



SALVIS GRATIA  SG TURNAROUND

Business Rescue Guide

Business rescue presents a lifeline for financially distressed companies in South Africa, offering a chance to navigate out of troubled waters and towards a path of recovery **Taking proactive steps can help safeguard your company's future** and potentially restore its financial health.

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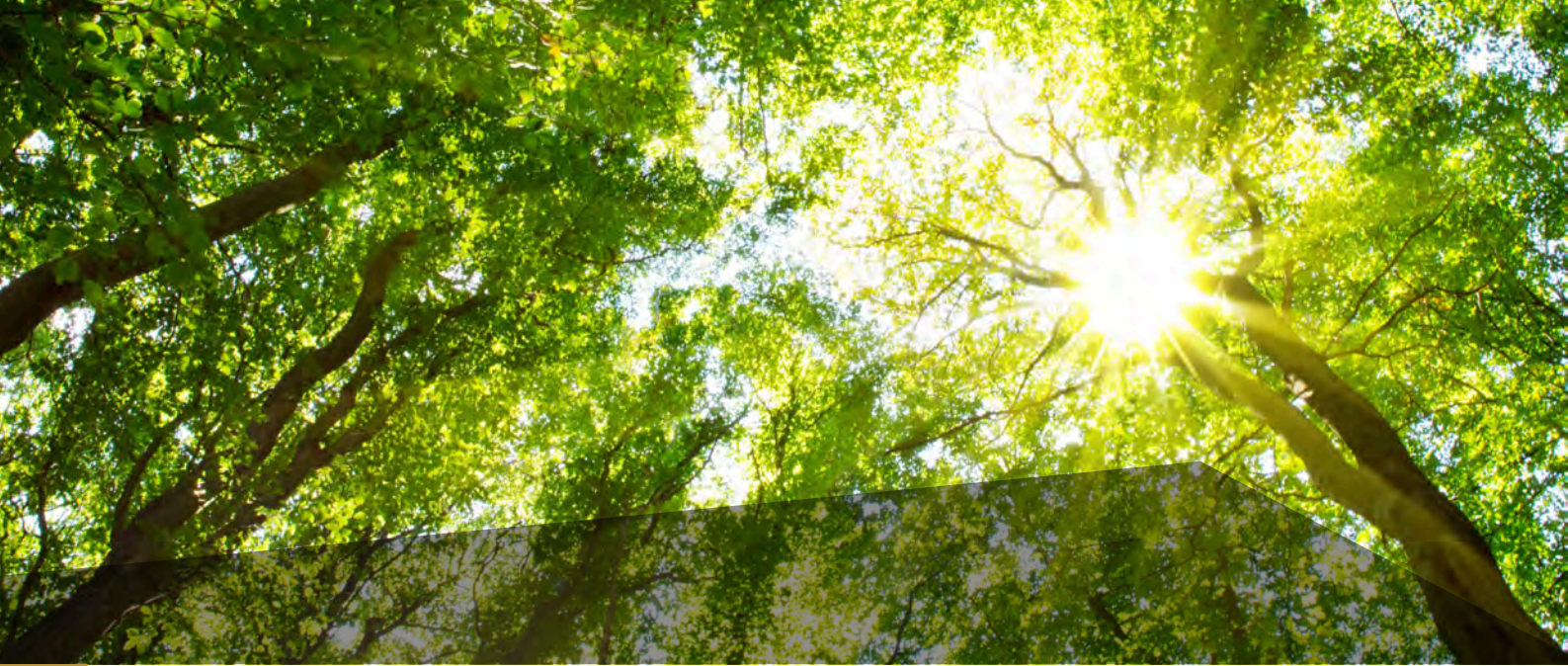


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What is Business Rescue?

Business rescue, as outlined in Chapter 6 of the Companies Act 71 of 2008, is a statutory mechanism designed to assist financially distressed companies in South Africa. The purpose is twofold:

- 1. To rehabilitate the company and allow it to continue trading as a solvent entity.**
- 2. If rehabilitation is not possible, to ensure that creditors receive a better return than they would through liquidation.**

The business rescue practitioner (BRP) takes over the management of the company, and a temporary moratorium on creditors' claims is imposed. This gives the company the opportunity to reorganize its affairs, stabilize operations, and implement a strategy for recovery or a structured winding down.

How to Enter Business Rescue

Voluntary Business Rescue:

- The board of directors can resolve that the company is financially distressed and voluntarily enter business rescue by filing a resolution with the Companies and Intellectual Property Commission (CIPC).
- The board must also appoint a business rescue practitioner (BRP) within five business days and inform all affected persons (creditors, employees, shareholders).
- Once the resolution is filed, the BRP takes control of the company's management and begins restructuring.

Court-Ordered Business Rescue:

- Any affected person (shareholders, creditors, employees) can apply to the court to place a company under business rescue.
- The court will grant this order if it is satisfied that the company is financially distressed and has a reasonable prospect of rescue. In cases where a company is already in liquidation proceedings, business rescue may be pursued as an alternative upon a application to the court.

Financial Distress and Test for Business Rescue

According to the Companies Act, a company is financially distressed if:

- It is unlikely to be able to pay its debts as they become due in the next six months (commercial insolvency), or
- It appears that the company will become insolvent in the next six months (balance sheet insolvency)

Reasonable Prospect of Rescue: For a company to enter business rescue, there must be a reasonable prospect of it being rescued. This means the BRP needs to demonstrate that through restructuring, the company can recover and continue to operate, or at least offer a better return to creditors than liquidation. The courts have determined that more than mere optimism is required; the plan must be feasible and backed by factual evidence.

The Role and Powers of the Business Rescue Practitioner

The **Business Rescue Practitioner (BRP)** is central to the business rescue process. Appointed by either the board or the court, the BRP takes full control of the company's affairs. The key responsibilities include:

- Taking over the management of the company, effectively replacing the board and existing management.
- Investigating the company's financial position and the causes of its financial distress.
- Developing a business rescue plan that outlines how the company's operations, debt, and assets will be restructured.

Powers of the BRP:

- The BRP has the authority to suspend or cancel contracts that were in place before business rescue commenced.
- The BRP can negotiate post-commencement financing (PCF) to keep the company afloat.
- The BRP has the right to call meetings with creditors and shareholders to discuss the rescue plan and its approval.

The Business Rescue Process

1 Filing for Business Rescue

1

The board of directors files a resolution with CIPC or an affected person applies to the court to commence business rescue.

2 Notification of Affected Persons

2

The company must notify all affected persons –creditors, employees, shareholders–within five business days of filing the resolution.

3 Moratorium on Legal Action

3

A statutory moratorium is imposed on legal proceedings and claims against the company. This prevents creditors from taking any enforcement action against the company.

4 Appointment of the BRP

4

A BRP must be appointed to manage the company. The BRP assumes control of the company and develops a business rescue plan.

5 Development of the Business Rescue Plan

5

Within 25 business days of the BRP's appointment, the BRP must draft a business rescue plan. This plan should include a comprehensive analysis of the company's financial situation and the proposed restructuring steps.

6 Approval of the Business Rescue Plan

6

A meeting with creditors is held to discuss and vote on the rescue plan. For the plan to be approved, it must be supported by 75% of creditors' voting interests, and 50% of the votes must come from independent creditors.

7 Implementation

7

Once approved, the business rescue plan becomes binding on the company, creditors, and shareholders. The BRP is responsible for overseeing its implementation.

8 Termination or Conversion

8

Business rescue terminates when the BRP files a notice of substantial implementation, or if it becomes apparent that the rescue plan cannot succeed. In such cases, the BRP may convert the process into liquidation by applying to the courts for liquidation.

The Moratorium: Protecting the Company During Rescue

The **moratorium** is a key feature of business rescue. From the moment the resolution is filed or the court grants an order, no legal action, can proceed against the company without the BRP's consent or a court order. This provides the company with protection from aggressive creditors while it reorganizes.

However, this moratorium does not apply to:

Criminal proceedings against the company or its directors.

Impact on Contracts During Business Rescue

One of the BRP's most significant powers is the ability to suspend or cancel **pre-existing contracts**. This provision in the Companies Act allows the BRP to renegotiate terms that are unfavorable to the company's survival, such as supplier agreements or leases.

Post-Commencement Finance (PCF)

The **Companies Act** recognizes the need for companies in business rescue to continue financing their operations. **Post-commencement finance (PCF)** allows the company to secure new funding during the rescue process, often to pay for essential supplies, salaries, or to fund the rescue plan.

PCF is given priority over unsecured claims from before the commencement of business rescue. Lenders who provide PCF rank higher in the order of repayment and are therefore incentivized to support companies under rescue.

Rights of Affected Persons

The Companies Act gives substantial rights to affected persons—creditors, employees, and shareholders:

- **Creditors:** Have the right to vote on the business rescue plan. Creditors also have the right to challenge the BRP's decisions or the terms of the plan in court if they believe their interests are unfairly prejudiced.
- **Employees:** Employees are considered affected persons and can participate in the business rescue process. They retain their employment unless specific changes are made to contracts in compliance with labor laws.
- **Shareholders:** While their control is limited, shareholders retain the right to be consulted, especially in matters affecting the restructuring/security of shares

Business Rescue vs. Liquidation: Key Differences

Business Rescue is focused on restructuring the company to return it to solvency, whereas liquidation is a process of winding down a company and distributing its assets to creditors. Business rescue prioritizes the continuation of the company, safeguarding jobs, and preserving the value of the company's operations.

Liquidation, on the other hand, involves selling off assets to pay creditors, often resulting in lower returns. Business rescue can result in a more favorable outcome for creditors, particularly where the company has ongoing operations that can generate revenue.

Conclusion: Is Business Rescue Right for Your Company?

If your company is experiencing financial distress but has a realistic chance of recovery, **business rescue** offers a structured path to recovery under the protection of the Companies Act. However, early action is key. If left too late, the company may no longer be salvageable, and liquidation may become the only option.

Indicators that business rescue may be appropriate include:

- A decline in revenue affecting debt repayments.
- Legal threats from creditors.
- Insolvency or expected insolvency within the next six months

Situations when a company might consider entering business rescue

- **Financial Distress:** When a company is facing severe financial difficulties, such as mounting debts, cash flow problems, or an inability to meet its financial obligations, it may consider business rescue to avoid potential bankruptcy.
- **Operational Difficulties:** If a company is experiencing challenges in its operations, such as declining sales, loss of key customers, or inefficiencies in its processes, with a threat of not being able to repay its debt in the ensuing six months, business rescue may offer an opportunity to restructure and improve the company's performance.
- Business rescue is a viable option when **creditors threaten** to put the company into liquidation

Signs of Financial Distress

Recognizing the warning signs of financial distress is crucial for businesses to take timely action and potentially avoid insolvency. Some key indicators include:

- **Cash Flow Issues:** Persistent cash flow shortages, difficulty in paying suppliers or meeting financial obligations, and relying on credit to cover day-to-day expenses.
- **Mounting Debt:** Escalating levels of debt with high-interest payments, and difficulty in servicing loans or meeting interest payments.
- **Declining Profitability:** Sustained periods of losses or declining profit margins that threaten the company's ability to generate sustainable revenue.
- **Vendor and Creditor Disputes:** Frequent disputes with suppliers or creditors over unpaid bills or delayed payments.
- **Inability to Obtain Credit:** Struggling to secure credit or financing due to a poor credit rating or increased risk perception.



Benefits of Business Rescue

Protection Through Moratorium on Legal Proceedings

One of the biggest benefits of business rescue is the moratorium on legal proceedings against the company. This provides temporary relief from creditors' claims, preventing them from enforcing their rights during the rescue process. The moratorium allows the company time to stabilize and restructure without the immediate threat of legal action, asset seizures, or bankruptcy filings.

Possibility of Avoiding Liquidation

Business rescue aims to save the company from liquidation. Liquidation often results in the complete closure of a business, loss of jobs, and sale of assets at low values. With business rescue, there is a chance to rehabilitate the business, protect jobs, and restore financial stability. Even if the business cannot continue trading, business rescue can still provide a better return to creditors compared to liquidation.

Better Returns for Creditors

Creditors generally receive higher returns in a business rescue scenario than they would under liquidation. Business rescue provides for the restructuring of the company's debts and offers creditors a more favorable outcome through repayment plans, restructuring, or converting debt into equity. In contrast, liquidation may result in lower payouts due to the rapid sale of assets.

Safeguarding Jobs

One of the key focuses of business rescue is preserving jobs. Unlike liquidation, where employees are typically laid off and contracts are terminated, business rescue allows employees to remain employed under the same terms unless changes are negotiated or pursued in accordance with the labor law. This approach helps protect livelihoods while giving the company a chance to recover.

Time to Restructure

Business rescue provides companies with time to assess their situation and develop a workable solution to their financial distress. The business rescue practitioner (BRP) can renegotiate unfavorable contracts, reorganize operations, and implement cost-saving measures to give the business a fighting chance.

Post-Commencement Finance (PCF)

During business rescue, companies can raise post-commencement finance (PCF) to keep operations running. PCF enjoys preferential status and is given priority over other unsecured debts, making it easier for companies to secure necessary funding. This allows the company to continue trading while it restructures its finances.

Clear, Structured Process for Recovery

The Companies Act provides a structured framework for business rescue, offering clear steps to be followed. This framework provides certainty to all parties involved, from creditors to employees. It ensures that everyone's rights are protected, and that the rescue plan is subjected to scrutiny and approval by creditors and affected parties.

Transparency and Participation

Business rescue ensures transparency and gives affected persons—creditors, employees, and shareholders—a voice in the process. They are informed and consulted at various stages, including the formulation and approval of the rescue plan. This inclusive approach promotes fairness and ensures that decisions are made with the consent of the stakeholders.

Possibility of a Fresh Start

For many companies, business rescue represents an opportunity for a fresh start. It allows businesses to renegotiate contracts, reduce debts, and streamline operations, all under the protection of the law. Successful business rescues can return the company to profitability, preserving value for all stakeholders.

Involvement of a Professional Business Rescue Practitioner (BRP)

The appointment of a BRP ensures that the company's restructuring is overseen by an experienced and independent professional. The BRP brings objectivity, skills, and expertise to the process, guiding the company toward a realistic and achievable recovery plan.

Efficient Restructuring:

Business rescue allows for a comprehensive evaluation and restructuring of the company's operations, finances, and management to identify sustainable solutions.

Improved Cash Flow:

Through restructuring, the company can optimize its operations and cash flow, enhancing overall financial stability.

Continuity:

Business rescue allows the company to continue operating under the supervision of a business rescue practitioner, providing an opportunity to preserve jobs and maintain ongoing business relationships.



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Are you facing any of these challenges?

If the answer is yes, **you are not alone.**

Taking proactive steps can **help safeguard your company's future** and potentially restore its financial health.

Reach out to us today for a **FREE pre-assessment.**

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