy behind corporate rescue?

¹⁵ See Jackson (n 9 above)

¹⁶ See Finch & Milman, (n 8 above at pages 28 – 52) for an in-depth discussion on this topic, see also T H Jackson, *The Logic and Limits of Bankruptcy Law*, (Harvard University Press, Cambridge, Mass, 1986), Baird (n 5 above), T H Jackson and R Scott, *On the Nature of Bankruptcy: An Essay on Bankruptcy Sharing and the Creditors' Bargain*, (1989) 75 *Virginia Law Review* 155, D R Korobkin, *Rehabilitating Values: A Jurisprudence of Bankruptcy* (1991) 91 *Columbia Law Review* 717, E Warren, *Bankruptcy Policymaking in an Imperfect World*, (1993) 92 *Michigan Law Review* 336

¹⁷ Section 121 (1) (b) of the Insolvency Act [Chapter 6:07] on definition of "Corporate Rescue"

¹⁸ See Belcher, (n. 7 above)

2. What is the goal of the new Corporate Rescue Regime and does the new law as provided help achieve that goal?
3. What are the key features of the new law on Corporate Rescue which require investigation and critique?
4. Is there room for improvement?

1.5 OBJECTIVES OF THE STUDY

- ❖ To explore the normative theories of corporate rescue in general and to see how they inform our new law.
- ❖ To examine the goals of corporate rescue in general and in terms of our law.
- ❖ To unpack the new law on corporate rescue discussing the essential features of the law.
- ❖ To investigate whether the law as it is will be an upgrade from judicial management.
- ❖ To examine whether the new law promotes and facilitates corporate rescue.
- ❖ To see whether there is any room for improvements on the new law.

1.6 RESEARCH METHODOLOGY

This research is purely doctrinal in nature and focuses on source materials and analysing legal concepts. No empirical studies were done in coming up with any conclusions made herein. In other words, this is a library and desk research. The thrust has been to carry out a theoretical analysis of the new law (as provided for in the new Insolvency Act, 2018) and any other related legal provisions locally. We also studied the case law on this subject not only in Zimbabwe but in other jurisdictions with related legal provisions notably South Africa, England and the United States. The study also focused on core textbooks on this subject from these jurisdictions as well as journal articles by various authors on

the subject. Law reform materials from a few jurisdictions have also been considered especially from jurisdictions where the new law seems to be borrowed. These materials, as indicated above helped in carrying a purely doctrinal research or analysis of the new Zimbabwean Law on Corporate Rescue.

1.7 DELIMITATION OF THE STUDY

This study will focus on critically reviewing the new law on corporate rescue as provided for in the Zimbabwean Insolvency Act of 2018. It is important to note that the new Insolvency Act provides for what it terms corporate rescue proceedings and compromise with creditors¹⁹. Our focus will be on the corporate rescue proceedings and shall exclude compromise with creditors [Consequently, “corporate rescue” in the context of this research, shall mean corporate rescue proceedings that are replacing judicial management and this shall therefore exclude composition with creditors which is replacing schemes of arrangement in terms of the old Companies Act]. Corporate rescue is a multi-disciplinary subject that is of interest to other non-legal professional like finance and business managers as well as chartered accountants and insolvency practitioners. This study will not concern itself with what is of interest to these other disciplines but will merely focus on what the law provides, its role and effectiveness in achieving corporate rehabilitation. In doing so, we will look at the law in South Africa, the United States and England taking into account how the new law was developed. Reference to examples from these countries will be done in investigating the philosophy and goals of insolvency law as well as answering the question whether or not the law can help achieve corporate rehabilitation.

1.8 LIMITATIONS

The foremost limitation has been time constraints especially with the requirement that set deadlines had to be met without fail. One would not be able to sift through all

¹⁹ See Part XXIII of the Act

gathered materials in time to complete the whole process. Efforts had to be made to focus on materials from more reputable authors and publications. Unavailability of essential textbooks on the subject from the University Library or anywhere locally was one of the biggest challenge. The University Law Library had little if any relevant textbooks and journal articles that could be used for postgraduate study on this subject. As a result, the researcher had to make do with text books purchased from the United Kingdom and South Africa and this being a self-financing project, came at a huge cost. Purchasing and shipping to Zimbabwe such books take considerable time and this only added to the time constraints already alluded to above. The comforting result was however that the researcher managed to access the latest essential texts on this subject.

Some materials were also accessed from the internet but most of those readily available materials are not from known or reputable scholars on the subject and hence they were treated with a lot of caution. Proper journal materials accessible via the internet can only be accessed upon payment online and this again was a major constraint. Further, the Zimbabwean government no longer publishes white papers prior to passing legislation and there was very little benefit from these normally helpful materials. Beyond what could be gleaned from bills preceding the new Act, one may not know in detail the rationale behind any new legislation. This is also compounded by lack of any serious debate in Parliament on technical matters such as corporate insolvency.

CHAPTER 2

CORPORATE DISTRESS AS A TRIGGER TO RESCUE

2.0 INTRODUCTION

This chapter deals first with the development of the law on corporate rescue before we deal with the actual provisions of the new law relating to what triggers corporate rescue proceedings (or corporate distress), how these are commenced and the duration of the proceedings. Our main focus will be on financial distress as a trigger to corporate rescue and will distinguish financial distress from economic distress. Comparisons will be made, where possible, with the old law on judicial management. Further comparisons will also be made on key features noted above with positions in other countries, notably positions in South Africa, England and the United States. We will draw conclusions on whether these new provisions really help, at least theoretically, in the intended goal of rehabilitating the ailing corporate entity.

2.1 BACKGROUND

2.1.1 What is Corporate Rescue?

Corporate rescue should be understood to mean procedures that go beyond normal managerial responses to corporate troubles. These may take the form of formal (legal) or informal mechanisms. Attempts have been made to craft a proper definition of what corporate rescue is. A. Belcher, a leading author on this subject, has defined corporate rescue as *“a major intervention necessary to avert eventual failure of a company”*²⁰. This definition is evidently wide as it is meant to include both formal and informal rescue measures adopted in the face of corporate failure. A major intervention necessary to avert eventual failure connotes drastic action at a time of crisis. It therefore follows that managerial interventions to simply grow their business cannot be classified as rescue measures. Key to this concept of rescue is that there should be a crisis or as we will see

²⁰ Belcher, (n7 above p. 12). This definition has been adopted by Finch & Milman, (n. 8 above p. 197 and McCormack, (n. 14 above p. 3).

later on, there should be financial distress which is addressed by entering into rescue proceedings. In our case, these proceedings are those prescribed and regulated by law (formal rescue) as opposed to those informal rescues prescribed by turnaround specialists.

2.1.2 The Rise of the Rescue Culture

Corporate borrowing or simply borrowing is as old as commerce itself. It is borrowing that creates the creditor-debtor relationship. That relationship in turn brings in the concept of insolvency when the borrower (in this case the company) fails to pay its creditors leading to what has been termed “corporate distress”²¹. Law generally and Zimbabwean law on Corporate Insolvency Law in particular has over the years intervened to address corporate failure. Our law has roots in English Law since the subject of corporate insolvency developed together with the development of Company Law. The rise of the modern “rescue culture” in the United States started in the 1970s with enactment of Chapter 11 Corporate Rescue procedures in the Bankruptcy Code of 1978. In England, as already indicated above, it was only after the Cork Report of 1982 that Parliament enacted the 1986 Insolvency Act which provided for administration receivership and other related procedures. This Act was further developed by the Enterprise Act of 2002.

It is however key to note that the concept of judicial management (which is a precursor to the new corporate rescue regime) is alien to English Law. English Law only embraced corporate rescue following recommendations of the Cork Report on Insolvency Law and Practice²² of 1982. On the other hand, Zimbabwe had however borrowed the concept of

²¹ See generally G. Fuller (ed.), *Corporate Borrowings: Law and Practice* (5th Edition, Jordans, Bristol, 2016; E. Ferran and L. C. Ho, *Principles of Corporate Finance Law*, 2nd Edition, Oxford University Press, 2014) and also the *Cork Report* (n. 4above) Chapter 1, especially on paragraph 10, on credit as the “lifeblood of the modern industrialized economy” and “the cornerstone of the trading community”.

²² The Cork Report (n.4 above)

judicial management from South African Law and incorporated this concept in the Rhodesian Companies Act of 1951. Judicial management is a form of corporate rescue and was developed over the years in successive amendments to the 1951 Companies Act especially after the 1993 Christie/Fairburn Report 53²³.

The repeal of the old Insolvency Act [Chapter 6:04] and the enactment of the Insolvency Act [Chapter 6:07] of 2018 generally brought the consolidation of all insolvency legislation which had been fragmented before that. It also introduced the concept of Corporate Rescue the subject matter of this dissertation. Initially the Insolvency Act of 2018 was supposed to be passed simultaneously with a new Companies and Other Business Entities Act which would repealed all provisions on corporate insolvency in the old Companies Act but this could not be done as the new Companies and Other Business Entities Act [Chapter 24:31] could only be passed towards the end of 2019. It only took effect as from 18 February 2020. As a result, from 2018 when we had the new Insolvency Act, up to 18 February 2020, Zimbabwe had the old and new corporate rescue regimes (that is to say those in the old Companies Act [Chapter 24:03] and the new corporate rescue procedures in the new Insolvency Act) applying with equal force of law in any corporate insolvency situation. Companies and litigants had a choice between resorting to Judicial Management in terms of the old Companies Act or Corporate Rescue procedures in terms of the new Insolvency Act of 2018]. The new Companies and Other Business Entities Act of 2019 no longer provides for corporate insolvency ensuring that judicial management will now falls into disuse.

2.1.3 Corporate Rescue in the Insolvency Act, 2018

²³ R. H. Christie, *Business Law in Zimbabwe*, Juta & Co. Ltd 1998. 422, see also M. Tett and N. Chadwick, *Rhodesian Company Law*, University of Rhodesia, 1976, ps. 8 -10 on the historical development of Zimbabwean Company Law in general

Our Corporate Rescue law in the Insolvency Act [Chapter 6:07] of 2018 imports the concept of corporate rescue/ business rescue from South Africa with a series of identical and near identical provisions on the subject. The said business rescue procedures in the South African law are modelled along the English and American statutes indicated above²⁴. The Insolvency Act [Chapter 6:07], 2018 defines what is meant by corporate rescue within the confines of the Act. Section 121 (1) (b) defines “corporate rescue” as;

“proceedings to facilitate the rehabilitation of a company that is financially distressed by providing for -

- (i) The temporary supervision of the company, and of the management of its affairs, business and property; and**
- (ii) A temporary moratorium on the rights of claimants against the company or its property in its possession; and**
- (iii) The development and implementation, if approved, of a plan to rescue the company by restructuring its affairs, business, property, debt and other liabilities, and equity in a manner that maximises the likelihood of the company continuing in existence on a solvent basis or, if it is not possible for the company to so continue in existence, results in a better return for the company’s creditors or shareholders than would result from the immediate liquidation of the company”.**

The definition adopts the commercial insolvency paradigm that is the inability to pay debts²⁵. Various conceptual issues arise from this definition chief of which are that rescue proceedings are there only to play a facilitative role in the achievement of the ultimate goal of rehabilitating a company that has faced financial distress. The word “rehabilitation” is not defined but understood in its ordinary daily use means returning something to its original state. The success or failure of rescue procedures depends very

²⁴ Cassim ed (n.1above p 864)

²⁵ See B Wassman, "Business Rescue: Getting it Right." *De Rebus*, Jan/Feb 2014:36 [2014] *DEREBUS* 4, accessed on [http://www.saflii.org/cgibin/disp.pl?file=za/journals/DEREBUS/2014/4.html&query=%20\[2014\]%20DEREBUS%204](http://www.saflii.org/cgibin/disp.pl?file=za/journals/DEREBUS/2014/4.html&query=%20[2014]%20DEREBUS%204)

much on who does the assessment. Seen through the lenses of a manager or employee who loses his job due to a restructuring, a rescue procedure may be a failure. However, the same procedure may result in a better return for creditors who may then see the process as a success²⁶. A rescue may actually never be a full turnaround of a company since it may result in a sell- off, restructuring, buy outs and so forth. One may in fact conclude that rescue is only partial. The Act recognizes this fact by providing in the above quoted definition, the likelihood of the company not being successfully saved but the end result being better than an immediate liquidation. In other words, a future liquidation done after the company has undergone some rehabilitation is regarded as a rescue.

This also raises the point that a distinction can and should be made between the company and the business as a going concern. It is common for the phrases “corporate rescue” and “business rescue” being used interchangeably as we see in the Insolvency Act [Chapter 6:07], but these two terms may actually be differentiated. A company may in fact be liquidated but aspects of the business may be retained as operational enterprises thereby saving employment of some of the workers and some economic activity being retained. A take-over of a business may result in the business surviving but after having lost its original identity. Consequently, therefore, a distinction is sometimes made between rescue regimes that seek to rescue the company and those that seek to rescue the business as its primary concern.

2.2 CORPORATE DISTRESS AS A TRIGGER

The trigger or key consideration for corporate rescue in terms of the Insolvency Act [Chapter 6:07] is financial distress and this is so whether a company wishes to voluntarily enter into corporate rescue or a court application is made by an affected person seeking

²⁶ Belcher, (n. 7 above ps23 – 24) and Finch & Milman, (n. 8 above ps 197 – 198) and also M. Hunter, “*The Nature and Functions of a Rescue Culture*” [1999] *Journal of Business Law* 491 and R. Harmer, “*Comparison of Trends in National Law: The Pacific Rim*” (1997) 1 *Brooklyn Journal of International Law* 139 at p 143-148

to have the company placed under corporate rescue. Section 122 (1) of the Act provides that when a company seeks to voluntarily commence corporate rescue proceedings, there must be reasonable grounds to believe that the company is “*financially distressed and there appears to be a reasonable prospect of rescuing the company*”. As we shall see when dealing with voluntary commencement of rescue proceedings, there must be reasonable grounds for the board to believe that the company is financially distressed. The board is well placed to know this since it is seized with the management of the company. It is submitted that it should not be mere speculation. Those reasonable grounds should be there to believe that the company has reasonable prospect of being rescued²⁷. Section 124 (4) of the Act further provides that a court considering an application by an affected person to place a company under corporate rescue proceedings must be satisfied before granting such an application that the company is financially distressed or that it has defaulted on paying any amount due under or in terms of a public regulation, or contract with respect to employment related matters. The court may also consider whether it is just and equitable to grant the application for financial reasons. In addition to any of the above, the court must be satisfied that there is a reasonable prospect for rescuing the company.

It seems the law requires a lower burden of proof of this likelihood for rehabilitation because it only requires that there should “appear” that the likelihood to rescue is present²⁸. Corporate rescue law theoretically seeks to distinguish between economically viable businesses and those that are not. Major proponents of the rescue culture like the Cork Committee²⁹ stressed the need to ensure that not every company that is financially

²⁷ See, Wassman (*n.25 above* p 2) where the author says, “The second stage is to prove that a reasonable prospect of success exists. The wording in the Act itself does not, however, provide the standard of proof. It would appear that one need not prove that the rescue will succeed, but merely that reasonable prospects exist. The prospects should thus be objectively assessed and possible and should certainly be demonstrated in any application for business rescue”. The South African Supreme Court has held in the case of *African Banking Corporation of Botswana v Kariba Furniture Manufacturers & Others* (228/2014) [2015] ZASCA 69; 2015 (5) SA 192 (SCA); [2015] 3 All SA 10 (SCA) (20 May 2015) that, “... there can be no dispute that the directors voting in favour of a business rescue must truly believe that prospects of rescue exist and such belief must be based on a concrete foundation”. The same principle was earlier laid down in the case of *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami)(Pty) Ltd* 2013(4) SA 539 (SCA) para 29. It is likely that our courts may be guided by these authorities.

²⁸ Cassim, (*n. 1 above* p.864)

²⁹ See Cork Report, (*n. 4 above* paragraphs 204, 203 and 198 (j).)

distressed automatically qualifies for rescue. Only those companies where there is hope of turning them around should be placed under rescue procedures. Where there is no such reasonable prospect, the company should be liquidated. The court is further given wide discretion to grant an application in terms of Section 124 of the Insolvency Act if it is **“just and equitable to do so for financial reasons”**. The old Companies Act in Section 300 had a similar provision where a court was to consider that it is just and equitable to grant the application. The difference between the two provisions is that in terms of the Insolvency Act, such discretion is limited to considerations of **“financial reasons”** although what constitutes **“financial reasons”** is not defined in the Act. It remains to be seen how the courts will apply this provision.

2.2.1 What is Financial Distress?

“Financial distress” connotes financial trouble or crisis. *“Financially distressed”* is defined in Section 121 of the Act to mean that either it should be apparent that it is reasonably likely that the company will be unable to pay all of its debts as they become due and payable within the immediately ensuing six months or it should appear to be reasonably likely that the company will become insolvent within the immediately ensuing six months. In other words, there should be early signs of financial insolvency. The above provisions were adopted from the South African Companies Act of 2008 in Chapter 6 thereof where there are identical or near identical provisions on the same subject namely Sections 129 (1) and 131 (4). G. McCormack³⁰ stresses that it should be “financial distress” as opposed to “economic distress”. Economic distress implies that the business plan is not working. In other words, the economic model on which the company is grounded suffers from some flaws. Companies suffering from economic distress are not

³⁰ McCormack (n. 14 above p 9) and also generally on the distinction between financial and economic distress, G. Andrade and S. Kaplan *“How Costly is Financial (No Economic) Distress? Evidence from Highly Leveraged Transactions that Became Distressed”* (1998) 53 Journal of Finance 1443, and also D. G. Baird, *“Bankruptcy’s Uncontested Axioms”*, (1998) 108 Yale Law Journal 573 (at 580-583)

good candidates for rescue. He goes on to correctly point out that financial distress implies liquidity problems.

2.2.2 Timing of Rescue

It is key to note that a company has to enter into corporate rescue proceedings in the twilight of insolvency. Put differently, the law now requires that remedial action be taken before it is too late. In terms of Section 300 of the old Companies Act [Chapter24:03], a company could be placed under judicial management when due to mismanagement or some other reasons, it was unable to pay its debts or is being prevented from becoming a successful concern. Inability to pay debts is a sign of insolvency if one uses the cash flow test of ascertaining insolvency (commercial insolvency). As such companies that were already insolvent were candidates for judicial management. On the other hand, however, under corporate rescue, a company should not be in fact insolvent for it to qualify to enter into rescue proceedings (although in compulsory insolvency failure to make contributions relating to employees is a reason for a company to be placed under rescue). The company has to be close to insolvency. That theoretically, sounds like it enhances chances of rescuing or rehabilitating the company if remedial action is taken early in the face of an impending insolvency. Both South Africa and Zimbabwe borrowed the concept of financial distress as a trigger from English Law. On the other hand the Chapter 11 of the American Bankruptcy Code, does not require a company to be financially distressed or facing an insolvency for it to file for restructuring although the courts will require that there be good faith shown to carry out some restructuring³¹. It has been perhaps correctly argued the Chapter 11 is an instrument of debtor relief, not a remedy for creditors³². The apparent removal of the insolvency stigma on the requirements of Chapter 11 regime seems to encourage managers or directors to opt for rescue on time.

³¹ See *Re SGL Carbon Corporation* (1999) 200 F3d 154 where a petition which did not really show a genuine desire to restructure the company was dismissed. See also J L Westbrook, “*A Comparison of Bankruptcy Reorganization in the US with Administration Procedure in the UK*”, (1990) 6 *Insolvency Law & Practice* 90, G Moss, “*Comparative Bankruptcy Cultures: Rescue or Liquidation? Comparisons of Trends in National Law – England*” (1997) 23 *Brooklyn Journal of International Law* 115

³² P. Lewis, “*Corporate Rescue Law in the United States*” in Gromek Broc and Parry, *Corporate Rescue*, page 333

2.3 ENTRY ROUTES INTO RESCUE PROCEEDINGS

The new law retains the voluntary and compulsory methods of commencing rescue proceedings just as the old Companies Act³³ provided for both methods for entering into judicial management. However, the old and new procedures differ markedly. Voluntary entry into rescue no longer requires a court order but just a board resolution to that effect. It is only where an affected person makes a court application seeking an order placing the company under rescue, that resort to court is required. We will discuss these two methods below.

2.3.1 Voluntary Commencement of Rescue Proceedings

a) The Company Resolution

Section 122 (1) of the Insolvency Act now only requires that a company passes a board resolution providing that the company voluntarily commences rescue proceedings and has placed itself under supervision. As already indicated above, the board simply has to be satisfied that there are reasonable grounds to believe that the company is financially distressed and that there appears to be a reasonable prospect of rescuing the company. It is opined that the said resolution is not a special resolution and as such a general meeting cannot pass a resolution to place the company under rescue. Only a recommendation may be made to the board. It should be noted that the company should not allege as has been a requirement under judicial management that the financial distress was as a result of mismanagement by those in charge of the company³⁴. It can be said that what the company intending to undergo voluntary rescue only has to prove is that it may fail to pay its debts when they become due and payable or may become insolvent in six months from the date of the resolution coupled with proving that there

³³ See Sections 299 as read with Sections 300, 199 and 207 of the old Companies Act.

³⁴ See *Ellingbam Trading (Pvt) Ltd v Assistant Master* 2013 (1) ZLR 332 (H) at page 339 para. E – F) where Mutema J reiterated that an applicant company for an order of judicial management has to allege mismanagement in its application.

appears to be reasonable hope to rescue the company. There are conditions set for the resolution to be valid and to take effect, *viz*, that it cannot be passed if liquidation proceedings have been made against the company and secondly it should be filed with the Master of the High Court and the Registrar of Companies (or the Registrar of Co-operative Societies in the case of a co-operative society). Within five days after adopting the resolution, the board must do two mandatory things that is to say, it must give notice of the resolution to all affected persons and this should be accompanied by a sworn statement stating the circumstances on which the board based its decision. Secondly, the company must within that period appoint a consenting corporate rescue practitioner³⁵.

b) Debtor Friendly Process

This commencement method follows the Australian model³⁶ which has also been followed in South Africa³⁷. It is apparent that this procedure is meant to be swift and hurdle free because it does not depend on the court. This is quite unlike the American Chapter 11 rescue proceedings which always have to be commenced by court petition even though almost all of them are commenced voluntarily by the company³⁸. Further, the fact that it is a court-free procedure means it is a significantly cheaper procedure than the voluntary judicial management route of the old Companies Act. It can also be argued that such a straightforward and simple procedure should encourage directors to seek help early in case of a pending insolvency. This is a debtor-friendly system which is quite uncomplicated and easy to implement³⁹ and hence all these factors may work in favour of the rehabilitation of the company. The company making such a resolution has to inform all affected person by standard notice and throughout the corporate rescue

³⁵ See Section 122 (2) and (3)

³⁶ Part 5.3A of the Corporations Act 2001, Section 436 (1)

³⁷ See 129 of the South African Companies Act has a similar provision in terms of wording to the one in the Zimbabwean Insolvency Act

³⁸ See for a general discussion of this, McCormack, (n. 14 above p 123-124)

³⁹ Cassim ed (n. 1 above p 866)

procedures, these consultations are mandatory. It is therefore commendable that the process is inclusive and consultative in nature. All affected parties are guaranteed access to critical information and to participation should they choose to do so. This as well enhances cooperation and possibly encourages rescue.

c) Some Checks and Balances

It should be noted however that such a simple, easy to adopt and implement procedure may be subject to abuse by companies seeking to delay an inevitable liquidation or simply to frustrate their creditors. As such, the law dangles some carrots in form of the advantages stated above but also raises the proverbial whip by providing for strict and tight schedules which if not strictly followed, the resolution lapses. The company is required to file and publish the resolution within five days of its adoption and must appoint a practitioner within two days thereafter or else the resolution lapses. Once the resolution lapses, the company will be precluded from making another resolution seeking rescue within three months thereafter except with the leave of the court upon showing good cause⁴⁰. (Tight schedules are a key feature of the rescue proceedings in general in terms of the Insolvency Act). Additionally, the board of the company that has reasonable grounds to believe that the company is financially distressed but chooses not to make a rescue resolution must give notice to all affected persons stating the criteria for believing that the company is indeed financially distressed and the board's reasons for not adopting a rescue resolution notwithstanding the apparent

⁴⁰ See Section 122 (5) of the Insolvency Act. In South Africa the courts have held the strict procedural requirements should be adhered to without fail see *Advanced Technologies and Engineering Company (Pty) Ltd (in business rescue) v Aéronautique et Technologies Embarquees SA and Others* (GNP) (unreported case no 72522/11, 6-6-2012) (Fabricius J) where the court held that 'It is clear from the relevant sections contained in chapter 6 that a substantial degree of urgency is envisaged once a company has decided to adopt the relevant resolution beginning business rescue proceedings. The purpose of s 129(5), is very plain and blunt. There can be no argument that substantial compliance can ever be sufficient in the given context. If there is non-compliance with s 129(3) or (4) the relevant resolution lapses and is a nullity. There is no other way out, and no question of any condonation or argument pertaining to "substantial compliance".'

financial distress⁴¹. It is opined that this provision helps in alerting any affected person who may develop an interest to petition the court for an order for the company to be placed under rescue proceedings. Secondly such directors who fail to make a resolution for rescue and continue trading in the face of an impending insolvency may find themselves charged with insolvent or reckless trading (although the Act in this section does not state the fate of the directors who fail to pass such a resolution). That should therefore act as an incentive for directors to act responsibly when faced with an insolvency.

d) Residual Court Interference

Further, the Act does not oust the jurisdiction of the court in determining the appropriateness or otherwise of such a resolution as this would have offended against constitutionally guaranteed right of access to the courts in Section 69 (3) of the Constitution of Zimbabwe, 2013. Consequently, and perhaps as an extra measure to ensure that this process is not abused by directors, any affected person has a right to approach the court seeking an order that the resolution be set aside. Such an affected person must show that there is no reasonable belief that the company is financially distressed or secondly that there is no reasonable prospect of rescuing the company⁴² and thirdly that the company has failed to stick to the set procedures provided by law in adopting and giving effect to the resolution⁴³. The court may also be asked to set aside the appointment of a corporate rescue practitioner on the grounds that he does not meet the set qualifications, or that he

⁴¹ Section 122 (7).

⁴² See again the South African cases where the issue of a reasonable prospect of success was discussed, viz, *Kariba Furniture Manufacturers & Others* (228/2014) [2015] ZASCA 69; 2015 (5) SA 192 (SCA); [2015] 3 All SA 10 (SCA) (20 May 2015) and *Oakdene Square Properties (Pty) Ltd v Farm Bothasfontein (Kyalami)(Pty) Ltd* 2013(4) SA 539 (SCA)

⁴³ Section 123 (1) (a) of the Act. The South African Supreme Court of Appeal [when dealing with a similar provision under Section 129 of the Companies Act] has held that there is need to make an application to have the resolution set aside and rejected the argument that the provision seems to give only affected persons the right to apply to court to have the resolution set aside. See *Panamo Properties (Pty) Ltd & another v Nel & another NNO* [2015] ZASCA 76; 2015 (5) SA 63 (SCA) and also *Newton Global Trading (Pty) Ltd v Da Corte* [2015] ZASCA 199. It is likely that the courts in Zimbabwe may find these judgements persuasive and therefore follow them.

is not independent of the company or management or because he lacks the necessary skills having regard to the circumstances of the company⁴⁴. Another key provision meant to discourage abuse of the procedure is that in terms of Section 123 (5) (c), any director who voted for a rescue resolution when in fact the court then finds that there were no reasonable grounds to believe that the company would be unable to pay its debts as they become due and payable, any such director will be ordered to personally bear costs of any application made to set aside the resolution. A director may only escape liability if he shows that he acted in good faith and on the basis of information that the director was entitled to rely on.

2.3.2 Compulsory Commencement of Rescue Proceedings

a) The Court Application

Section 124 (1) of the Insolvency Act provides that an effected person (that is to say, shareholder, creditor, employee or trade union representing the employees of the company) may apply to court seeking an order placing the company under supervision and commencing corporate rescue proceedings. Such an application should be served upon the Master of the High Court, the Registrar of Companies and upon all affected persons⁴⁵. Every affected person has a right to participate in the hearing of the matter. A court considering the application may dismiss the application and make an appropriate order like placing the company in liquidation. The court can also grant the application if is satisfied that the company is financially distressed, or that the company has defaulted on its obligations regarding contributions in respect of employment related matters or it is otherwise just and equitable to do so for financial reasons⁴⁶. Whichever reason the court considers satisfied, there should also be in addition, a reasonable

⁴⁴ Section 123 (1) (b) of the Act

⁴⁵ Section 124 (2) of the Act

⁴⁶ Section 124 (4) of the Act

prospect of rescuing the company, a requirement adopted from English Law. In terms of Section 124 (6), any liquidation proceeding pending against the company will be automatically suspended by an order for corporate rescue. Within five days of the order, the company should notify all affected persons of the granting of the said order.

There are some notable differences with judicial management especially that the Minister of Justice no longer has a right to make the application which he had under the old Companies Act. An employee or his or their trade union now have the right to not only make the application but fully participate in the hearing of the application. Employees could only apply to have a company placed under judicial management if they were creditors and not in their capacity simply as employees. It is apparent that an individual director who is not or part of the company board who are not either shareholders, employees or creditors of the company have no right to make an application for a company to be placed under rescue proceedings.

b) Conditions to be Satisfied by Applicants

Business rescue overrides liquidation because any liquidation should be suspended until rescue proceedings are terminated. This is in line with the underpinning policy of preserving viable commercial enterprises rather than shutting them down by liquidation⁴⁷. What comes out clearly is that corporate rescue is an alternative to liquidation and as such the law requires that rescue be tested first before resorting to liquidation. Further, an order in terms of the law is not there for the taking. The court has to be satisfied that certain conditions have been proven. As such frivolous applications meant to harass a debtor will not find favour with the court. It would however appear that where an applicant alleges that a company has defaulted on payment of any amount due in relation to

⁴⁷ Cassim (n. 1 above p. 873)

employee-related matters, there is no need to prove a series of defaults. One default may be enough because the provision uses the word “any” which denotes even a single default suffices. This position may sound harsh on the debtor but we will leave it to the courts to determine the correct meaning. As already discussed under voluntary rescue court challenges, what the court is asked to consider as “just and equitable for financial reasons” is a new concept and its extent is uncertain. In South Africa a High Court judge had this to say when commenting on the above phrase in their Companies Act, 2008;

“The phrase “it is otherwise just and equitable to do so for financial reasons” is extremely vague. The immediate question arises: “for financial reasons” of whom, the company, the creditors, shareholders or the employees? Since the company cannot apply to court for a business rescue order, as it is not an “affected” person, one can immediately say that the financial reasons of the company are not referred to. However, that would render this provision absurd as it is primarily the financial health of the company which is at stake. I have little doubt that the Legislature never intended such absurdity. I would, therefore, hold that financial reasons relating to all the stakeholders, except that of the practitioner, contemplated in the business rescue provisions, are to be considered by the court when applying this provision”⁴⁸.

The concerns of the court in the above case are appreciated and we wait to see how the local superior courts will interpret this statement.

A reasonable prospect to rescue the company appears to be close to what judges are called upon to consider under English Law where the law states that an **“administration order is reasonably likely to achieve the purpose of the administration”**. The standard of proof seems to be not so rigorous as in England

⁴⁸ *Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others, Farm Bothasfontein (Kyalami) (Pty) Ltd v Kyalami Events and Exhibitions (Pty) Ltd and Others* [2012] ZAGPJHC 12; 2012 (3) SA 273 (GSJ); [2012] 2 All SA 433 (GSJ)

the courts have followed the interpretation that there should be merely a **“real prospect”** of achieving the purposes of the Act⁴⁹. It is submitted that **“a reasonable prospect”** to achieve rescue should be interpreted along the same lines. The prospects should not be fanciful but real. In South Africa⁵⁰ a court held obiter that there should be less a **“reasonable possibility”** or less than a **“reasonable probability”** to rescue the company. In other words, the court went on, what is required is **“more than a mere prima facie case or an arguable possibility. Of even greater significance, I think, is that it must be a reasonable prospect – with the emphasis on ‘reasonable’ – which means that it must be a prospect based on reasonable grounds. A mere speculative suggestion is not enough. Moreover, because it is the applicant who seeks to satisfy the court of the prospect, it must establish these reasonable grounds in accordance with the rules of motion proceedings which, generally speaking, require that it must do so in its founding papers”**.

2.4 DURATION OF CORPORATE RESCUE PROCEEDINGS

“When it comes to business proceedings, the Act envisages a short term approach. This is so for self-evident reasons. There must be a measure of certainty in the commercial world. Creditors should not be left in a state of flux for an indefinite period”⁵¹.

This observation is truthful as we shall see in this section. One feature of the new rescue regime is the requirement to stick to tight schedules. The quicker and shorter the time frames, the less it is likely going to prejudice creditors. It further helps eliminate as far as possible, abuse of rescue procedures. Stating when corporate rescue proceedings commence or terminate also helps in determining when the legal effects of corporate

⁴⁹ See *Re Harris Simons Construction (Pvt) Ltd* [1989] 1 WLR 368; *Re SCL Building Services Ltd* (1989) 5 BCCC 746; *Re Primlaks (UK) Ltd* [1989] BCLC 734

⁵⁰ See *Oakdene Square Properties (Pty) Ltd case Supra*

⁵¹ See the South African case of *Ex parte: Target Shelf 284 CC; Commissioner, South African Revenue Service and Another v Cawood N.O. and Others* [2015] ZAGPPHC 740

rescue are deemed to take effect or end. In terms of Section 125 of the Insolvency Act, 2018, corporate rescue proceedings commence in one of four ways. They commence once a company files a resolution placing itself under supervision or applies to court for consent to file a fresh resolution after the previous one has lapsed. They also commence when an affected person makes an application to court placing the debtor company under corporate rescue. Lastly they commence when, during the course liquidation proceedings, the court instead orders the company to be placed under corporate rescue.

Corporate rescue proceedings end in one of five ways in terms of Section 125 (2) of the Act. They end when the court sets aside a company resolution that placed the company under supervision. They are also terminated when they are converted into liquidation proceedings. The corporate rescue practitioner can also file with the Master of the High Court a notice of termination of the proceedings. They also terminate when a corporate rescue plan is put to the vote in terms of Section 145 of the Act and it is rejected and no affected person acts to extend the proceedings. Lastly, once a corporate rescue plan has been adopted and implemented, the practitioner may also file a notice of substantial implementation of the plan thereby terminating the proceedings. In terms of Section 125 (3) of the Act, corporate rescue proceedings are expected to last for three months unless the court extends the period on application by the practitioner. If the proceedings last longer than three months, the practitioner must prepare a report on the progress of the corporate rescue proceedings, and update it at the end of each subsequent month until the end of the proceedings. The report should be delivered to the court if the proceedings were subject to a court order and to the Master of the High Court in all cases.

Concern can be raised as to the practicability of meeting all the tight schedules especially where an outsider without knowledge of the company is expected to craft a plan that will save the company from liquidation. It must however be borne in mind that judicial management normally would go for indefinite periods with no end in sight. That was one of its drawbacks because the longer it takes to

complete a rescue process, the more the prejudice creditors are likely to suffer than if the company were to proceed to liquidation. Such an indefinite rescue process may also result in abuse by rescue practitioners who draw remuneration from managing the company. So the longer it takes to complete the rescue process, the longer, the practitioner will be drawing some remuneration from the ailing company. As a result, companies with no prospect of being rescued could end up in some “eternal” judicial management proceedings simply because a practitioner is looking at his own interests instead of the interests of the creditors and employees. Much will be seen however, on how effective the tight timelines will be in achieving a quick turnaround of distressed companies.

It is of interest to note that practitioners are required by their Code of Conduct⁵² to ensure that they should keep a diary of his activities complete with reminders for him not to miss deadlines. The same clause provides that an insolvency practitioner who misses deadlines and needs to extend time within which to do something required of him may not be entitled to any remuneration for seeking with the court such extension of time.

2.5 CONCLUSION

The new law on this aspect is different in key areas from the old law on judicial management. In conclusion we can say that the new law on what triggers rescue and entry routes into rescue, seeks firstly to arrest corporate distress early before the situation becomes difficult to reverse and secondly, the procedures prescribed seem to be debtor friendly as they are now simple and mostly court free. Measures however had to be put in place to discourage abuse of the process but encourage genuine rescue cases. Certain unclear portions of the law may be clear once the

⁵² Clause 23 of the Second Schedule to the Estate Administrators Act [Chapter 27:20] inserted by the Estate Administrators Amendment Act, 2018

courts start to pronounce themselves on these matters. By and large the law seems to, at least in theory, encourage rescue because of the features noted above. It may be concluded that a debtor-friendly process helps create the necessary environment for the rehabilitation of an ailing company.

CHAPTER 3

THE GENERAL MORATORIUM AND CREDITORS' RIGHTS

3.0 INTRODUCTION

There are many legal consequences that result from the company being placed under rescue proceedings. These include the general moratorium on legal proceedings against the company, protection of property interests, treatment of post-commencement finance, effect on employees and contracts as well effect on directors and shareholders. One of the key features of the definition of corporate rescue is the temporary moratorium on the rights of claimants against the company or in respect of property in its possession⁵³. Some of the stated legal effects are also closely related to this and will be discussed in turn under this broad heading of the general moratorium. We will deal with the general moratorium on legal proceedings and the effect on contracts and property interests and leave the effect on employees, shareholders and directors to the next chapter. We will also cover the rights of creditors who lose the right to pursue claims due to the moratorium.

3.1 THE GENERAL MORATORIUM ON LEGAL PROCEEDINGS

a) The General Moratorium

This is the foremost legal consequence or stand out feature of the commencement of rescue proceedings. This is a freeze or stay of all legal proceedings and enforcement actions against the company. Section 126 (1) of the Insolvency Act provides that

“During corporate rescue proceedings, no legal proceeding, including enforcement action, against the company, or in relation to any property belonging to the company, or lawfully in its possession, may be commenced or proceeded with in any forum, except –

(a) with the written consent of the practitioner; or

(b) with the leave of the Court and in accordance with the terms the Court considers suitable; or

⁵³ Section 121 (1) (b) of the Act

- (c) 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 corporate rescue proceedings began; or
- (d) criminal proceedings against the company or any of its directors or officers; or
- (e) proceedings concerning any property or right over which the company exercises the powers of a trustee; or
- (f) proceedings by a regulatory authority in the execution of its duties after written notification to the corporate rescue practitioner.”

Further, during corporate rescue proceedings, a guarantee or surety by the company may not be enforced without the leave of the court and in terms of terms and conditions the court may consider just and equitable⁵⁴. Prescription is also suspended whilst the company is under corporate rescue proceedings. Section 126 quoted above is identical to Section 133 of the South African Companies Act of 2008. This concept of a general moratorium on legal proceedings and enforcement action is a common feature between the American Chapter 11 proceedings and English Administration regime.

b) Significance of the Moratorium

*“In any corporate rescue system there needs to be a circuit breaker that provides a breathing space whilst a consideration is given to the prospect of saving the company”*⁵⁵. A distressed company indeed needs a break against enforcement of rights by its creditors if it will realize the intended goal for corporate rescue which is to facilitate rehabilitation of the company that is facing an impending insolvency. It is clear from Section 126 (1) that so long as the corporate rescue proceedings have not yet been terminated in terms of the Act, the moratorium will

⁵⁴ Section 126 (2) of the Act

⁵⁵ C Anderson, *Viewing the Proposed South African Business Rescue Provisions from an Australian Perspective*, *Potchefstroom Electronic Law Journal*, page 6 on <https://www.SAFLII.za>

apply. The philosophy behind the moratorium is that it gives the company some breathing space where the company is given time to focus on reorganisation efforts without being distracted by the demands of the creditors⁵⁶. This moratorium applies to all creditors including secured creditors and those who may have withheld their support for the rescue. There are some differences between the moratorium under the Insolvency Act and that in terms of the old Companies Act. In the latter Act, Section 301 (1) (b-c), the moratorium was not automatic. The law simply stated that an order for judicial management “may” contain directions that there be a stay on proceedings and executions. This, in our view, was correctly interpreted by Zhou J in *Bindura University of Science Education v Tetrad Investment Bank Ltd & Anor*⁵⁷ to mean that the moratorium is granted purely at the discretion of the court. The court is not obliged, as a matter of law, to grant directions on moratorium⁵⁸. Although this interpretation may not find favour with other critics, it is submitted that this wording of the Companies Act presented one of its major weaknesses which had to be addressed by explicitly making the moratorium automatic by operation of law.

It is important to note is that unlike under judicial management, the moratorium covers both pre-rescue and post rescue legal proceedings. The Act provides that no legal proceedings may be “*commenced or proceeded*” with in any forum, without satisfying the listed conditions. It is clear that not only does the moratorium cover new proceedings (*commenced*) but also pre-rescue proceedings (*proceeded*). Under judicial management and as held by Zhou J in the case of *ZFC*

⁵⁶ van Zwieten, (n.3 above p.508). See also statement by the US House of Representatives No. 595, 95th Congress, 1st Session (1977) when Congress was debating the Bankruptcy Bill that was passed into law in 1978 containing the so called Chapter 11 proceedings. Congress stated that the automatic stay “*gives the debtor a breathing spell from its creditors...It permits the debtor to attempt a repayment or reorganization plan, or simply to be relieved of the financial pressures that drove him into bankruptcy*”, (as quoted in McCormack, (n. 14 above p. 156).

⁵⁷ 2017 (1) ZLR 193 (H), page 196 para. E - H

⁵⁸ See also Zhou J in *ZFC Ltd v KM Financial Solutions (Pvt) Ltd & Anor* 2015 (1) ZLR 63 (H) at page 65 para. D – F where the court had this to say; “... *the staying of actions, applications, and execution of writs and summonses in terms of S 301 (1) is not an automatic or inevitable consequence of an order of provisional judicial management. Rather, it is relief which the court in its discretion may grant*”.

*Ltd supra*⁵⁹, Section 301 (1) uses the words “**be stayed and not proceeded with**” and this means only pre-judicial management proceedings could be stayed. He correctly distinguished the wording prohibiting action against a company in liquidation under Section 213 (a) of the old Companies Act where the prohibition uses the wording used now in the Insolvency Act Section 126 (1) and the wording discussed above in Section 301 (1) of the old Companies Act. It is submitted that the Insolvency Act moratorium also applies to vindicatory actions against a company under rescue so long as the property to be vindicated is in lawful possession of the debtor company. As such this covers actions to evict a company under rescue from premises it is renting or recovery of property the debtor company is leasing.

c) Lifting of the Moratorium

A new feature of the new moratorium is that the corporate rescue practitioner may consent in writing that a creditor proceeds with legal process or enforcement action against the company under rescue. A judicial manager has or had no such power to consent to the lifting of the moratorium. It should be assumed that the corporate rescue practitioner should have good reason and would have exercised good judgement to come to a conclusion that the moratorium should be lifted. In England a wrongful refusal by an administrator to allow an owner of goods to repossess them was rendered a ground for the administrator to be held liable to pay compensation to the claimant⁶⁰. Our courts may also be inclined to follow this reasoning.

A creditor can apply to court for leave to commence action or execute against the debtor company if the corporate rescue practitioner turns down a request to lift the moratorium. The old Companies Act did not state the circumstances in which the court may permit

⁵⁹ 2015 (1) ZLR 63 (H) page 66 para. B - F

⁶⁰ See *Barclay Mercantile Business Finance Limited v Sibec Development Ltd* [1992] 1 WLR 1253

legal process to be proceeded with or executed against the company notwithstanding the existence of a judicial management order. It therefore left everything to the discretion of the court. It was held in the above case of *Bindura University of Science Education v Tetrad Investment Bank Ltd & Anor supra* that **“the discretion reposed in the court in respect of execution of a writ of execution against a company which is under judicial management must, like in every case where the court has discretion, be exercised judicially upon a consideration of the relevant factors and circumstances. Where the discretion is conferred by statute, it must be exercised in the light of the objects of the statute concerned”**⁶¹. The judge then went further to state that the court would not readily accede to a request to execute against the company under judicial management where the execution would destroy the company and prejudice all the creditors. It is submitted that the court correctly stated the principles of the law. The Supreme Court recently buttressed this position in the case of *Zambezi Gas Zimbabwe (Pvt) Ltd v N.R. Babber (Pvt) Ltd and Another*⁶². In that case, the court stressed that leave to sue a company under judicial management was required where the action contemplated involved monetary claims that would have an adverse effect on the status of the company in relation to its shareholders and creditors. It seems this case is still persuasive authority under the new law because the Insolvency Act does not also state the circumstances in which the court has to lift the moratorium. The courts are likely to follow the reasoning in this case.

Perhaps our courts may follow the position in England where the Court of Appeal in *Re Atlantic Computer Systems plc (No.1)* ⁶³, had occasion to lay out the guidelines that could assist administrators in deciding whether to grant consent or not. These principles will also be considered in an application for leave to execute or commence action namely:

⁶¹ At page 197 para. A

⁶² SC 3/20 at pages 5 -6 of the cyclostyled judgement

⁶³ [1992] Ch 505 at 542-544

1. The onus is on the applicant to establish a case for leave.
2. The moratorium is intended to assist in achieving the purposes of administration (which is the equivalent of our corporate rescue). If granting leave to the applicant is unlikely to impede those purposes, the leave should normally be given.
3. In other cases, the court should balance the legitimate interests of the Applicant and the legitimate interests of the other creditors of the company.
4. In carrying out the balancing exercise, great importance is normally to be given to the proprietary interest of the Applicant. Administration should not be used to prejudice those who were secured creditors or lessors at the commencement of the administration.
5. It will be sufficient ground for the grant of leave if significant loss would be caused to the applicant by the refusal. But if substantially greater loss would be caused to others by the grant of leave, or loss which is out of all proportion to the benefit which leave would confer on the applicant, that may outweigh the loss to the applicant caused by a refusal.
6. In assessing the respective losses, the court will have regard to matters such as; the financial position of the company; its ability to pay rental arrears and continuing rentals or in case of security, interest thereof, the administrator's proposals, the period for which the administration order has been in force; the effect on the administration if leave is granted and on the applicant if leave is denied; the end result sought to be achieved by the administration; the prospects of that result being achieved and the history of the administration so far.
7. Assessing the probability of the consequences (highlighted above) happening.
8. Other factors such as the conduct of the applicant are relevant.
9. Where the applicant is fully secured delay in enforcement is likely to be less prejudicial than where the security is insufficient.

d) Exceptions to The Moratorium

There are some few exceptions to the general moratorium. Set-off is allowed whether the action resulting in the set-off commenced before or after the company had been placed under rescue. It is however not clear if set-off does not negate the equality of creditors and the rule against preferential treatment in insolvency if the creditor is to benefit ahead of others from the set-off. Further, criminal proceedings are excluded from the general moratorium be they against the company or its officers or directors. This is sound law since the criminal proceedings contemplated may not necessarily hinder the rehabilitation of the company. A company can be sued for a property or right over which it exercises the powers of a trustee. This again is straightforward because in this case the company is not a beneficiary of the property or right but a mere steward. Such right or property does not help it in its rehabilitation. The last exception is that a regulatory authority in the exercise of its regulatory duties only needs to notify the corporate rescue practitioner before commencing legal proceedings. This follows the American position⁶⁴. The reasoning is that the corporate reorganization process should not be permitted to interfere with the operation of essential governmental functions. This exception should in our view apply where a governmental entity is suing a company to prevent or stop a violation of fraud, environmental protection or safety. As G. McCormack⁶⁵ posits correctly, the view is that corporate reorganization proceedings should not, per se, excuse compliance with other laws in the absence of a compelling insolvency-specific justification.

It is important to note that guarantees or surety by the company may only be enforced with the leave of the court. The Corporate Rescue Practitioner has no authority to consent to their enforcement. It is not clear why these have been singled out as different from other creditors where the practitioner has leeway to

⁶⁴ See Section 362 (b) (4) of the Bankruptcy Code, 1978

⁶⁵ McCormack, (n, 14 above p. 161)

consent to commencement of legal action. Lastly, and perhaps in order to balance things, prescription is suspended and time within which to assert a claim, is also suspended while the company is still under rescue.

It should be noted that the moratorium does not blankly prohibit commencement of legal proceedings against a company under rescue. All what it does is to make such commencement subject to the consent of the practitioner or subject to leave by the court. It therefore follows that commencement without such consent or leave does not render the proceedings entirely null and void. Under English law such proceedings may be adjourned while the consent of the practitioner or leave of the court is sought⁶⁶. This is persuasive authority on this matter. Lastly, the term **“legal proceedings”** is not defined and its extent is unknown. F.H. Cassim⁶⁷ argues correctly in our view, that the term should be widely to include quasi-legal proceedings like arbitration and tribunal hearings and he bases this argument on English case law that leans towards the view that such quasi-legal proceedings are covered by the restriction⁶⁸. This position makes sense because arbitration normally results in some need to enforce the award and hence should not be differentiated from formal legal proceedings. This could also be correct because the Act provides that legal proceedings shall not be commenced or proceeded with **“in any forum”**⁶⁹. The words **“in any forum”** accords to a wide meaning which may include formal courts as well as tribunals and arbitrations.

3.2 PROTECTION OF PROPERTY INTERESTS

Section 127 of the Insolvency Act provides for the disposal of property by a company under rescue as well as use by or of property of a company under rescue and it borrows

⁶⁶ Such a position was followed in the English case of *Carr v British International Helicopters Ltd* [1994] 2 BCLC 474 and *Bank of Ireland v Colliers International UK Plc (in administration)* [2013] Ch. 422

⁶⁷ Cassim, (n. 1 above p 881)

⁶⁸ See English cases of *Carr v British International Helicopters Ltd supra*; *Re Railtrack plc* [2002] 1 WLR 3002

⁶⁹ Section 126 (1) of the Insolvency Act

from Section 134 of the South African Companies Act ,2008. Under judicial management regime,⁷⁰ the disposal of company assets was only possible in terms of a court order or in the ordinary course of business. Proceeds therefrom were to be applied towards the payments of judicial management costs, or to pay creditors or to run the business in terms of the judicial management order. Everything was left to judicial discretion since the Act did not define what the court was to consider in granting such leave. The process also added to costs like legal and court fees further burdening an already ailing company. Precious time was also spent approaching the court and this may have affected or impeded the rehabilitation process especially in circumstances where time was of essence. Nothing was provided for regarding the use of property belonging to third parties by the company or the use of the company's property by other parties in lawful possession of such property.

The new provisions in the Insolvency Act are now different and have been broadened. The new law has removed the time consuming process of seeking leave of the court and is now costs effective. This will obviously be to the advantage of the company which requires all the available time and resources to achieve rehabilitation especially considering that this corporate rescue regime requires everything to be done within the shortest possible timeframes. Disposal can still be done in the ordinary course of business or in a bona fide transaction at arm's length for fair value approved in advance and in writing by the practitioner. The latter scenario, in our view, should be a transaction where the corporate rescue practitioner and any buyer of such property are acting independently free from any influence and are acting in their own self-interest with equal bargaining power. Disposal could also be done in pursuance of a corporate rescue plan approved in terms of the Act.

⁷⁰ See Section 307 of the old Companies Act

There could be concern that errant practitioners may abuse this provision. However, and as we shall see in the next chapter, there are considerable safeguards through the regulation of practitioners. The Estate Administrators Act [Chapter 27:20] now requires high standards of honesty and professionalism from practitioners coupled with severe penalties for defaulters. This will be discussed fully in the next chapter. Suffice to say at this stage that Clause 18 of the Second Schedule to the Estate Administrators Act (Code of Ethics for Insolvency Practitioners) clearly amplifies what practitioners have to bear in mind in order to ensure that disposal of an asset of a company under rescue is above board and is viewed as objectively executed. The code discourages disposal of assets immediately upon appointment of an insolvency practitioner or disposal on pre-arranged terms. It also encourages that disposal be done after a valuation of the asset by professional valuers.

Disposal of a property where another person has a security or “*title interest*” is covered by Section 127 (3) of the Act. (It is however unclear what “*title interest*” means and a South African High Court rightly struggled to come up with a meaning to this phrase and in the process lambasted the “shoddy” drafting by the legislature⁷¹. The company intending to dispose such property must first seek the consent of the interested party unless the proceeds to be realised exceeds the company’s indebtedness to that party. Further, the company must pay promptly to the interested party and from the proceeds of the sale all what is due to the interested party or alternatively provide security for the due payment of what is owed or supposed to be paid. The processes have been made simpler, straightforward and cost effective.

Any third party using property belonging to the company under rescue in terms of a valid contract made in ordinary course of business prior to the company entering rescue,

⁷¹ *JVJ Logistics (Pty) Ltd v Standard Bank of South Africa Ltd and Others* (7076/2015) [2016] ZAKZDHC 24; [2016] 3 All SA 813 (KZD); 2016 (6) SA 448 (KZD). The court concluded that this phrase did not mean ownership, something it is normally taken to mean but was close to “security interest”.

may continue to use such property in terms of that agreement unless the practitioner chooses to suspend the contract as we shall see below when dealing with effect of rescue on contracts. Further, and despite whatever is contained in any contract, no person may exercise any rights in respect of any property in the lawful possession of the company, whether this property belongs to the company or not, except to the extent that the practitioner consents in writing. The practitioner shall not unreasonably withhold this consent having regard to the purposes of corporate rescue, the circumstances of the company and the nature of the property and the rights claimed in respect of it. This may relate to leases which may be critical to the operation of the company and such a restriction may work in favour of the company. It is submitted that any person who is not satisfied by the withholding of consent by the practitioner is entitled to assert his right in a court of law if regard is had to the right to use one's property in terms of Section 71 (2) of the Constitution of Zimbabwe, 2013. The law itself is in our view constitutional since the affected third party is deprived of the use of his property in terms of a law of general application.

3.3 MORATORIUM ON CONTRACTS

The old Companies Act did not provide for suspension or cancellation of contracts. This matter was left to the laws relating to contract. Section 129 of the Insolvency Act now addresses this matter. A struggling company may find it difficult or impossible to discharge its obligations in terms of contracts it may have lawfully entered into with third parties. Compelling such a company to perform its obligations arising from such contracts during its rehabilitation period may hamper the achievement of the chief goal of corporate rescue. At the same time the rights of the other parties involved should be preserved or protected. This therefore calls for balance between the competing interests. Section 129 (2), (3) and (4) provide for suspension and cancellation of contracts. A corporate rescue practitioner may suspend a contract to which the company is a party either entirely or partially or conditionally, for the duration of the corporate rescue proceedings. Once the practitioner suspends the contract, the other party is by operation

of law bound by such suspension. The law allows the aggrieved party to assert a claim for damages against the company. The Corporate rescue practitioner has no power to unilaterally cancel contracts as he is supposed to first seek the leave of the court to cancel any contracts. Where a court cancels a contract in terms of this section, the other party to the contract loses his right to seek specific performance. The law provides for a safeguard in that the party who had contracted the company under rescue will be entitled to claim damages. The suspension or cancellation does not also apply to certain contracts covered by Section 35 and 36 of the Act as well as employment contracts which will be discussed in the next chapter.

3.4 RIGHTS OF CREDITORS

Creditors have traditionally been the major concern of insolvency law especially where the philosophy of the law has been that insolvency law is all about collective debt collection. An insolvent company's creditors expect to recover as much as is possible whether the company is liquidated or is rescued. The automatic moratorium against these creditors means that they are deprived of their right to immediately take recovery measures against the company under rescue and as such the law should grant them something in return. What they get in return are the rights we are going to look at here. Generally speaking, creditors of a company under rescue have similar rights to those creditors of a company under judicial management, that is to say creditors are given the right to influence the way the company is run during the rescue procedure.

a) Right to Participate in Proceedings

We have already noted in previous chapter, the right of creditors to initiate the rescue process by making an application to court to commence rescue or an application to object to a rescue resolution as we dealt with the Chapter 2 above. Here we will look at the rights that creditors have when the company is now under rescue. Section 138 of the Insolvency Act deals with the rights of creditors and this is modelled along the provisions of Section 145 of the South African Companies Act, 2008. Creditors are accorded the right to receive notice of each court

proceeding, decision, meeting or other relevant event concerning the corporate rescue proceedings⁷². What is “relevant event” is not defined and it would appear the Master and the practitioner have discretion to determine whether an event is relevant enough to require them to give notice to the creditors. A creditor has the right to participate in any court proceedings arising during corporate rescue⁷³. The creditor has the right to participate formally and informally in the crafting and adoption of the corporate rescue plan⁷⁴. To this end the creditors have the right to vote to amend, approve or reject a rescue plan and if it is rejected to propose the development of an alternative plan as well as acquiring the voting interests of all other creditors⁷⁵. The common thread running through the above provisions is that the creditors are given room, as much as is possible, to participate in the whole rescue process.

b) Independent Creditors

In terms of Section 138 (5) of the Act, the practitioner must determine whether or not a creditor is independent for purposes of the Act. This aspect is important and what is an “**independent creditor**” is defined in Section 121 (1) of the Act as a creditor (including an employee) who is not related to the company or director or the rescue practitioner of the company. There are certain things creditors who are not independent are not allowed by the law to do for example constituting a creditors’ committee as we shall see below. Independence is one of the key aspects we have looked at when we dealt with the practitioner. The law expects the process to have integrity and free from manipulation by creditors who may have their judgment influenced unduly by their connections to the company, its directors or the corporate rescue practitioner. This aspect of independence was not as refined in the old Companies Act in respect of companies under judicial

⁷² Section 138 (1) (a) of the Act

⁷³ Section 138 (1) (b) of the Act

⁷⁴ Section 138 (1) (b) and (c) of the Act

⁷⁵ Section 138 (2) of the Act

management as it is now. In practice, subsidiaries or other related companies and creditors of a company under judicial management could use their positions and influence to vote at meetings to approve or disapprove certain things much to the detriment of independent creditors.

c) Creditors' Voting Rights

Voting by creditors is governed by Section 138 (4) of the Insolvency Act. Secured and unsecured creditors have a voting interest equal to the amount owed by the company. In other words, the voting interest is proportional to the value of the debt owed. The bigger the debt, the bigger the voting interest. This obviously creates fairness in the whole voting process and this has been the voting procedures under the repealed Insolvency Act. Any creditor whose claim was subordinated to another claim has a voting interest equal to what he possibly could have recovered if the company were to be liquidated. A suitably qualified person may be engaged to do a proper valuation of the subordinated claim. Anyone not satisfied with such valuation may take the decision on review. This is done to protect the interest of the creditor whose claim may not be readily determinable. The central feature here is the equality of creditors and safeguards as provided where the creditor's claim may not be easily ascertainable.

According to Section 140 (1) of the Act, the first creditors meeting must be convened and presided over by the Master 15 (fifteen) business days after the appointment of the practitioner. At that meeting the Master must inform the creditors whether or not he believes that there is a reasonable prospect of rescuing the company and may receive proof of claims. This section is not clear since it simply says **"within 15 business days after being appointed, the Master must convene and preside over, a first meeting of creditors..."** It does not state whose appointment is being referred to but it seems it is that of the practitioner. This is one of the many areas where the drafting of the Act is poor especially where the

drafters were borrowing heavily from the South African Companies Act, 2008. The South African equivalent (Section 147 of the Companies Act, 2008) provides that it is the practitioner who makes the opinion on whether or not he sees prospects of rescue and he makes that opinion at the creditors' meeting convened 10 business days after his appointment. We have seen in Section 134 (1) of the Insolvency Act that the practitioner must as soon as possible after his appointment, investigate the affairs of the company and thereafter formulate an opinion as to whether there is any reasonable prospect of the company being rescued. It would appear that the Master's opinion would be informed by the report and opinion of the practitioner done in terms of Section 134 (1). Proper notice as provided for should be given prior to the meeting and all creditors whose addresses are known or can be reasonably be obtained by the Master, should be served with notice of this meeting. This is important and ensures that the outcome of the meeting is not faulted by anyone who could not attend the meeting because he was not served with notice. The Master is only bound to serve notice on those whose addresses are known or could be obtained. Voting at this meeting is by simple majority of independent creditors.

d) Creditors' Committees

Section 138 (3) creates the right of creditors to form creditors' committees through whom the practitioner may consult the creditors during the development of the corporate rescue plan. As we have argued in respect of employees, this provision works well in curtailing the consultative process. The committee has functions spelt out (unlike the employees' committee)⁷⁶. The purpose of the committee is to consult with the practitioner on any matter related to the rescue proceedings but

⁷⁶ Section 141 of the Act

shall not have power to direct or instruct the practitioner. This is important so as to maintain a balance between the need to consult and maintaining the independence of the practitioner. The committee may, on behalf of the general body of the creditors receive and consider reports by the practitioner. It must however always act independently of the practitioner so as to ensure that it acts in an unbiased manner in representing the interests of creditors. The election of this committee is done at the first creditors' meeting as provided for in Section 140 (1) of the Act. Only independent creditors may constitute the creditors committee personally or by proxy. This is crucial so as to maintain the independence of the committee.

One aspect which we may have to explore is whether or not the costs incurred by the creditors in attending to or discharging the business of the committee are costs recoverable from the company as costs of rescue. The commitment of the elected creditors (especially those with small unsecured claims) to the business of the creditors' committee may be affected if for example a creditors' claim gets diminished by inflation or simply by incurring costs to attend to the business of the committee especially if such costs are not recoverable as claims (possibly preferential claims) against the company. Only those creditors with big claims who have much at stake may end up participating in order to protect their interests. It is suggested that in order to encourage participation of creditors in the creditors' committees, all reasonable expenses they incur are recoverable against the company as costs of rescue. That may promote the participation of all creditors small or big.

3.5 POST-COMMENCEMENT FINANCE

We have looked above at the rights of creditors but there is a category of creditors which calls for some detailed analysis. These are creditors who finance the company while

under rescue proceedings, or what has come to be known as post-commencement finance.

3.4.1 Significance of Post Commencement Finance

It is undeniable that new finance is often critical to the survival of a distressed company. Unless such finance is available from some other source, a company may be forced to sell some of its assets at break-up value in order to raise finance for the business something This may affect the efforts to rehabilitate the ailing company thus leading to liquidation (something which corporate rescue is meant to avoid). New lenders may have no great incentive to lend the distressed company since such loans run the risk of not being repaid in full. Corporate assets may already have been fully secured by pre-rescue creditors. Those existing lenders may be reluctant to increase their exposure or perhaps may want to extend further loans at exorbitant interest rates. (In any event these existing lenders may already be owed huge sums of money which they are not permitted to claim due to the moratorium). The law is therefore expected to respond to this scenario in order to enhance the survival chances of the distressed company. The United States Bankruptcy Code therefore pioneered the so called “super-priority” status to all post-rescue finance. In other words, this financing is given priority to pre-rescue creditors in terms of being paid or in case of insolvency. Therefore financing companies in difficulties has grown into big business in America⁷⁷. A. Belcher⁷⁸ calls this super-priority, “queue-jumping” meaning that the queue is the ranking of creditors in a winding up and creditors in an insolvency would try to improve their position in this ranking order⁷⁹.

3.4.2 Statutory Super-Priority under the Insolvency Act

⁷⁷ Referred to as “DIP” financing or “debtor-in-possession” financing- see McCormack, (n. 14 above p. 176).

⁷⁸ Belcher, (n. 7 above p. 161)

⁷⁹ The British Parliament rejected an amendment of the Insolvency Act in 2002 that would have created a statutory framework for super-priority finance after commencement of corporate rescue (see House of Lords parliamentary debates for 29 July 2002 and the discussion in S Davies, *ed Insolvency and the Enterprise Act 2002*. (Bristol, Jordans, 2003) at pages 20-26). It was decided to leave the whole issue to the judgement of the lending market since the decision whether to lend or not was a commercial decision which should not be interfered by the law.

Statutory super-priority has therefore been accepted in South Africa⁸⁰ from which our Insolvency Act, 2018 borrowed the concept in the form of an identical Section 128. Section 128 provides that any post-rescue remuneration or reimbursement for expenses or any amount due to any employee arising from his employment, shall be treated as post-commencement finance having the same status as all financing obtained by the company during corporate rescue in form of debt financing. This post-rescue debt financing (other than that relating to employee dues) may be secured with any available company assets. However post-rescue finance relating to employee dues stated above will have preference over any debt financing sourced by the company to run the business during rescue irrespective of whether such debt financing is secured or not⁸¹. The preference also extends to all unsecured pre-rescue creditors. All other post-rescue finance other than that relating to employees, will have preference in the order in which they were incurred over all unsecured creditors of the company. If rescue fails and the company is liquidated, the super-priority status of the finance stated above is maintained⁸². It is clear that the treatment of post-rescue employee dues as post-commencement finance with super-priority was meant to protect workers. The importance of workers to any enterprise in distress has been discussed elsewhere in this work. What is of more interest really is post-rescue finance which a company obtains in order to run the business. This may take many forms of debt financing.

This super-priority concept is not new as it existed in the old companies Act in respect of judicial management albeit in a different form⁸³. It was not automatic. It was only conferred upon post judicial management creditors if by resolution at a properly convened meeting, the pre-judicial management creditors voted for a resolution creating this super-priority status. So if the adoption of the resolution was to fail, no super-priority status existed for post judicial management creditors. This was one of the weaknesses of

⁸⁰ Section 135 of the Companies Act, 2008

⁸¹ Section 128 (3) of the Act

⁸² Section 128 (4) of the Act

⁸³ Section 309 of the old Companies Act

the judicial management regime. This super-priority concept has however been rejected in England and the Enterprise Act, 2002 does not explicitly provide for the concept. G. McCormack⁸⁴ argues that the British Parliament was cautious not to create a **“situation that would essentially guarantee a return to lenders advancing funds on the basis of such priority irrespective of the commercial viability of the rescue proposals. In its view, the issue of whether to lend to a company in administration was a commercial one that was best left to the commercial judgement of the lending market”**. In any case replicating the United States Chapter 11 in the UK would not have been good because of the differences in the business culture and business environment. K. van Zwieten⁸⁵ notes that in England efforts to up to 2016 by the Insolvency Service have not yielded anything towards statutory super-priority because those interviewed noted that post administration finance rarely affects the administration⁸⁶. The writer notes that this is unsurprising because the rise of “pre-packaged” rescue measures, businesses are sold swiftly after commencement and the issue of finance becomes irrelevant. It is only in trading administration that this issue has salience. That said, we submit that statutory super-priority in the form provided for in the Insolvency Act is far better than that in the old Companies Act and the new provisions may go a long way in facilitating rescue. The new process is not time consuming especially with the strict timelines under corporate rescue. There is also much certainty that helps decision makers from both the lender’s side and the borrower.

3.6 CONCLUSION

The legal effect of corporate rescue is now more defined under corporate rescue and have been improved to match contemporary positions in jurisdictions that share a common legal history as us. The automatic statutory moratorium on legal proceedings is a new feature which has been celebrated in America and England and is a welcome

⁸⁴ (n. 14 above p. 176)

⁸⁵ (n. 3 above p. 546)

⁸⁶ “*A Review of the Corporate Insolvency Framework: Summary of Responses*”, (2016) at [5.2]

development. Automatic statutory “super-priority” for post rescue finance is another new development that encourages lenders to extend credit to companies in financial distress as this super-priority status of their finance is an incentive. The corporate rescue practitioner, as we shall also see in the next chapter, has been given more power to make key decisions which under judicial management normally required leave of the court. This also as we have noted above helps save time and financial resources and what is required is to ensure that the system is not abused through strict regulation of practitioners. All in all, the new law in the areas covered so far is indeed an upgrade from judicial management and theoretically, it is believed that the law may help in rehabilitating financially distressed companies.

CHAPTER 4

THE RIGHTS OF EMPLOYEES, SHREHOLDERS AND DIRECTORS

4.0 INTRODUCTION

The Insolvency Act now provides for a closed list of “affected persons” and we have touched on this term in the preceding chapters. This group is constituted by employees, creditors and holders of company securities. We will investigate what rights are accorded these groups during rescue. Some of these rights have already been looked at for example

the rights of affected persons to initiate rescue proceedings, right to object to a rescue resolution or appointment of a practitioner. We will now look at the right to be furnished with all relevant notices and court papers and the right to participate in the rescue process as well as receiving updates. Comparisons will be made with regimes in South Africa, United States and England.

4.1 RIGHTS OF EMPLOYEES

“For employees of a financially distressed company, there is seldom a more emotionally wrenching issue than the treatment of their wage and benefit claims in a restructuring process. Employees, who are the lifeblood of the enterprise, too often find that they are treated as expendable and their pension or retirement savings may have evaporated. Stories about the loss of employee benefits and resulting hardships abound in the newspapers throughout the world. The legacy costs associated with employee wages, benefits and pension claims can be enormous and are often among the most intractable issues confronted in a restructuring company”⁸⁷ Employees and their representatives, the trades unions, should be considered key actors in the process, and require a voice if their interests are to be taken into account. The fate of employees cannot be remedied while they are not represented at the bargaining table. Some questions therefore need to be asked of the actors if the law’s aims around improved corporate recovery are to be achieved. It has been said that **“the insolvency of a company may prove traumatic for employees, especially those who have invested years of effort and skill in the enterprise”**⁸⁸.

⁸⁷ International Association of Restructuring, Insolvency & Bankruptcy Professionals, Report of 2005, see also the position of the World Bank which has called for special treatment of employee claims during insolvency, recognizing that workers are a vital part of an enterprise. It suggests that careful consideration should be given to balancing the rights of employees with those of other creditors, (see World Bank, *Principles and Guidelines for Effective Insolvency and Creditor Rights Systems*, (World Bank, 2001).

⁸⁸ Finch & Milman, (n. 8 above p. 645), and for further detail on the subject see also D Pollard, *Corporate Insolvency: Employment and Pension Rights*, 5th Edition, Bloomsbury Professional, Haywards Heath, 2013

The truth of this statement may not be overstated. One of the foremost goal of corporate rescue is to save employment. Saving employment is more than a legal issue but a moral as well as political issue. However, the goal to save employment has to be delicately balanced with the interests of other interested parties like creditors. G. McCormack⁸⁹ notes that companies experiencing financial difficulties may often blame labour or employment costs for their failure to make a sufficient profit. Some critical questions have to be asked like are employees given an appropriate voice within the schemes of accountability that operate in insolvency? Does the law create rights to employees that are fair? Or do employees really need any special protection different from other affected constituencies like creditors? It becomes apparent therefore that there arises some need to offer some protection to employees.

4.1.1 Effect of Rescue on Employees and Employee Contracts

The law recognizes some form of protection to employees in Section 129 (1) of the insolvency Act which has an equivalent provision in the South African Companies Act⁹⁰ with almost identical wording. This common position is borrowed from the English Insolvency Act, Section 248 (as amended by the Enterprise Act of 2002). Employee contracts entered into immediately prior to rescue are protected and will continue subsisting except to the extent that changes may occur in the ordinary course of attrition or the parties to the contract agree by mutual consent to the amendment of such employment contracts. Any retrenchment will also be done in terms of the applicable labour laws. Such contracts shall not be suspended by the practitioner in the exercise of his general powers to suspend certain contracts. The law here does not seek to bar any restructuring of a company in a way that may involve reducing a company's workforce or termination of contracts of employees whose skills may no longer be

⁸⁹ McCormack, (n.14 above p. 209)

⁹⁰ See Section 136 (1) of the South African Companies Act. Different jurisdictions adopt different models and for further reading see, J Sarra, *Recognizing Workers' Economic Contributions: The Treatment of Employee and Pension Claims During Company Insolvency, A Comparative Study of 62 Jurisdictions*, Research funding by the University of British Columbia Faculty of Law, the International Insolvency Institute and the Social Sciences and Humanities Research Council of Canada, University of Columbia, 2008.

required in terms of the restructuring. All it does is to ensure that contracts are not arbitrarily terminated and that any termination has to be with appropriate compensation in terms of retrenchment packages. Changes can also happen lawfully for example where employee contracts are terminated due to death of the employee or due to lawful disciplinary proceedings.

4.1.2 Preferential Treatment of Pre-Commencement Remuneration

The law adopts a model that creates statutory super-priority to all pre-commencement employee related debt owed to an employee remains a preferential claim against the company⁹¹. This super-priority is necessary as an incentive to employees who are a key constituency in the quest to turn around the fortunes of the struggling company. Treating employees' dues in any other way would perhaps leave them without the motivation to continue working for the company and cooperating with the insolvency practitioner in his efforts to revive the ailing company. As we have seen above the philosophy in support of preferential treatment of workers is that business must, in the face of insolvency, remember the plight of workers as a moral issue as one author said; "But when the demands of doing business conflict with the morality or well-being of society, it is business that has to yield, and this, perhaps, is the ultimate point of business ethics".⁹²

4.1.3 Procedural Rights

The rights that are accorded by the Insolvency Act as we shall see in this part are in addition to any other rights arising or accruing in terms of any law, contract, collective agreement, shareholding, security or Court order⁹³. In other words, the Insolvency Act does not seek to take away any rights of employees they have as against the company upon commencement of rescue but only seek to add to those rights. The rights which are created by the Insolvency Act are more of procedural rights than substantive rights. This

⁹¹ Section 137 (2) of the Act

⁹² B. Solomon, *Business Ethics, in A Companion to Ethics*, ed. Singer, Blackwell, Oxford, 199, p.364

⁹³ Section 137 (5) of the Act

is in keeping with the philosophy that insolvency law should not create any substantive rights. Such substantive rights must be left to other branches of law and that is precisely why the Act states that rights accruing to employees by operation of any other law, contract or court order, remain unchanged. As we have already noticed in the previous chapters hereto, employees have some rights in respect of making court applications commencing rescue whether in their capacity as just employees or as creditors. They also have the right to be served with all notices and court papers regarding rescue proceedings. Their contracts are protected and any entitlement due to them post-commencement are ranked as preferred claims. They may also challenge the appointment of a rescue practitioner and propose the appointment of a replacement. Those rights mainly refer to the rights accorded to employees as part of the group known as affected persons. We will not go again into any detail about those rights which we have already discussed but will focus on other employee protection rights accorded by the Act to employees in their capacity as employees and not as part of the broader group of affected persons. Employee protection is a feature that is conspicuous or stronger under English Law (and the South African Law) than in the United States⁹⁴. American philosophy is that freedom of contract should prevail and leaves employment matters largely unregulated. The reasoning is that restructuring operations could be frustrated or seriously impeded if the company's ability to reduce its workforce is restricted, or if the corporate decision making process is heavily burdened⁹⁵.

Section 137 of the Insolvency Act deals with the rights accorded to employees during rescue. Section 137 (1) guarantees the right of employees to participate in rescue proceedings either individually or through a trade union of their choice which may be representing them or by proxy through an employee organization or representative. This provision is welcome to both employees and other affected person or stakeholders since

⁹⁴ See generally McCormack, (n. 14 above p. 209) and Cassim *ed.* (n. 1 above p. 809)

⁹⁵ McCormack *ibid* quoting D. Skeel Jr, "*Employees, Pensions, and Government in Chapter 11*", (2004) 82 Wash University Law Quarterly 1469 at 1472. As such Chapter 11 bankruptcy procedures do not seek to protect employees.

a company under rescue may have thousands of employees and creditors. This huge number may make it very difficult to deal with them as individuals. The Section 137 (3) guarantees participation of employees (either individually or through their trade union) in all relevant matters relating to the rescue processes. These include the right to be notified by standard notice of all court proceedings, decision, meeting or other relevant event concerning the corporate rescue proceedings. This is in accordance with the consultative nature of the rescue proceedings as stated in Chapter 2. Employees also have a right to participate in any court proceedings arising during rescue. They also play a part in formulation of a rescue plan by the rescue practitioner who has to afford employees the right to be consulted. They can also attend a meeting called to consider a proposed rescue plan and to present and make submissions at that meeting. They have a right to vote with other affected persons for or against a rescue plan but only to the extent that the employees are creditors. They can also propose to develop an alternative rescue plan to a rescue plan that may be rejected at a meeting called to consider a proposed rescue plan. The law fully recognizes the collective rights of employees by allowing them to be represented by their trade unions. Trade unions provide strength in numbers especially considering the bargaining that is expected in coming up with the corporate rescue plan.

4.1.4 Employees' Representative Committees

Employees are generally affected by restructuring of a distressed company in that they may be retrenched, be asked to take pay cuts, the business may be sold and so forth and it makes much sense to grant participatory rights to such employees. One way employees are expected to exercise their collective rights is by forming what the Act calls "a committee of employees' representatives"⁹⁶. Unlike the South African Companies Act⁹⁷, which provides details on the functions of the committee of employee's representatives, the Insolvency Act, which has borrowed much of the provisions relating to rights of affected person from the

⁹⁶ Section 137 (3) (c) of the Act

⁹⁷ Section 144 (3) (c) of the Companies Act, 2008 as read with Sections 148 and 149 of the same Act

South Africa Companies Act, says nothing else about the committee of employee's representatives. Unless the Act is amended to clarify this issue, either this supposedly noble provision may fall into disuse or may simply create confusion in practice. The last issue to note regarding employees is that of a medical scheme or pension scheme for the benefit of employees which is classified as a "right" but seems like there is no right being created. Any amounts due by the distressed company under rescue are unsecured claims whether they arise prior or post commencement of rescue⁹⁸. It is not clear what the reasoning is behind this provision especially when all other dues for the benefit of employees are regarded as preferential claims.

4.2 RIGHTS OF SHAREHOLDERS AND DIRECTORS

4.2.1 Legal Effect of Rescue on Shareholders and Directors

In terms of Section 130 (1) of the Insolvency Act, 2018, the classification or status of issued company securities (other than transfer of securities in the course of business) does not change unless the High Court directs otherwise or any changes are done as part of the implementation of a corporate rescue plan. This position is the same as in South Africa⁹⁹. The effect of corporate rescue on directors is what differs in Zimbabwe and South Africa. The Insolvency Act retains the management displacement paradigm of the old Companies Act. Section 301 (1) (b) of the old Companies Act clearly provides that a judicial management order must contain a provision that once a provisional judicial manager is appointed, any other person vested with the management of the company shall from the date of the order be divested of the management role. Section 130 (2) of the Insolvency Act provides in no uncertain terms that during corporate rescue proceedings, the board of the company will be deemed to be dissolved and each of the individual

⁹⁸ Section 137 (4) of the Act

⁹⁹ Section 137 (1) of the Companies Act, 2008

director may no longer act as director and may only exercise a management role within the company in accordance with the express instructions or direction of the practitioner to the extent that it is reasonable to do so. Each director is however required by law to attend to the requests of the corporate rescue practitioner at all times and to provide the practitioner with all information about the company's affairs as may be reasonably required¹⁰⁰. Any action purportedly taken by a director during corporate rescue shall be null and void unless approved by the corporate rescue practitioner¹⁰¹.

4.2.2 Management Displacement

Management displacement is a key feature of the English corporate rescue regime and this is in line with the historical development of corporate insolvency law in English Law which placed so much emphasis on fault by the old management and the protection of creditors' interests¹⁰². American Chapter 11 by contrast favours retention of the pre-petition management under the "Debtor-in-Possession" arrangement. G. Moss observed the English cultural emphasis on fault and had this to say; **"In England insolvency, including corporate insolvency, is regarded as a disgrace.... In the United States business failure is very often thought of as a misfortune rather than a wrongdoing."**¹⁰³

Management displacement ensures that the managers who are considered guilty of getting the company into distress due to mismanagement are removed from the helm of the company in favour of a rescue practitioner. G. Moss famously criticized the American debtor-in-possession arrangement as something akin to "leaving an alcoholic in charge of a pub"¹⁰⁴ because it is generally thought that mismanagement leads to corporate failure. This appears to be the philosophy that

¹⁰⁰ Section 130 (3) of the Insolvency Act

¹⁰¹ Section 130 (4) of the Insolvency Act

¹⁰² Finch & Milman, (n. 8 above p. 229)

¹⁰³ G. Moss "*Chapter 11*", page 18, quoted by Finch & Milman, *supra* p. 231

¹⁰⁴ G. Moss *supra* page 19, quoted by Finch & Milman, *ibid* p. 237

informed our new law in this respect. However, it can be argued as well that corporate troubles do not always stem from mismanagement but other issues like credit pressure and other outside factors.

It can be argued that retaining the pre-rescue management has some advantages in that this management comprises of people most familiar with and the best equipped to know the financial affairs of the company and the extent of its difficulties. The South African model¹⁰⁵ borrows from both English Law and Chapter 11, and in England the board of directors is not dissolved but should work under the direction or control of the corporate rescue practitioner. This may create problems on the control of the company especially if the practitioner's directions and control is not specific. The Zimbabwean approach seems better by simply requiring that the directors are legally required to co-operate with the practitioner and the practitioner may assign management roles to a director as the practitioner thinks appropriate. There is a balance on utilizing the knowledge of the pre-rescue managers and maintaining the independence of the corporate rescue practitioner.

4.2.3 Procedural Rights

Section 139 of the Insolvency Act deals with the rights that are accorded to holders of the company's securities. We have already seen in the previous chapters the right of shareholders in their capacity as affected persons to initiate rescue proceedings. However, the rights under Section 139 are not limited to shareholders only but to all holders of the Company's securities like shares, debentures, or other company instruments. Ordinarily shareholders are the residual claimants against the company in the event of liquidation. As such their rights are subordinate to those of creditors. Holders of the company's securities

¹⁰⁵ Section 137 (2) of the Companies Act, 2008

are however guaranteed certain procedural rights similar to those of creditors or employees with some variations especially on voting rights. They, like creditors, are entitled to receive notice of each court proceeding, decision, meeting or other relevant event concerning the corporate rescue proceedings¹⁰⁶. They can also participate in any court proceedings arising from the rescue proceedings. They can participate formally in the corporate rescue proceedings as provided for by the Act but can only vote for or against or for the amendment of a rescue plan if the plan would alter the rights associated with the class of securities held by those voting. They can also propose the development of an alternative rescue plan in the event of a rescue plan being rejected.

4.5 Conclusion

The Insolvency Act of 2018 has retained the management displacement thrust of the judicial management regime. It also introduces elaborate rights afforded to each interested party in a rescue scenario. This certainly defines what each party is or is not entitled to and brings that clarity that lacked under judicial management. It is also noteworthy that the rights referred to here are mainly procedural rights and not substantive rights which remain governed by other branches of the law like contract, delict, labour and company law. The rights encourage consultation and participation of affected persons in the whole rescue proceedings. Some changes may be welcome especially regarding the costs incurred by creditors in discharging the business of creditors' committees. It is suggested that since these creditors will be acting on behalf of other creditors, the costs they incur in that regard should be treated as costs of rescue and should be borne by the company.

CHAPTER 5

¹⁰⁶ Section 139 (a) of the Act

THE POWERS, DUTIES AND ROLE OF THE CORPORATE RESCUE PRACTITIONER

5.0 INTRODUCTION

It has been said that the success of any insolvency system largely depends upon those who administer it¹⁰⁷. The corporate rescue practitioner plays a pivotal role in managing the business in place of the board and is charged with the crafting of an appropriate corporate rescue plan that should turn around the fortunes of the financially distressed company. It needs no emphasis that with all the powers and duties the practitioner is accorded by statute, he should be a person of honesty, integrity and considerable business skill and professionalism. In this chapter we will look at the qualifications, regulation, powers and duties, removal from office of corporate rescue practitioners as provided for in Sub-Part B of Part XXIII of the Insolvency Act, 2018 and the Estate Administrators Act [Chapter 27:20]. We will compare the legal position with that in South Africa and England because the United States Chapter 11 procedures are not modelled along management displacement but “debtor-in-possession” design of corporate rescue law.

5.1 APPOINTMENT AND QUALIFICATIONS OF THE PRACTITIONER

a) Appointment of the Practitioner

Section 121 (1) (d) of the Act introduces what is termed a “corporate rescue practitioner” who is essentially an insolvency practitioner as defined by the Estate Administrators Act [Chapter 27:20]. The person is appointed to manage the affairs of a company under rescue. A corporate rescue practitioner is appointed in a number of ways stated in the Insolvency Act, 2018. First, he may be appointed by a board

¹⁰⁷ The Cork Report, (n. 4 above para. 732)

resolution five days after the company has adopted a resolution commencing rescue¹⁰⁸. Second, the practitioner may be appointed by the court following a court application objecting to the board resolution commencing rescue. Such practitioner must be recommended or approved by the majority of independent holders of voting interests¹⁰⁹. Third, the practitioner may be appointed by the court upon application to commence rescue proceedings by an affected party. The appointment is on the recommendation of the applicant(s) subject to approval at a creditor's meeting¹¹⁰. The last way the practitioner is appointed is in terms of Section 132 of the Insolvency Act where this follows removal or vacation of office by the practitioner in terms thereof. The company or affected person who initially appointed or nominated the departing practitioner will be required to appoint a replacement.

b) Qualification of the Practitioner

The corporate rescue practitioner appointed should meet the criteria set in terms of Section 131 of the Insolvency Act. A corporate rescue practitioner must not be disqualified for appointment as a liquidator in terms of Section 74 of the Act. We will not enumerate the various factors that disqualifies one for appointment as a liquidator but it is important to note that these touch mainly on integrity and independence of the person to be appointed. A corporate rescue practitioner must be registered in terms of the Estate Administrators Act as an insolvency practitioner¹¹¹. The practitioner must not have a relationship with the company which would a reasonable and informed person to conclude that the integrity, impartiality or objectivity of that person is compromised by that relationship¹¹². He should not be disqualified from acting as a director in terms of the Companies Act [Chapter 24:03]. The person should not be an associate of any person named above so as to maintain

¹⁰⁸ Section 122 (3) of the Insolvency Act

¹⁰⁹ See Section 126 (6) of the Insolvency Act

¹¹⁰ See Section 124 (5) of the Insolvency Act

¹¹¹ See section 25A on that Act

¹¹² See Section 131 (1) (d) of the Insolvency Act.

the integrity, impartiality and objectivity of the person so appointed. This is so because the practitioner will be taking over the role normally played by the directors of the company. He must also provide security in an amount and on terms and conditions set by the Master of the High Court to secure the interests of the company and affected person.

It is important to note that that issues of integrity, impartiality and objectivity rank very high in the qualification of a practitioner. The reason as set out in the previous chapter is simple. The practitioner is granted vast powers in running the affairs of the company as we shall see later on. The exercise of those powers cannot be carried out properly by a person who lacks in the stated virtues. Registration in terms of the Estate Administrators Act requires further investigation. This Act was amended in 2018 to separate mere estate administrators from insolvency practitioners. It is from the later pool that corporate rescue practitioners are drawn. Their qualification is now very rigorous. They should now be either Legal Practitioners or Public Accountants or Auditors or Chartered Secretaries¹¹³. They can also be drawn from other profession that the Council for Estate and Insolvency Practitioners may designate. Applicants must also have completed 2 500 hours of pupillage under a registered insolvency practitioner for a period of two to three years. They should also pass an examination on Insolvency Law set by Council¹¹⁴. The Estate Administrators Act has now created a highly regulated profession with a Council overseeing matters of registration, regulation and discipline of practitioners. An elaborate Code of Ethics for practitioner is provided for in the Act with a lot of emphasis on integrity, impartiality, professionalism and ethics for practitioners¹¹⁵. The concept of having a regulated body for insolvency practitioners who are qualified and under ministerial

¹¹³ Section 25D (1) of the Act

¹¹⁴ Section 25D (2) of the Act

¹¹⁵ Second Schedule of the Act

control arose in England after the recommendation of the Cork Report¹¹⁶. These recommendations were adopted in the English Insolvency Act, 1986¹¹⁷.

5.2 REGULATION OF PRACTITIONERS

The regulation of corporate rescue practitioners or insolvency practitioners is not directly covered by the Insolvency Act. This is left to the Estate Administrators Act which we have considered above. As briefly noted above, insolvency practitioners are regulated by the Council of Estate Administrators and Insolvency Practitioners appointed by the Minister of Justice¹¹⁸. The Council is mandated to register and regulate the conduct of practitioners complete with disciplinary powers over members of this new profession. Practitioners are required to maintain audited trust accounts and their trading licences should be renewed annually¹¹⁹. As indicated above, a fairly comprehensive code of ethics is provided for to further regulate the conduct of practitioners. Regulation is key in order to maintain the confidence and respect of all key stakeholders in practitioners. Accountability is undeniably an important factor especially where so much power and responsibilities are reposed in the practitioner by the Insolvency Act as we shall see later in this chapter. However, it should be noted that almost all practitioners (drawn from legal practitioners, chartered accountants and chartered secretaries) are already regulated by their own professional bodies under the relevant statutes and by-laws such as the Law Society of Zimbabwe. This kind of “double regulation”, in our view should not be a problem but may actually further instil discipline and ethical conduct in practitioners.

¹¹⁶ Cork Report Chapter 15

¹¹⁷ See Part XIII of the Act

¹¹⁸ Part II of the Act

¹¹⁹ Section 29A of the Act

5.3 REMOVAL FROM OFFICE OF A PRACTITIONER

Corporate rescue practitioners are expected to act professionally and with the skill expected of them. They must act impartially and must have the confidence and respect of affected persons. Once a corporate rescue practitioner fails in that respect, he obviously may be removed from office. A corporate rescue practitioner may be removed from office in any of the ways stated in Section 132 of the Insolvency Act, 2018. Like in the South African Companies Act, 2008¹²⁰, a practitioner may be removed from office by the court in any of the listed ways. The two Acts in that respect have almost identical provisions. The removal may be after a voluntary rescue board resolution has been challenged on the suitability of the practitioner. The court may also, upon request by an affected person or on its own motion, remove a practitioner from office for any of the six reasons listed in Section 132 (2). These include incompetence or failure to perform his duties, failure to exercise proper degree of care in the performance of his duties, engaging in illegal acts or conduct, conflict of interest or lack of independence, incapacitation and the practitioner ceasing to be qualified in terms of Section 131 of the Act. It should be expected that evidence must be laid before the court to prove that the practitioner should be removed from office. These reasons for removal broadly touch on the expertise, competency and integrity of the practitioner which are important in a regime that gives so much powers and responsibilities to a practitioner.

A practitioner may only be removed by the Master of the High Court for the same reasons and manner as a liquidator¹²¹. It may be argued that removal by the court may provide some protection to the practitioner especially where an affected person intends to just harass a practitioner who may otherwise be not guilty of any misconduct or breach of the law. However, the law in this regard tends to remove

¹²⁰ Section 139 of the Act

¹²¹ In terms of Section 79 of the Act

that reliance on court procedures which are time consuming and often costly on the person intending to have the practitioner removed. A cheaper way that is free from the intricacies and expenses of superior court litigation will be welcome. Time might also be of essence in certain circumstances and resorting to litigation may actually take time while the probably unfit practitioner is presiding over the management of the company. As such in terms of Section 79 of the Insolvency Act, the Master may remove from office a practitioner if the practitioner is not qualified or his appointment was unlawful. He may further remove a practitioner if the majority of creditors in number and value who have proved their claims have requested the Master in writing to remove the practitioner or have at a creditors' meeting voted to remove the practitioner, provided that proper notice would have been given prior to the meeting that such a resolution would be tabled for a vote. The Master may also accept a resignation by a practitioner or may remove him because he has been absent from Zimbabwe for more than sixty days without the permission of the Master or is in breach of conditions the Master gave for such absence from the country. The Master may in term of Section 79 (2) remove the practitioner who fails to perform satisfactorily any duty imposed by him (the Master) or by the law or has failed to comply with a lawful demand from the Master. The later scenario may be problematic because the Master may arbitrarily exercise his powers to the detriment of practitioners. Aggrieved practitioners may however naturally seek review of their removal in terms of the law.

5.4 POWERS AND DUTIES OF PRACTITIONERS

We have noted above and in the previous chapter that our law follows the management displacement model of corporate rescue and this has been the model under judicial management. Section 133 of the Insolvency Act provide for the general powers of the corporate rescue practitioner. He assumes **“full management control of the company in substitution of its board and pre-existing management which is**

dissolved in terms of the provisions of Section 130 (2)." This power differs materially with the South African equivalent in Section 140 (1) of the Companies Act, 2008 in that in South Africa, the board and pre-existing management are not dissolved but simply exist under the control of the practitioner. The Zimbabwean position seems desirable because the practitioner is given discretion by Section 133 (1) to delegate any of his power of function to a person who was a member of the board or pre-existing management of the company. So instead of retaining wholesome the pre-existing management and board who were in charge when the company failed, the practitioner may only assign roles or duties to those whom he selects should there be need. The practitioner may also appoint a new person to the management of the company either to fill a vacancy or not¹²². Perhaps the major function of the practitioner which makes or breaks the rehabilitation effort is the development of a rescue plan for consideration by affected persons and the implementation of the approved rescue plan¹²³. His skill and expertise are required in this respect because the stronger the plan, the better the chances the company has for survival. We will have a more detailed look at the role of the practitioner regarding the rescue plan in the next chapter.

The practitioner also has the duty to inform all regulatory bodies having authority over the activities of the company of the fact that the company has been placed under rescue and of his appointment¹²⁴. The power of the practitioner to appoint a manager or advisor are limited in circumstances where it would lead to suspicions of a compromise on the integrity, impartiality or objectivity of that person due to his relationship with the company¹²⁵. The practitioner needs leave of the court to do so. This is a sound safeguard against improper appointments. It should be expected that this should be a rare occurrence since a practitioner would be best advised to avoid

¹²² Section 133 (1) (c) of the Act

¹²³ Section 133 (1) (d) of the Act

¹²⁴ Section 133 (2) of the Act

¹²⁵ Section 133 (3) of the Act

controversial appointments unless it is absolutely necessary to appoint someone whose appointment may be queried. During corporate rescue, a practitioner is an officer of the court and is required to report to the court in terms of the rules of the court or in terms of the court order¹²⁶. He has the responsibilities, duties and liabilities of a director of the company¹²⁷. This has far reaching consequences and requires a practitioner to act with due care and loyalty as required of a director. We will not get into detail about these duties as enumerated by Section 193 and Sections 54 and 55 of the new Companies Act. These cover the new concept of the business judgement rule and duty of loyalty. The Act also absolves a practitioner from liability for any act or omission for anything done in good faith in the performance of his duties as a practitioner. However, there is a limit to this since he may be liable for any act or omission amounting to gross negligence¹²⁸.

The management displacement model of the new corporate rescue regime has its own pitfalls as we have seen in the previous chapter. Once the pre-existing management and the board of the company are dissolved by operation of law, the practitioner may find it difficult to access information regarding the company or to work his way towards a viable rescue plan. The law had to provide a cure for that predicament. In terms of section 135 of the Insolvency Act, the directors are required, as soon as practically possible after commencement of rescue proceedings, to deliver to the practitioner any books and records in their possession¹²⁹. If the records or books are not in the possession of the director but he knows the whereabouts of such information, then such director is obliged to disclose such whereabouts to the practitioner. The directors are given five days from the commencement of corporate rescue to provide a comprehensive statement to the practitioner containing at a minimum information pertaining to material transactions by the company or

¹²⁶ Section 133 (4) (a) of the Act

¹²⁷ Section 133 (4) (b) of the Act

¹²⁸ Section 133 (4) of the Act

¹²⁹ Section 135 (1) of the Act

involving the assets of the company covering a period of twelve month prior to rescue, information relating to legal or quasi legal proceedings involving the company, assets and liabilities of the company and its income and disbursements within the immediate preceding twelve months. The statement should also include the numbers of employees and any collective agreements with them and information on the debtors and creditors of the company¹³⁰. Such information has to be produced as required by law and this co-operation has to be distinguished from the appointments which the practitioner may make or the delegation of duties and powers he may make as regarding pre-existing management and directors as discussed above. Whether a director has been appointed or assigned any duties by the practitioner, he still has an obligation to co-operate with the practitioner.

5.5 INVESTIGATING THE AFFAIRS OF THE COMPANY

This is a function of the practitioner which perhaps deserves separate attention. As soon as practically possible after his appointment, the practitioner must investigate the company's affairs, business, property, and financial situation and then formulate an opinion as to whether there is any reasonable prospect of rescuing the company¹³¹. A judicial manager has the similar powers in terms of Section 303 (c) (vi) of the old Companies Act especially on formulating an opinion on the prospects of saving the company. That opinion should be viewed as independent and coming from a professional. It should then be used to inform the court and affected persons in formulating the decision whether or not to continue with the rescue efforts. If at any stage during rescue, a practitioner formulates an opinion that there are no prospects of rescuing the company, the practitioner must inform the court, the company and all affected persons and apply to court for an order terminating the rescue

¹³⁰ Section 135 (3) of the Act

¹³¹ Section 134 (1) of the Act

proceedings and placing the company into liquidation¹³². If the practitioner's opinion is that there are no more reasonable grounds to believe that the company is no longer distressed, the practitioner must inform the court, the company and affected persons of this opinion. If the proceedings were commenced by a court order, the practitioner has to apply to court to terminate the proceedings or otherwise file a notice terminating the proceedings.

If during the investigations the practitioner discovers evidence that there are impeachable dispositions, he has to take the necessary steps to rectify the matter in terms of the relevant provisions of the Insolvency Act¹³³. These dispositions will include dispositions without value in terms of Section 24, voidable preferences in terms of Section 26 and collusive dealing in terms of Section 27 of the Insolvency Act. If there is evidence of reckless trading or insolvent trading, fraud or other illegalities, the practitioner must either report the matter for prosecution by a relevant authority for further investigation or apply the procedures in section 117 and 118 of the Act to any misappropriated assets of the company¹³⁴.

5.6 REMUNERATION OF THE PRACTITIONER

The remuneration due to a practitioner is critical because if not controlled by statute, may be subject to abuse. It also may have a bearing on the independence of a practitioner. Section 136 of the Insolvency Act deals with this subject. A practitioner's remuneration is ordinarily provided for in a tariff which is amended from time to

¹³² Section 134 (2) (a) of the Act

¹³³ Section 134 (2) (c) of the Act

¹³⁴ Section 134 (2) (c) (ii) of the Act

time by the Minister of Justice¹³⁵. The fees are charged on a sliding scale with a minimum fee. Additional fees may be agreed with the company on the basis of a contingency relating to the adoption of the rescue plan or inclusion of a particular matter within the plan or the attainment of a certain result or combination of results relating to the rescue¹³⁶. It would appear that the additional remuneration is meant as an incentive to the practitioner. Safeguards are that the additional contingency fee should be approved by the majority of creditors by value at a properly convened meeting and by the majority of shareholders present and voting at such a meeting¹³⁷. A further safeguard is that any creditor or shareholder who voted against this contingency fee may apply to court within ten business days after the adoption of the proposal for an order setting aside the agreement on the basis that the agreement is not just and equitable or that the remuneration is unreasonable having regard to the financial circumstances of the company¹³⁸. The Master may, for good cause, increase or decrease the practitioner's remuneration in particular to compensate him for time spent in criminal prosecutions or investigations into the company's affairs or to disallow fees due to any delay in the discharge by the practitioner or because of improper performance of his duties¹³⁹. It would appear that this provision is a "carrot and stick" provision meant to encourage diligence and commitment by the practitioner while discouraging lack thereof. Unpaid practitioner remuneration ranks in priority above all secured and unsecured creditors¹⁴⁰ a further hedge around the remuneration of the practitioner.

5.7 CONCLUSION

¹³⁵ Section 136 (1) as read with the Second Schedule item 1 of the Act

¹³⁶ Section 136 (2) of the Act

¹³⁷ Section 136 (3) of the Act

¹³⁸ Section 136 (4) of the Act

¹³⁹ Section 136 (6) of the Act

¹⁴⁰ Section 136 (5) of the Act

The Insolvency Act has reaffirmed the management displacement paradigm of our corporate rescue law. Rigorous qualification requirements meant to maintain expertise and integrity of the profession stick out conspicuously. An elaborate regulatory regime, with a fairly detailed code of ethics for practitioners is provided for in the Administrators of Estates Act and this helps keep practitioners maintain their independence, impartiality and fairness in whatever they do. In return, the law gives the practitioner extensive powers regarding the management of the company and the preparation of an appropriate rescue plan. The practitioner is rewarded with a fair compensation for his efforts in the form of a regulated remuneration regime.

CHAPTER 6

THE CORPORATE RESCUE PLAN

6.0 INTRODUCTION

The success or failure of a rescue process depends much on the quality and suitability of the proposed plan. Our law gives exclusive rights to the practitioner to craft an appropriate rescue plan after consulting only named stakeholders. Unlike under judicial management, the new rescue law requires a plan partly containing some prescribed contents to be crafted and be voted for within set timeframes. Creditors and holders of the company securities where the proposed rescue plan alters the rights of such securities, are the ones who have the exclusive rights to vote for or against a rescue plan, although employees are given the right to contribute with ideas towards the development of the plan and during the debate leading to the vote. We will in this chapter focus on the rescue plan (which is also called the reconstruction or reorganization plan). we will consider how it must be developed, considered, adopted and its effect. Comparisons will be made wherever necessary with positions in other jurisdictions. As we shall see below, rescue (or restructuring/reconstruction) plans are a common feature in South Africa, United States and England, although there are differences on how they are developed and eventually adopted.

6.1 DEVELOPMENT OF THE CORPORATE RESCUE PLAN

Section 142 of the Insolvency Act, 2018 prescribes in some detail, how the rescue plan has to be developed, by whom and the minimum content of the plan. The practitioner has the exclusive right to develop the rescue plan but has to consult

creditors, employees and shareholders (affected persons) as well as the management of the company¹⁴¹. As we have seen in earlier chapters, our law maintains the management displacement design of corporate rescue law. As such the practitioner is expected to play the role of developing the rescue plan. we have also considered the fact that the practitioner would have, by the time he develops a rescue plan, carried out an investigation into the company's affairs in terms of Section 134 of the Act. Consequently, the practitioner gets down to work armed with the requisite information from the investigation and from other sources. the Insolvency Act follows the trend in South Africa and England where the law favours management displacement as well. The pre-commencement management, as we have seen in previous chapters, is deemed dissolved and management of the company firmly vests in the practitioner. Although this management has all the information regarding the company, we have concluded in previous chapters that they cannot be trusted to come up with a plan to rehabilitate the company when the company went into distress under their watch. In England, Snowden J reasoned in *Davey v Money*¹⁴², that directors and shareholders may have "an overly unrealistic and over-optimistic view of the company's business and prospects of rescue" and hence they cannot be trusted with the duty to develop a rescue plan.

The other option would have been to perhaps adopt the American model that gives the company exclusivity in formulating the reorganization plan for some 120 days after which any creditor(s) may then choose to develop the plan. the reasoning has been touched on in previous chapters when we dealt with the aspect of management displacement versus the American debtor-in possession model. It is argued that indeed the pre-existing management was in charge when the

¹⁴¹ Section 142 (1) of the Act

¹⁴² [2019] EWHC 997 (Ch). See also *Van Zwieten*, (n. 3 above p. 556), where the author supports the view of the court and generally the position that it is the practitioner who is best positioned to come up with a reconstruction plan than the pre-commencement management

company went into distress but they are best placed to know the business of the company hence the idea that they should develop a restructuring plan. It is also further argued that if management is not given the exclusive right to develop a restructuring plan, they will keep the company out of rescue until it was too late to save the business¹⁴³. These could be sound justification for the debtor in possession paradigm but as we have seen in this work so far, the management displacement model works very well and has been the model under judicial management. Further and in any event, the Insolvency Act, just like the Chapter 6 business rescue model in South Africa (and to some extent administration procedure in England), the practitioner is required to consult not only creditors but other affected persons and the management of the company. As such, even if the management is not exclusively responsible for crafting a rescue plan, they are given an opportunity to contribute towards its development. Consultation with managers and affected persons also help in another respect. Creditors (and in some cases, shareholders and other security holders) are the ones that will vote to approve the rescue plan. chances of these voters rejecting the rescue plan are reduced if they are consulted in advance and their views are taken into consideration.

The Insolvency Act, 2018 also prescribes what the rescue plan should contain. In terms of Section 142 (2) of the Act, a rescue plan “must contain all the information reasonably required to facilitate affected persons in deciding whether or not to accept or reject the plan”. It sounds quite an indeterminate statement of what exactly is required but the long and short of it is that the rescue plan must contain essential information on the affairs of the company and its chances of successfully shaking off financial distress so as to assist the affected persons to decide whether

¹⁴³ See generally McCormack, (n. 14 above p. 252) where the author refers to the American legislative records (i.e reports of the Senate and House of Representatives (HR Rep No. 95-595 at 231 – 232). In those reports the American Congress extensively relied on this reasoning in giving management exclusivity in formulating the restructuring plan.

to accept or reject the plan. The information prescribed must be included as a requirement of law. A structure of the plan is prescribed and the first of the three parts into which the plan must be divided must contain background information on various matters including, information on all creditors and assets of the company, the probable dividend each creditor would receive if the company were to be liquidated, a complete list of the holders of the company's issued securities, information about any agreement on the practitioner's remuneration and a statement whether the rescue plan includes a proposal made informally by a creditor¹⁴⁴. As already indicated above, this information is part of what affected persons need in order to make a decision as whether to proceed with the rescue or to go for liquidation.

The second segment of the plan must contain proposals which must include as a minimum, the nature and duration of the moratorium for which the rescue plan makes provision, the extent to which the company will be released from paying its debts and any proposal regarding conversion of debt into equity in the company or some other company, how existing agreements will be treated, the assets available for distribution to creditors and the order of preference, the benefits in terms of returns in case of rescue as opposed to liquidation and the effect that the rescue plan will have on holders of any class of the company's issued securities¹⁴⁵. The information that must be included is meant to be sufficient enough to guide affected person in decision making. What is prescribed is not a closed list of proposals. It is simply a minimum and a practitioner is expected to include any relevant proposals as he may deem appropriate. The last part of the plan must contain assumptions and conditions and these must include conditions which must be fulfilled in order for the plan to take come into operation or for it to fully implemented. It must also contain information on the effect, if any, that

¹⁴⁴ Section 142 (2) (a) of the Act

¹⁴⁵ Section 142 (2) (b) of the Act

the rescue plan contemplates on the number of employees and their terms and conditions of employment. It should have a projected balance sheet of the company and a projected income and expenditure statement for the ensuing three years based on the assumption that the proposed corporate rescue plan is adopted. That part should also state the circumstances in which the rescue plan will end. The rescue plan must conclude with a certificate by the practitioner stating that the information provided is accurate, complete and up to date and that estimates were done in good faith¹⁴⁶. There is no prescribed penalty for any false information being provided in the Insolvency Act but one would expect the code of ethics to cover such an eventuality. The plan should be published within 45 business days after the appointment of the practitioner or such a longer period and may be allowed by the High Court or by the majority of holders of the creditors' voting interests¹⁴⁷. It appears from the above that the Act seems to over-prescribe what has to be included but in our view, this is necessary so as to measure the appropriateness of a plan. There is always a yardstick against which a rescue plan can be measured. Prescribing such information also helps practitioners and affected person especially in a situation where the plan is not subject to court confirmation as is the case in the United States.

6.2 CONSIDERATION OF THE CORPORATE RESCUE PLAN

A key feature of the new corporate rescue regime has been to avoid complex and time consuming court procedures where possible. The rescue plan does not need the approval of the court as is the case in the United States of America. In terms of Section 143 of the Insolvency Act, the practitioner (not the Master) must convene and preside over a meeting 10 business after the publication of the plan. this meeting must be attended by creditors and any other holders of voting interest.

¹⁴⁶ Section 142 (4) of the Act

¹⁴⁷ Section 142 (5) of the Act

All affected person may attend this meeting a proper notice must be given together with a summary of the rights of affected persons to participate and vote at the meeting. It is at this meeting that the practitioner must introduce the rescue plan and must also indicate that he still is of the opinion that there are reasonable chances of rescuing the company¹⁴⁸. Employees, who will not vote unless they are creditors, must be given a chance to address the meeting through their representatives. Discussion on the plan seems to be open to all affected persons although only creditors (and security holders in circumstances where the plan affect their rights) vote for or against the plan. A preliminary vote on the plan may be carried out and in cases where the plan has no effect on rights of security holders of any class, that preliminary vote is final¹⁴⁹. Approval of the rescue plan requires support of holders of 75% of the creditors' voting interest that voted and the number must also include at least 50% of independent creditors' voting interest. In other words, a rescue plan may fail if it received the 75% vote but within that vote, the 50% threshold was not reached in respect of independent creditors. Approval by creditors requires a simple majority support of security holders whose rights will be affected by the rescue plan for it to become binding¹⁵⁰.

A rejected plan does not necessarily mean that the rescue process is terminated immediately. In terms of Section 145 of the Act, either the practitioner or any affected person may call for a vote to approve submission of a revised plan. The whole determination and voting process is also repeated in respect of the revised plan. It is important to note that the practitioner is still the person required to submit a revised rescue plan and not any affected person. An affected person may apply to court to have the result set aside on the basis that it was "inappropriate". The word "inappropriate" is not defined by the Act and leaves this provision

¹⁴⁸ Section 144 (1) of the Act

¹⁴⁹ See Section 144 (1) (e) as read with Section 144 (2) (b) of the Act

¹⁵⁰ Section 144 (c) of the Act

vague. The situation is made worse when in terms of Section 145 (8) of the Insolvency Act, the court may set aside the vote on a rescue plan if it is satisfied that “it is reasonable and just to do so” having regard to the interests represented by those who voted against the rescue plan, the provisions made in the plan in respect of those persons, and the fair and reasonable estimate of the return to that person if the company were to be liquidated. It appears that the court is called upon to intervene as a safeguard against abuse of the voting interests by those participating in the vote. The court may deal with issues touching on the independence of those voting against the plan and whether or not they did not vote to sabotage an otherwise good rescue plan.

In South Africa the courts have held that the word “inappropriate” refers to or means an act which unduly undermines the achievement of the purpose of the Act. Any vote which unduly undermines the achievement of the rescue of a financially distressed company will be “inappropriate”. A vote that resulted in the rejection of the proposed business rescue plan, which rejection was to the detriment of the respondent and other affected creditors was deemed “inappropriate”. It was that the vote had the ability to frustrate the efficient rescue and recovery of the financially distressed respondent. The test to be applied is an objective test and not a subjective test.¹⁵¹ It remains to be seen how the courts will interpret this section.

Two issues in the determination of the rescue plan deserve further consideration and these are the voting process and the involvement of the courts. The Insolvency Act, 2018 borrows heavily from the South African business rescue procedures in

¹⁵¹ See the majority judgement in the case of *FirstRand Bank Ltd v KJ Foods CC (In Business Rescue)* [2015] ZASCA 50. The court also held that once a vote has been set aside by the court pursuant to such a challenge, the rescue plan cannot be subjected to another vote because there may end up being endless applications regarding the same challenged vote. The rescue plan is adopted by operation of law. This is a very difficult position to accept but we believe the courts knew the inadequacies of the law in dealing with such a matter.

Chapter 6 of the South African Companies Act in respect of these two issues. Voting for or against the rescue plan seems to be done in both jurisdictions by the whole body of creditors in one meeting without differentiating them by their size or status, that is to say without differentiating between secured and concurrent creditors, or those owed a few hundred dollars and those owed millions or between preferred creditors and other creditors. The American Chapter 11 bankruptcy procedures recognize the differing interests that creditors represent and are therefore grouped into classes for purposes of considering the restructuring plan. they recognize that “different creditors may have different views on the value of the reorganised company and the risks presented by extended repayments schedules. The ability to mould creditors into separate classes is a powerful one”¹⁵². It should be noted also that creditors who may have alternative third-party sureties or guarantees may have different incentives in respect of rescuing the debtor. Further, creditors who have trade debts owed by the ailing debtor company may want the company to survive so that they can continue trading with it yet those with no trade links with the company like delictual claimants may have no real incentive to support the survival of the company. Secured creditors who may have sued and recovered immediately against the company may not necessarily want to wait for rescue while their money is locked up in the security offered by the company. All these factors tend to support the idea that it would be better to group creditors into classes for purposes of determining the rescue plan. Perhaps the reason why the courts can be called to set aside a vote was to create a safeguard against voting trends that may result as a consequence of voting together as one body of creditors. In any event the court intervention in terms of the Insolvency Act as described above only

¹⁵² B A Markell “*Clueless on Classification: Toward Removing Artificial Limits on Chapter 11 Claim Classification*” (1994) 11 Bankruptcy Development Journal 1 at 16 (quoted by McCormack, (n. 14 above p. 257-258)

applies when a plan has been rejected and not when it is accepted and a creditor is not happy with it.

The “cram down” process in the United States of America works better if creditors are classified according to interests. (“Cram down” is the process by which other classes of creditors are made to accept the result of the majority in approving a restructuring plan. It is a term normally used in the United States Chapter 11 Bankruptcy voting procedures but can be used to refer to the voting thresholds discussed above in the Insolvency Act, 2018). It is easier to follow voting trends if creditors vote in pre-determined classes that when all voters vote as a single block. In the United States the courts are involved for the final approval of the restructuring plan. This seems like an undesirable requirement especially when courts are not really equipped with the technical knowledge of investment bankers or business management experts. It is therefore desirable that the creditors and shareholders determine the direction in which the company should take subject to some safeguards when the rescue plan has been rejected.¹⁵³ A court free rescue process is desirable in that it works well with the model that gives tight schedules in executing and completing the rescue process. The American Chapter 11 is criticized for involving the courts too much that it is made complex and time consuming.

6.3 EFFECT OF THE APPROVAL OF THE RESCUE PLAN

¹⁵³ The requirement that the court endorses a rescue plan in America is an entrenched part of the Bankruptcy Code yet a certain American Judge Bruce McCullough lamented that *“you must have seen some of those plans. Some of them are as big as the New York telephone book. How is a judge who is foreclosed from participating in the reorganization ever going to read that plan and find anything wrong with it?...I don’t care how smart you are, you wind up talking to yourself, challenging your own assumption and driving yourself crazy. The judge isn’t going to be allowed to call and examine a bunch of expert witnesses. That’s not a typical judge’s role. It may be a judge’s responsibility, but as a practical matter they can’t do it.”* See McCormack, (n.14 above p. 256).

An adopted rescue plan is binding on the company, and all the creditors of the company and holders of the company's securities whether or not that such person was present at the meeting on which the approval was made or whether or not the person voted against the adoption of the plan. Creditors are further bound whether or not they had already proven their claims¹⁵⁴. We have already looked at this "cram down" concept above. That is the whole idea of corporate rescue that unanimity of votes is not necessary but a special majority of those present and voting is enough. Satisfying any condition on which the rescue plan is contingent as well as the implementation of the plan is left to the company under the direction of the practitioner¹⁵⁵. This is the critical part of the whole process because this makes or breaks the rescue process. Its success is measured at this stage and the results that come out at last. The practitioner may also where necessary in terms of a rescue plan, determine the consideration for and issue the company's securities and this power is exercised notwithstanding any other provision of the Companies Act to the contrary. He may also in terms of the approved rescue plan amend the company's memorandum of incorporation to authorise, and determine the preferences, rights, limitations and other terms of any securities that are otherwise not authorised and this power may be exercised notwithstanding any provisions of the Companies Act to the contrary¹⁵⁶. These wide powers are necessary since the management displacement model of the law means that the board of directors which would normally do this is dissolved by operation of law as we have seen in previous chapters. Shareholders' pre-emptive rights in respect of a fresh issue of shares of a company under rescue may not be exercised unless otherwise allowed by the rescue plan. Once the rescue plan is substantially implemented, the corporate rescue practitioner must file a notice of substantial

¹⁵⁴ Section 144 (4) of the Act.

¹⁵⁵ Section 144 (5) of the Act

¹⁵⁶ Section 144 (6) of the Act

implementation of the rescue plan thus enabling the company to move out of rescue.

Once a rescue plan has been implemented in accordance with its terms, creditors' rights to recover debts are limited in that all those creditors who agreed to the discharge of the whole or part of their debts lose the right to enforce the relevant debt or part thereof¹⁵⁷. Any debt that was owed by the company immediately before the commencement of the rescue procedures may no longer be enforced except to the extent provided for by the rescue plan. these are significant consequences which may encourage financially distressed companies to seek protection of the corporate rescue procedures.

6.4 CONCLUSION

The development of the corporate rescue plan is in keeping with the management displacement model of the new rescue regime. The exclusive right granted to the practitioner to develop the rescue plan is qualified by the mandatory requirement to consult managers and affected persons. This helps in that adoption chances of the plan by creditors and shareholders are enhanced if they are consulted in advance. The approval of the rescue plan is left to the creditors and in some cases shareholders. This process is made as court free as possible because approval of such plans should not be a judicial function. A court free process also ensures that precious time is save to the benefit of all the affected persons. The legal effect of rescue on debts owed by the company should act as an incentive to companies to voluntarily commence rescue proceedings at an early stage.

¹⁵⁷ Section 146 (1) of the Act

CHAPTER 7

CONCLUSIONS AND RECOMMENDATIONS

7.0 INTRODUCTION

We shall draw conclusions on what we have discussed in this research and make some recommendations on how to further develop and clarify the law on corporate rescue. An attempt will be made to make general evaluations of how we see the new rescue regime as well as making general comparisons with judicial management which the rescue regime seeks to replace. Where necessary, we may suggest some further developments on the law. This law is still new and the superior courts have not yet pronounced themselves on key matters and we shall, where necessary, suggest what we believe to be the legal position.

7.1 RESTATING THE PURPOSE OF THE RESEARCH

The stated purpose of this study was to unpack the new law on corporate rescue as provided in the Insolvency Act, 2018. In doing this we set out to first deal with the normative theories of corporate rescue in general and see how it informs our law. It was also our goal to investigate whether the new corporate rescue regime is an upgrade from judicial management, a regime which corporate is meant to replace. The research also sought to examine whether the new law as it promotes corporate rehabilitation. Lastly we sought to see whether there could be any room for development of the law.

7.2 SUMMARY OF ARGUMENTS OF THE STUDY

To achieve what we set out as the purpose of the study, we started off in Chapter 1 by introducing the research topic and went on to state the research objectives, the research questions, the theoretical framework of the study and the research methodology. We then went into the next chapters to look at then law and

critically reviewing it. We did this by tracing the origins of the concept of corporate rescue and its development. We then compared our law with the laws from jurisdictions with which we share a common legal history. Superior court judgements in South Africa may help shape the way to be adopted by the local courts as far as this law is concerned because our corporate rescue law is very similar to the law on business rescue in South Africa.

7.3 SUMMARY OF CONCLUSIONS OF THE STUDY

- ❖ We have seen that the corporate rescue regime is almost a direct transplant of the South African Chapter 6 business rescue procedures in the Companies Act, 2008. Such a direct transplant has some notable advantages and disadvantages as well. Our local practitioners, courts and lawyers benefit immensely from the experiences in South Africa. Starting such a system from scratch may prove very difficult especially in such technical matters. Judicial precedents from South Africa may also help shape our jurisprudence. However, our countries may still differ in many respects especially in economic development. It may be difficult to implement even a robust rescue regime in a country where inflation is very high. Creditors tend to lose in such a situation when their debts are eroded in value due to the moratorium on enforcement procedures.

- ❖ It would appear that the primary motivation for the rescue culture is what has influenced insolvency regimes the world over, that is to say there must be a viable option to liquidation. Insolvency law should not be all about processing and punishing failures but should be more inclined towards rehabilitation. Rehabilitation ensures that interests on all concerned parties are catered for if a company is saved from liquidation or if liquidation is deferred to a later date. These words by a South African High Court sums up the design and purpose of the rescue regime in South Africa where we borrowed much of our law on

corporate rescue; “**Business rescue**” as the definition proclaims or explains, is a regime which is largely self-administered by the company, under independent supervision within the constraints set out in Chapter 6 of the Act, and subject to court intervention at any time on application by any of its stakeholders. This is an important difference or aspect that differentiate business rescue from its counterpart in the old Companies Act, 1973, namely, judicial management. Business rescue is geared at saving significant costs, thus among others enabling financially distressed small (and big) companies to opt for it as a viable alternative to “*last resort*” liquidation”¹⁵⁸. The above statement sums up the new paradigm of the new corporate rescue regime in the Insolvency Act, 2018 which as we have seen in this work is modelled along the South African Chapter 6 business rescue regime in the Companies Act of 2008. The new corporate rescue regime seeks to ensure that commercial matters like corporate rescue be as court free as possible, the court only intervening when necessary as an indispensable safeguard. Courts should not be expected to make commercial decisions for those is business. These decisions should, as much as possible be left to the business community. This way, much time is saved and the procedures are costs effective.

- ❖ We noted that the timing for commencing rescue is critical. The new regime requires that rescue measures be commenced well in advance of an insolvency. At least six months in advance when at the commencement stage the company is still solvent and able to pay its debts. This theoretically allows the company a huge chance to survive as remedial action is taken before the situation is too late.

¹⁵⁸ Kgomo J in the South African case of *Merchant West Working Capital Solutions (Pty) LTD v Advanced Technologies and Engineering Company (Pty) Ltd and Another* [2013] ZAGPJHC 109 at p109

- ❖ We have examined the corporate rescue regime and noted that its design is meant to be easy to understand and implement for companies that are faced with financial distress. The procedures for commencing and managing the process are fairly straightforward and companies do not necessarily need to resort to intricate superior court procedures in order to get into rescue.
- ❖ Further the mostly court free design saves time and is cost effective. This is quite unlike the procedures under judicial management. These new procedures are meant to be swift and cheap as it allows companies to simply file a resolution to commence rescue which becomes effective immediately upon filing of the resolution. This theoretically enhances the chances of rehabilitating a financially distressed company.
- ❖ Judicial management had inherent weaknesses and could be abused by companies as a way to evade immediate payment of debts. The lack of strict and short deadlines within which the whole judicial management procedure was to be concluded, meant that some companies would be under judicial managements for very long periods of time. This came obviously at a cost to creditors who may have wanted to recover their debt immediately before high inflation started eating into their debts. On the other hand, the new regime has strict deadlines which must be adhered to failing which the process may be rendered void in some cases. This helps deal with the possible abuse of the rescue process. Only those genuinely seeking rescue will be accommodated.
- ❖ We also explored the legal effect of corporate rescue especially the automatic moratorium on enforcement procedures and property rights as well as the super-priority of post commencement finance. These again are provisions which clearly depart from the unclear and ineffective moratorium under judicial management. The new position theoretically improves the chances of the company being rescued as its protection is immediate and clearly set out.

This automatic moratorium, though it compromises the right of creditors to enforce their rights, it comes coupled with the tight schedules that have to be adhered to. In fact, the process up to the adoption of a rescue plan may be done in ninety days.

- ❖ The creation of a new profession of insolvency practitioners who are regulated in and under the supervision of a Council improves the chances of the company being rescued as only qualified practitioners with proper professional training may act as corporate rescue practitioners. The development of a Code of Ethics also helps in the regulation and discipline of practitioners.
- ❖ The rights of all stakeholders are now clearly spelt in the Act and improves that cooperation of the se stakeholders in the development and consideration of the corporate rescue plan. Safeguards have been provided wherever possible to ensure that the procedure is not abused and that practitioners do not exercise their powers arbitrarily.
- ❖ On the negative side however, one major concern is the way the Insolvency Act, 2018 was drafted especially in the part dealing with corporate rescue. We have noted some areas where, perhaps due to the fact that the legislature sought to rely as far as was possible, on the provisions of the South African Companies Act, they ended up making some errors. The South African Supreme Court of Appeal lamented the drafting of Chapter 6 of the Companies Act, 2008 (from where our legislature took a wholesale transplant into the new corporate rescue regime), as follows;

“I do not believe it is unfair to comment that many of the provisions of the Act relating to business rescue, and s 153 in particular, were shoddily drafted and have given rise to considerable uncertainty.”¹⁵⁹

- ❖ we have also noted some areas where there may be need to clarify certain matters by way of amendments. For example, the Act should have clarified what is meant by certain critical terms used therein. Some of these are *“financial reasons”* in Section 124 (4) (a) (iii), *“legal proceedings”* in section 126 and *“title interest”* in Section 127.
- ❖ There are also some grey areas which need clarification. Some of these are, what penalty, if any, is imposed on directors who do place a company into rescue despite filing a written notice to affected persons in terms of section 122 (7). There is no detail on **“committee employees’ representatives”** in terms of Section 137 (3) (c) of the Insolvency Act. The South African Companies Act from where these provisions were borrowed has details on how these committees are constituted, their role and duties. There is also no clarity on what happens when an affected person approaches the court in terms of Section 145 (1) and (2), as read with Section 145 (8) of the Insolvency Act. The South African Supreme of Appeal has held that the rescue plan would be adopted by operation of law once the court rules in favour of setting aside a rejection on the rescue plan.

¹⁵⁹ Leach JA in *African Banking Corporation of Botswana Limited v Kariba Furniture Manufacturers (Pty) Limited and Others* **2015 (5) SA 192** (SCA) para 43. The judge also went on to quote an author, A Loubser, *The Business Rescue Proceedings in the Companies Act of 2008: Concerns and Questions (Part 2)* : **2010 TSAR 689** at 700 – 701) who said the following about the standard of drafting of Chapter 6 of the Companies Act; *“It is therefore regrettable that the drafters of the provisions regulating the new rescue proceedings did not exercise more care in constructing the new procedure to avoid introducing principles and provisions that are completely foreign and even in conflict with our established law. ... The many unclear, confusing and sometimes alarming provisions regulating the business rescue proceedings in the Companies Act of 2008 will certainly not assist in making the procedure more acceptable or successful.”*

7.4 RECOMMENDATIONS

The new corporate rescue regime has not yet been implemented for a long time since the law was passed in 2018 and litigants still had a choice between the pursuing judicial management in terms of the old Companies Act or commencing rescue proceedings in terms of the new Insolvency Act. We will state what we believe are some useful recommendations.

- ❖ Since the regime is till newly introduced and the law is generally good and a notable upgrade from judicial managements, it is important to give business a chance to try to implement the new law and for courts to deal with any issues that may arise. A comprehensive review may then be done after some time of applying the law. That way, we will avoid piece meal amendments.
- ❖ Immediate amendments may however be required in those stand out areas noted in our conclusions where urgent clarification is needed especially after drawing lessons from the South African experiences when implementing similar provisions.
- ❖ Some editing may also be done to clarify certain issues. Notable areas that may need some editing are Sections 140 (1) of the Insolvency Act to clarify that the meeting is convened by the master 15 business days after the appointment of the rescue practitioner. There is also need to edit Section 144 (3) (c) (ii) B to reflect that an opposed rescue plan is dealt with in terms of Section 145 instead of Section 144.
- ❖ By and large, we would recommend that the business community be allowed to implement the new rescue regime and lessons are learnt in the process. Recommendation will be made after a trial run of sorts. Insolvency law is

predominantly procedural law. As such there is need to test the procedures in practice for some time before changes could be recommended.

7.5 OVERALL CONCLUSION

Corporate rescue is a welcome development in our law as we believe it is an upgrade to the judicial management regime which was old and required an overhaul. This new regime follows developments not only globally but in countries that share a common legal history with us. The procedures and design are at least theoretically meant to enhance chances of rehabilitating ailing companies. There is need to first test the law before wholesale changes are made. Much will be clearer when the Superior Courts start considering the provisions of the Insolvency Act. 2018.

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