SUSCEPTIBILITY OF CREDITORS RIGHTS IN TERMS OF SECTION 131 (1) OF SOUTH AFRICA'S COMPANIES ACT 71 OF 2008

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Abstract

The automatic statutory moratorium on legal proceedings and enforcement action that endures from commencement to termination of the business rescue process is central to the legislative scheme. This is important for a country which envisages rescuing ailing companies as a priority. The moratorium has, nevertheless, a considerable impact to the affected persons. The company creditors are a leading group among the affected persons which likely to be more affected by this stay on enforcement action. The crux of this study is to discover to what extent this statutory moratorium is of detriment to the creditors rights. The overall analysis of the business rescue proceedings provisions and more specifically Section 131 (1) of the Companies legislation: in conjunction with the available case law that have interpreted the aspect of moratorium were important tools in exploring the magnitude of the vulnerability of creditors rights. The study has learned that the stay on action covers a wider scope for the purpose of achieving the goals necessitated for the mechanism to be established. The statute has, however, not given a full stay against legal proceedings and enforcement rights of creditors. Further, during the execution of the mechanism by the business rescue practitioner, creditors are not barred to approach the court whenever they are of the view that their interests are subject to prejudice. It is, therefore, safe to state that the legislation and court have simultaneously taken cognisance of the rights of creditors and broad policy objectives of business rescue.

Keyword: *Company legislation, Creditors Rights, Business Rescue Proceedings, Financial Distress*

1.0 Introduction

1.1 Moratorium in Business Rescue Proceedings

The preamble to South Africa's Companies Act 71 of 2008 (hereinafter 2008 Act) acknowledges one of its objectives as being to provide for the efficient rescue of financially distressed companies.[1] For this to be implemented an important aspect of the statutory corporate restructuring regime, that is a temporary moratorium was established. This is provided as follows under Section 133 (1) of the 2008 Act:

> (1) During business 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 any forum, except-
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> (a) with the written consent of the practitioner;

[1] S 7 (k) of 71 of 2008

(b) with the leave of the court and accordance with any terms the court considers suitable;

(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 business rescue proceedings began;

(d) criminal proceedings against the company or any of its directors or officers;

(e) proceedings concerning any property or right over which the company exercises the power of a trustee; or

(f) proceedings by a regulatory authority in the execution of its duties after written notification to the business rescue practitioner.

The legislation provides this moratorium automatically[2] and for a specified duration of time.[3] Generally, the moratorium in corporate reorganisation intends to give the company a breathing space in which creditors cannot institute or enforce legal proceedings for the payment of claims.[4] Further, the moratorium intends to allow viable companies to get back on

[2] This is necessary in order to prevent the restructuring proceeding from being frustrated by some creditors immediately after its initiation, see Keay, A. and Walton, P., *Insolvency Law Corporate and Personal*, 2nd Edition, London: Jordans, (2008), 107.

[3] See *AG Petzetakis International Holdings Limited v Petzetakis Africa (Pty) Limited and Others (Marley Pipe Systems (Pty) Limited)* 2012 (5) SA 515 (GSJ) para 29 the High Court stated the reason for the moratorium to be temporary is because business rescue proceedings should be conducted in an expeditious manner. This assertion was, however, differently established by Olsen J. in *JVJ Logistics (Pty) Ltd v Standard Bank of South Africa Ltd and Others* (7076/2015) [2016] ZAKZDHC 24; para 34, where he stated that with regard to the activities associated with the proceedings, the moratorium is temporary due to that fact that it has a finite life span.

[4] See INSOL International, Statement of Principles for a Global Approach to Multi-Creditor Workouts (2000) which discusses the extent of co-operation that is expected of a creditor toward a distressed company during the moratorium. In *Chetty v Hart* (20323/2014) [2015] ZASCA 112; para 39 the Supreme Court of Appeal stated the said that, "Section 133(1) was enacted to protect a company under business rescue against claims from creditors. Its object is to prevent the practitioner being inundated with legal proceedings without sufficient time within which to consider whether or not the company should resist them and to prevent the company that is financially distressed from being dragged through litigation while it tries to recover from its financial woes. Its effect is to stay legal proceedings except in those circumstances mentioned in s 133(1)(a) to (e). The creditor may initiate or continue the proceedings in terms of s 133(1)(a) with the written consent of the practitioner."

their feet financially.[5] The moratorium also assists in ensuring the equal treatment of the company's creditors, secured and unsecured.[6]

The thrust of this study is to unveil the rights of creditors during the moratorium period in business rescue proceedings. This is achieved by looking at the extent Section 131 (1) of the Act protects the ailing company during the restructuring processes; together with the analysis of the available case law which has put the right of creditors to legal proceedings and enforcement action into question.

1.2 The Scope of Moratorium under Business Rescue Proceedings

The Act is drafted in a manner that retains the confidence of the company's creditors throughout the business rescue proceedings.[7] The creditors are entitled to seek the consent of the rescue practitioner or the leave of the court to institute or enforce legal proceedings against the company, although the bar against such proceedings in this regard is not absolute[8] and the criteria on which consent or leave will be granted or refused are not made explicit in the Act. In *Merchant West Working Capital Solutions (Pty) Ltd v Advanced Technologies (Pty) Ltd*[9] and *Redpath Mining South Africa (Pty) Ltd v Marsden NO and Others*[10] it was held that leave to litigate would be granted only in special circumstances.[11]

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[5] The first South African legislation incorporating corporate restructuring proceedings was The Companies Act 46 of 1926 which introduced Judicial Management mechanism without providing for stay of action on legal proceeding against the company. However the economic threat during that time necessitated for the amendments which introduced moratorium on companies in judicial management proceedings under Companies Act 11 of 1932. See also, Claessens, S. and Klapper, L.F., 'Bankruptcy around the World: Explanations of its Relative Use,' (2002), World Bank Policy Research Working Paper 2865, 6 and 8, available at **www.univie.ac.at/bwl/ieu/lehre/ss06/..../debtor_in_possession.pdf** , accessed on 25. July. 2014. In this study among other things the authors discussed the need of stay in legal proceedings in corporate turnaround.

[6] See Pretorius, M. and Rosslyn-Smith, W., 'Expectations of a Business Rescue Plan: International Directives for Chapter 6 Implementation,' (18)2, Southern Africa Business Review, (2014), 114.

[7] As it is under Ss 130, 132, 134, 136, 141, 144, 145, 146, 147, 148, 149, 151, 152, 154 to mention but few of the 71 of 2008. It was further stated by Dal Pon, P.G. and Gig, L., 'A Principled Justification for Business Rescue laws: A Comparative Perspective (Part I),' (1996), 5 (1), IIRV 67 that the statutory provisions in respect of the moratorium require careful and expert drafting, so that creditors will regard the general moratorium as being, overall, in their interests or at the least not to their significant and long-term disadvantage.

[8] S 133 (1) (a) for the consent and 1 (b) 71 of 2008 for the application. Further, according to *Chetty v Hart* (20323/2014) [2015] ZASCA 112; para 45 the availability of these remedies and the way the moratorium provision is tailored guarantees the creditors that there is no absolute bar on legal action against the company. However, Haselman, R., and others, `How the Law Affects Lending,' Columbia Law and Economic, (2006) Working Paper No.285, (2006), 12 stated that there is a need of having to weigh the considerations pro and contra before allowing such proceedings.

[9] [2013] ZAGPJHC 109; at para 67 Kgomo, J. stated that-"… A court being asked for leave to proceed against a company under business rescue, thus during a moratorium, must receive a well-motivated application for that so that it could apply its mind to the facts and the law if necessary and then be in a position to make a ruling in accordance with any terms it may consider suitable in the peculiar circumstance."

[10][2013] ZAGPJHC 148 para 71 and following his judgment in *Merchant West Working Capital Solutions (Pty) Ltd Case* (2013), Kgomo, J. held that the failure of the applicant to show exceptional circumstances meant the the application had to be rejected..

[11] See also, *Concorde Plastics (Pty) Ltd v NUMSA and Others* 1997 (11) BCLR 1624 (LAC) at 1644F-1645A it was held that very powerful considerations are required.

The courts are thus not constrained by the Act in this regard and will take account of the policy objectives of business rescue.[12] Lifting the moratorium in respect of a creditor's claim can jeopardise the entire attempt at business rescue and prejudice other creditors.[13]

The approach of Kgomo, J. in *Redpath Mining South Africa (Pty) Ltd Case* (2013) and *Merchant West Working Capital Solutions (Pty) Ltd* (2013) was held to be unconvincing in *Moodley v On Digital Media (Pty) Ltd and Others*[14] where the High Court construed the moratorium as not restricting an affected person from approaching the court on matters regarding the business rescue practitioner or the company in relation to the business rescue plan. The court observed that issues that arise during the operation of the business rescue are not subject to the moratorium. Similarly, in *Resource Washing (Pty) Ltd v Zululand Coal Reclaimers Proprietary Limited and Others* the court disagreed with the views advanced in

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[12] In *Natal Joint Municipal Pension Fund v v Endumeni Municipality* 2012 (4) SA 593 (SCA) para 18, it was held that a court must take account of context, as well as language. Delport, P., et al *Henochsberg on the Companies Act 71 of 2008*, Service Issue 9 Vol 1 at 478(6) comments that the intention of the moratorium is to cast the net as wide as possible in order to include any conceivable type of action against the company.

[13] *Re Absa Bank Ltd v Caine N.O* [2014] ZAFSHC 46 para 48 where the rescue proceeding had already being in existence for the past two and half years. Under this prevailing circumstance the court ruled that it will not be fair to prevent creditors from exercising their contractual rights during the stay of business rescue proceeding should not exceed to an extent that it detriments the rights of creditors. This is a kind of circumstance that the court thought it just and equitable to grant leave for the party to enforce its right irrespective of the existing stay of enforcement

Further, in an English decision *Re Atlantic Computer Systems plc* [1992] Ch 505 at 542-544 where an applicant applied to be granted a permission to exercise its property right of repossessing the computers which were held by a company in administration under both hire purchase and long lease agreements. The Court of Appeal made some points that a court could consider when it is called upon to grant a leave to lift a moratorium:

1. In an event a party is applying for a leave so that it exercises its property right, such as repossession, the court will look whether that act will frustrate the mechanism, if not it will grant the leave.
2. The court should take a balance the interests of the party claiming to repossess against the interests of the other creditors.
3. In the balancing exercise undertaken by the court due weight should be given to the owners of the property. This is done for the purpose of preventing the owner of the property to indirectly finance the proceeding for the benefit of unsecured creditors.
4. Also the court would grant a leave for legal proceeding if the refusal will significant harm to the applicant.
5. In a circumstance that it has rejected a leave, the court should order the practitioner to act in a manner that ensures fairness.

[14] (20456/2014) [2014] ZAGPJHC 137; paras 10 the court stated that: "The language of s 133, when read in context with the other relevant provisions in Chapter 6 and having regard to its purpose, *does not include within its ambit proceedings relating to the development, adoption or implementation of a business rescue plan.* It is the business rescue practitioner who must develop a business rescue plan and implement it if adopted and the company, under the direction of the practitioner, must take all necessary steps to attempt to satisfy any conditions on which the business rescue is contingent and implement the plan as adopted. *Legal proceedings, such as the present case, which seek that an adopted business rescue plan be executed and implemented strictly according to its terms and in accordance with the applicable provisions of the Companies Act, are legal proceedings against the business rescue practitioner and the company in business rescue in connection with the business rescue plan. They are not legal proceedings against the company or property belonging to the company or lawfully in its possession within the meaning of s 133(1)"* [Emphasis supplied].

In in para 11 the court concluded that "Section 133, therefore, finds no application in legal proceedings against a company in business rescue and its business rescue practitioner in connection with the business rescue plan, including its interpretation and execution towards implementation…"

Redpath Mining South Africa (Pty) Ltd and pointed out that nowhere does the Act state that exceptional circumstances must be present for the court to grant leave in this regard.[15]

2.0 Contractual rights

It is established that not all legal disputes arising during business rescue proceedings are subject to moratorium. In *Kythera Court v Le Rendez-Vous Café CC and Another*[16] the urgent application for a leave order to be granted in terms of *Section 133 (1) (b)* of the Act was found by the court to not be necessary. This order was sought by applicant for the purpose of lodging an action of evicting the tenant on the ground that the lease agreement has been cancelled, hence expired. This case illuminates the fact that as long as the tenant has failed to fulfil its obligations, the lease agreement can be lawfully cancelled by the landlord despite the fact that the company is in business rescue. The lessor is, therefore, not barred by the moratorium to bring legal proceedings to evict the tenant. However, the court stated that this can only take place in a situation where a business rescue practitioner has not suspended the obligation of the tenant set forth in the lease agreement.[17]

In *Murray NO v Firstrand Bank Ltd t/a Westbank*[18] the Supreme Court of Appeal held the following with regard to contractual rights from an agreement made before the initiation of the business rescue proceedings–

> "The liquidators' construction that, in terms of Section 133 (1), the cancellation of an agreement constitutes 'enforcement action' which requires the consent of the practitioner or the court, would also fundamentally change our law of contract. As explained earlier, our law of contract provides for a unilateral cancellation in the case of a breach of contract. The way I see it, *the legislature intended to allow the company in distress the necessary breathing space by placing a moratorium on legal proceedings and enforcement action in any forum, but not to interfere with the contractual rights and obligations of the parties to an agreement.* Such an intention would, in any event, be contrary to the tenet of our law that *the legislature does not intend to alter the existing law more than is necessary, particularly if it takes away existing rights"* [Emphasis supplied].

Fourie AJA held that a party to a contract can, in the exercise of common law rights, unilaterally cancel the contract without permission from the business rescue practitioner or the leave of the court, as the right of cancellation is not affected by the moratorium and does not amount to legal proceedings as envisaged in the Act.[19] Thus, a party to a contract can exercise

[15] (10862/14) [2015] ZAKZPHC 21, para 10-13.
[16] 2016 (6) SA (GJ)
[17] S 136 (2) (a) 71 of 2008 which grants the business rescue practitioner to suspend contracts which a company in business rescue is a party.
[18] (20104/2014) [2015] ZASCA 39, para 40.
[19] The court interpreted the phrase "no legal proceedings, including enforcement action" to mean enforcement action as a result of legal proceedings. Thus, cancellation of a contract is a unilateral act by a party that does not involve any legal proceedings.

this right notwithstanding the objectives of business rescue proceedings. In understanding the importance of appreciating the other existing laws of the land, yet taking into consideration the intention of the business rescue proceedings, it will be challenging for its objectives to be achieved; if a party to the contract can exercise its right regardless of the objectives of the commencement of the proceedings.[20] It is unexpected that the Act was not drafted in a manner that makes the cancellation of a contract subject to the moratorium.

2.1 Quasi-judicial Proceedings

The stay on legal proceedings against the company during the business rescue proceeding encompasses quasi-judicial proceedings. A noteworthy aspect of South Africa's business rescue regime is the importance accorded to the company's employees.[21]
In *Fabrizio Burda v Integcomm (Pty) Ltd*[22] it was held that proceedings in the Commission for Conciliation, Mediation and Arbitration constitute legal proceedings as envisaged in the business rescue legislation provision, and are thus subject to the moratorium. In *National Union of Metal Workers of South Africa obo Members v Motheo Steel Engineering*[23] which concerned an urgent application in relation to the applicability of *Section 133 (1) (a)* of the Act, the Labour Court held that labour law does not bar employees from exercising their right to institute legal proceedings, except where the Constitution provides otherwise.[24]

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[20] However in *Murray NO and Another Case* [2015] para 35 the court stated that by invoking Section 136 (2) (a) and 154 (2) of the Act the company in business rescue is enough protected from action a party to the contract can exercise. This study with all due respect, holds different view with regards to these two provisions stated by the court as safeguards against unilateral cancellation of contracts. Section 136 (2) (a) give power to a rescue practitioner to suspend entirely, partially or conditionally, any obligation of the company that arises under an agreement to which the company was a party at the commencement of the business rescue proceedings. This power does not preclude a creditor from unilaterally cancelling of a contract hence sabotaging the whole purpose of the mechanism when the party to contract has cancelled an obligation after having received the notice that the company is entering the rescue proceedings under Section 129 (3) (a). At this time the rescue practitioner has not yet been appointed. This again refers to the need for the statutory requirement necessitating the other party to continue with the contractual obligations, until the rescue practitioner finds it otherwise. In contrast to that, the business rescue proceeding can only materialise if the company negotiates with its creditors prior to entering the formal rescue procedure. Regarding Section 154 (2) if comprehensively read it shows that it will come into operation after the approval of the rescue plan. Hence, this provision will not be applicable when a creditor is cancelling the contract at the time between the initiation of mechanism and approval of the rescue plan. The decision of the Supreme Court of Appeal to interpret cancellation of contract no to form a part of enforcement action due to the fact that it does not involve any forum for it be executed endangers the purpose of the legislation and mechanism at large. Despite of making reference to the *Natal Joint Municipal Pension Fund Case 2012 (4) SA 593 (SCA*) para 18, in interpreting Section 133 of the legislation, and considering the issue of language used in the provision as a point of departure but taking into account the context used and purpose of the legislation and mechanism it is difficult to comprehend basis for the court in reaching to that decision. Further, the sensible meaning and business-like practice of the provision could have deemed proper if its regard the cancellation of a contract as part of enforcement action hence barred.

[21] Joubert, E.P and Loubser, A., 'Executive Directors n Business Rescue: Employees or Something Else?,'
(2016) De Jure, 95. the authors acknowledge the importance accorded to employees throughout the business rescue proceedings. Lesser emphasis in this regard is accorded in countries such as UK, Germany, USA and Canada.

[22] (Unreported case No. JS539/2012, 29.11.2013).

[23] (J271/2014) [2014] ZALCJHB 31, para 1.

[24] The court referred to Section 210 of the Labour Relation Act, 66 of 1995.

These two conflicting decisions regarding the enforcement rights of workers during business rescue proceedings were to some extent resolved in *Sondamase v Ellerine Holdings Limited (in business rescue)*[25] where the Labour Court recognised that the stay of legal proceedings against a company in rescue proceedings includes arbitration proceedings in labour tribunals. The Supreme Court of Appeal finally resolved the issue in *Chetty v Hart.*[26] In this case, the court had regard to the purpose of the moratorium in business rescue and related it to alternative dispute resolutions in labour matters, and ruled that a wide scope must be accorded to the moratorium. As to the meaning of "forum" in *Section 133* of the Act, the court affirmed the interpretation adopted in *Murray NO* [27] which held that a *forum* is a court or tribunal. It is safe to state that the decisions taken in these two cases took a practical approach to the purpose of moratorium in business rescue proceedings.[28]

3.0 Duration of the Moratorium

The moratorium protects the debtor company from the commencement of business rescue through to its termination. This was established in a obiter dictum of *Kariba Furniture Manufacturers Case* (2013),[29] where the respondents submitted that the moratorium comes to an end after the adoption of the rescue plan; the High Court rejected this notion by first affirming the fact that the statute has only provided for the definition of the term "business rescue" and left "business rescue proceedings" definition unattended for that purpose. However, in the definition of the term business rescue under Section 128 (1) (b) among other things it provides that the proceeding is still in action even during the implementation of the adopted plan. Also Section 132 (2) (c) (ii) provides for circumstances that rescue proceedings come to an end when the plan is approved and rescue practitioner has filed for the notice of substantial implementation in terms of Section 152 (8).[30] Therefore, considering the fact that the company is protected by the moratorium throughout the proceedings, then the adoption of the rescue plan does not waive the stay.

It has been suggested that in such moratoriums, the period of moratorium must be neither too long nor too short. In *Gormley v West City Precinct Properties (Pty) Ltd*, *Anglo*

[25] (Unreported case No. C669/2014, 22.01.2016)

[26] (20323/2014) [2015] ZASCA 112; at para 35 it was held that "…the purpose of the provision, which is to give breathing space to the practitioner to get the company`s financial affairs in order, *also requires it to be construed widely because arbitrations, like court proceedings also involve diversion of resources-both time and money-that may hinder the effectiveness of the business rescue proceedings*. To construe it narrowly, as the court a quo did, and as the respondent contends we should, would be at odds with its language, defeat its purpose and lead to insensible and impractical consequences" [Emphasis supplied].

[27] (20323/2014) [2015] ZASCA 112. At para 19 the court ruled that if the drafters had intended to restrict legal proceedings to court proceedings, they would simply have used the word 'court' instead of 'forum' in S 133 of 71 of 2008.

[28] In *JVJ Logistics (Pty) Ltd v Standard Bank of South Africa Ltd and Others* (7076/2015) [2016] ZAKZDHC 24; at para 36 it was held that it would be impossible to conduct business rescue proceedings in the absence of a moratorium.

[29] para 5.

[30] This was also emphasised in *JVJ Logistics (Pty) Ltd Case* [2016] para 34.

Irish Bank Corporation Ltd v West City Precinct Properties (Pty) Ltd[31] the High Court stated that:

> "…The Act envisages a short term approach to the financial position of the company. This is so for self-evident reasons. There must be a measure of certainty in the commercial world. *Creditors cannot be left in the state of flux for an indefinite period*…It must either be unlikely that the debts can be repaid within the ensuing 6 months. In the case the company is presently insolvent and cannot pay its debts unless a moratorium of 3-5 years is granted. The fact of this matter does not bring West City`s financial situation within the definition of financially distressed" [Emphasis supplied].

For the purpose of fulfilment of business rescue proceeding's objectives a balance needs to be struck in this regard between the interests of the company and the rights of its creditors.[32]

4.0 The operation of moratorium in other jurisdictions

In some jurisdictions, a moratorium is not automatic as it is in South Africa, there are others with no moratorium at all and others have to be imposed by court order. India is an interesting example of a jurisdiction which had no moratorium for some creditors[33] in its corporate reorganisation mechanism, following the enactment of the Reconstruction of Financial Assets and Enforcement of Security Interest Act 2002 and before Companies Act 2013 came to force.[34] In Chapter 11 proceedings in the USA, the debtor company, once it has

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[31] (19075/11) [2012] ZAWCHC 33, para 11, See also Eloff AJ in S*outhern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 (Pty) Ltd* [2011] ZAWCHC 442 para 24. Further, see Finch, V., 'Re-invigorating Corporate Rescue', [2003], J.B.L., 538. In Kang, N. and Nitin, N., `The Evolution of Corporate Bankruptcy Law in India,' ICRA Bulletin Money and Finance, Oct 2003- March 2004, 49, the authors cite the example of India where the corporate rehabilitation procedure can take up to fifteen years to be finalised. Under this situation the unfair prejudicial of creditors' interests is inevitable.

[32] Pretorius, M., Business Rescue Status Quo Report Final Report, Business Enterprises at University of Pretoria (Pty) Ltd (30 March 2015), 34 cites the following factors when determining whether the duration of a moratorium is reasonable:

(a) Industry effect (mining very long and retail industry short).
(b) Sources of PCF sought (international vs local funders require different times to complete due diligences etc.).
(c) Shareholder country of origin vs that of creditors relative to South Africa (influence *n travel, negotiation, exchange controls).
(d) Number of times creditors request revisions of the proposed plan.
(e) Legal proceedings initiated by affected parties during the process of the rescue. These can be of various natures.
(f) Nature of the cause of decline/distress
(g) External and environmental factors (ex. Businesses in the platinum belt are suffering due to the strike).

[33] Institutional creditors such as banks together with other financial institutions, the central government and any state government were not barred by moratorium.

[34] This was spearheaded by the fact that before 2002 India under its Sick Industrial Companies (Special Provisions) Act 1985, companies could abuse the moratorium at the expense of creditors by prolonging the restructuring procedure for years. See Zwieten, K., 'Corporate Rescue in India: The Influence of the Courts', Journal of Corporate Law Studies, (2015), 3. This is evidently in the decision of *Board Opinion v Hathising Mfg Co Ltd* [2004] 119 Comp Cas 25 (Gujarat) where a company was under the rehabilitation proceeding for 12

filed for the rehabilitation, is granted a ninety-day automatic stay of all proceedings. Same time limits also apply in South Africa's business rescue.[35] In the UK the moratorium in the Administration proceedings must be supported by the creditors and it has to be approved by the court.[36] An automatic right to a stay of execution is vulnerable to abuse.[37]

Providing for an automatic moratorium allows the companies to be at ease in the filing or applying for the restructuring processes, as they are aware that they will be protected from the creditors.[38] But this automatic right of stay on execution is subject to abuse by the companies against the creditor interests.[39] The requirement of the approval of either the creditors or court or both so that a company can be granted a moratorium allows the creditors to be supreme hence they are the ones who will determine the fate of the company.[40] This stops the company`s management from filing on time for the rehabilitation proceedings, in

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years. After the establishment of Reconstruction of Financial Assets and Enforcement of Security Interest Act 2002 creditors had the power to seize collateral after the debtor has defaulted paying the loan upon being given a sixty-day notice. The worst part of it is that the debtors only had a chance of appealing after the repossession of the securities by the creditor has taken place. This avenue put creditors, in this respect the secured ones, in a comfortable environment of realising their payment in a more expeditious manner possible. Under these circumstances the debtors are forced to pay the debts on time regardless of the financial situation they are in or else the collateralised assets will be taken away. As far as reconstruction of a company is concerned, this will fast track the liquidation of those distressed financially viable companies which mostly depend on those assets for their operations purposes that have now been taken away by the claimants. On the other hand the nonexistence of a moratorium, however, can be a motivational factor to force the debtors to respond quickly to financial distress occurring in their companies by sitting down with their creditors and negotiating before embarking on the rescue proceedings.

[35] S 132 (3) of 71 of 2008. If the proceedings have not terminated within three months, the business rescue practitioner has the right to apply to court for an extension.

[36] Sections 10 and 11 of the UK Insolvency Act 1986. These provisions provide for a moratorium during the application stage and after the order for administration mechanism has been granted by the court. In other countries such as Hungary they have changed the moratorium practice during the rehabilitation proceeding from the automatic to the one which should first be approved by the creditors. Also in Poland the stand still should first be affirmed by the secured creditors.

[37] Haselman, R., and others, `How the Law Affects Lending,' Columbia Law and Economic, (2006) Working Paper No.285, 1 also observed that the presence of automatic moratorium undermines creditors' right to enforce their security.

[38] The absence of an automatic stay is considered as an important feature when discovering jurisdictions that have a creditors` regime rehabilitation mechanism, see La Porte and others, ''Law and Finance'', JPE, (106)6, (1998), 1135 and 38. This empirical study which dealt on analysis of creditors' right in various countries, discovered nearly half of them do not have an automatic stay on assets. It was however realised that legal origin mattered in the presence of this stay, in common law countries 72 percent had no automatic stay where as in French-civil-law 26 percent has no automatic stay and Germany-civil-law 67 percent have no automatic stay. This implies that common law and Germany-civil-law has a greater creditor's protection while the weakest protection is found in French-civil-law countries.

[39] Haselman, R., and others, `How the Law Affects Lending,' Columbia Law and Economic, (2006) Working Paper No.285, 1 also observed that the presence of automatic moratorium undermines creditors' right to enforce their security.

[40] It is, however, believed that protecting the debtor from creditors' harassment during financial distress encourages a sense of entrepreneurship. For instance, Israel has to some extent stripped away the protection the creditors had, for the sake of encouraging innovation and a way forward for stabilising itself as a private market economy. This happened in 1995 when the country was transforming from socialist based to capitalist economy, See Erfat, R., 'The Transformation of the Israel Bankruptcy System as a Reflection of Social Changes,' 10 (1), Journal of Transnational Law and Policy, (2002), 39-68

the fear that creditors will scramble for their claims resulting in liquidation.[41] The absence of an automatic moratorium makes the interests of creditors a priority versus that of the company.

5.0 Conclusions

The act of putting a bar on legal proceeding, such as enforcement action by creditors, in relation to a property belonging to the company, or lawfully in its possession, is justifiable, considering the objectives of the business rescue proceedings, that are reviving ailing companies or repaying the creditors more than liquidation value. It is difficult to comprehend how could either of these objectives be achieved with the absence of tools for operation such as machinery, buildings and other resources which are subjected to collateral or raw-materials procured on hire are taken away by creditors who are enforcing their claiming rights.[42] Even though all the creditors, more specifically the secured creditors' immediate right of claim is denied under business rescue proceedings, one has to acknowledge the difficulty in achieving the purpose of the restructuring without a moratorium.[43] On the contrary, the availability of a moratorium will also protect the interests of the body of creditors as a whole. The presence of the moratorium bars most of the secured creditors who are assured of receiving their payment in full during the liquidation proceedings, but other creditors cannot enjoy this privilege if the company is subjected to that proceeding.[44]

The statutory moratorium is not absolute and all-encompassing, and this flexibility is intended to be a positive feature of the process. It allows creditors under certain conditions to enforce their rights. It is envisaged that this has a small chance of occurring, especially in a situation where the proceeding has focused on rehabilitating the corporate entity save for the situation where that creditors' enforcement will not be a distraction for the proceeding to achieve its purpose. It was mentioned in the research literature that the presence of an automatic stay against enforcement rights of creditors in a corporate rescue procedure qualifies as one of the attributes of a debtor regime. Thus, the creditors are not fully prevented from enforcing their rights during this period as long as they have been sanctioned by the business rescue practitioner or courts. The study finds it to be difficult for either of

[41] This will further lead to companies embarking on rescue proceedings when they are in an irreparable circumstance.

[42] The rights most commonly affected by the moratorium are security rights, rights of sale, other contractual rights, rights of foreclosure, reciprocal rights arising from performance by creditors, and rights to set-off, see Wood, P.R., *Law and Practice of International Finance: Principles of International Insolvency*, 2nd Edition, Sweet and Maxwell, (2007), 37

[43] The Companies Act 46 of 1926 introduced judicial management mechanism without providing for stay of action on legal proceeding against the company. However the economic threat during that time necessitated for the amendments which introduced moratorium on companies in judicial management proceedings under Companies Act 11 of 1932. See Chapter 2.11.2.

[44] So the other classes of creditors will be assisted by the stay in enforcement as it ensures that the company will be in a position to increase their dividends unlike if it was immediately wound up. Further, in corporate restructuring there is normally a deviation from absolute rule, whereby it benefits the shareholders and other concurrent creditors. See Pretorius, M. and Rosslyn-Smith, W., 'Expectations of a Business Rescue Plan: International Directives for Chapter 6 Implementation,' (18)2, Southern Africa Business Review, (2014), 114.

those two to grant such a decision unless the request will not have a negative effect on the proceedings.