



## **CORPORATE RESCUE- THERAPY FOR BUSINESSES**

### **THE FUNDAMENTALS OF CORPORATE RESCUE PROCEEDINGS IN ZIMBABWE**

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#### **WHAT IS CORPORATE RESCUE**

Corporate rescue means proceedings to facilitate the rehabilitation of a company that is financially distressed. The concept of corporate rescue was introduced into our Zimbabwean law by the enactment of the Insolvency Act [chapter 6:07] (hereinafter referred to as the Act) in 2018. The enactment saw the substitution of judicial management, which was provided for in the old Companies Act (Chapter 24:03), by the concept of corporate rescue. The concepts of judicial management and corporate rescue are similar in nature and designed for the same purpose but the law has detailed and more transparent provisions for the conduct of corporate rescue proceedings. Our law borrows heavily from the South African concept of business rescue which is designed for similar purposes. This article will outline and analyse the basics of corporate rescue proceedings in Zimbabwe.

#### **A 'FINANCIALLY DISTRESSED COMPANY'**

A company is deemed to be financially distressed when it appears to be reasonably unlikely that the company will be able to pay all of its debts as they become due and payable within the immediately ensuing six months. A company is also financially distressed when it appears to be reasonably likely that the company will become insolvent within the immediately ensuing six months.<sup>1</sup> Corporate rescue therefore gives relief to such a company by providing for:

- (i) the temporary supervision of the company, and of the management of its affairs, business and property by an outsider; and
- (ii) a temporary moratorium on the rights of creditors against the company or in respect of 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.

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<sup>1</sup> Section 121(1)(f) of Insolvency Act



## WHAT IS THE AIM OF CORPORATE RESCUE?

Although the aims of corporate rescue are not clearly enunciated in the Act, it can be deduced that it aims to resuscitate distressed companies, saving them from extinction which would have been otherwise suffered through liquidation. Effectively speaking, corporate rescue intends to award distraught companies with a second chance at survival. The South African Courts articulated the purpose of corporate rescue in the case of **Absa Bank Limited vs Caine No and Another**<sup>2</sup> where it was held that;

*Business rescue proceedings are much more flexible and financially distressed company friendly than judicial management. The potential business rescue plan provided for in ss 128(1)(b)(iii) has two objects in mind, the primary object being to facilitate the continued existence of the company in a state of solvency and secondly and in the alternative, in the event that the primary objective cannot be achieved or appears not to be viable, to facilitate a better return for the creditors or shareholders of the company than would result from immediate liquidation.*

It is important to highlight that the reference and definition of ‘financial distress’ in the Act appears to be more focused on the future. The provisions in the Act on corporate rescue therefore address questions of probable insolvency as opposed to immediate insolvency. The implication is that corporate rescue proceedings cannot be applied to save companies that are already insolvent.

## CORPORATE RESCUE VERSUS LIQUIDATION

The purpose of liquidation proceedings is to shut the company down, dispose of its assets and settle creditors’ claims. The proceeds from the disposition of the assets will be used to pay the creditors of the company. On the other hand, corporate rescue aims to rehabilitate distressed companies to avoid the winding down of the business. This makes corporate rescue a more attractive option for businesses. However, there is interplay between the two options. In the event that liquidation proceedings had commenced against a company, an application to court for corporate rescue will suspend the liquidation proceedings.<sup>3</sup> In the same vein, where corporate rescue proceedings fail to resuscitate the company, liquidation proceedings may be commenced to serve the interests of the company’s creditors. It is apparent that even though liquidation is an avenue open to distraught companies, it is the last resort. Where there is a chance of survival, a company must be placed under corporate rescue.

## CORPORATE RESCUE PRACTITIONER

A corporate rescue practitioner is a person whose role is to investigate the company’s affairs, business, property and financial situation and thereafter consider whether there is any reasonable prospect of rescuing the company. Section 131 of the Act outlines the qualifications of a corporate rescue practitioner.

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<sup>2</sup> 2014 ZAF SCH 48

<sup>3</sup> Section 124(6) of the Insolvency Act



The key element being that a corporate rescue practitioner must not have a relationship with the company such as would lead a reasonable person to conclude that the integrity, impartiality and objectivity of the corporate rescue practitioner is compromised by that relationship.<sup>4</sup> For a person to be appointed as a corporate rescue practitioner, he or she must be registered with the Council of Estates Administrators and the Insolvency and Restructuring Association of Zimbabwe (IRAZ).

➤ **POWERS OF A CORPORATE RESCUE PRACTITIONER**

A corporate rescue practitioner is responsible for the full management of the company in substitution for its board and pre-existing management.

In addition to that a corporate rescue practitioner is responsible for developing a corporate rescue plan to be considered by affected parties and implementing any corporate rescue plan that has been adopted. In essence, the corporate rescue practitioner becomes takes charge of the affairs of the company and is responsible for charting the revival process. He thus has a duty to act in the best interests of the company and its stakeholders. The corporate rescue practitioner can be sued if he performs his duties fraudulently or in a grossly negligent manner which is prejudicial to creditors, shareholders or the company itself.

The corporate rescue may delegate any of his/her powers or functions to a person who was part of the board or pre-existing management of the company.

➤ **DUTIES OF A CORPORATE RESCUE PRACTITIONER**

Section 133(4) makes it clear that during a company's corporate rescue proceedings, the corporate rescue practitioner is an officer of the court and must report to the court. Adding on to that, a corporate rescue practitioner has the responsibilities, duties and liabilities of a director of the company.

➤ **CORPORATE RESCUE PRACTITIONER'S REMUNERATION**

A corporate rescue practitioner is entitled to charge an amount to the company for the remuneration and expenses of the practitioner in accordance with the Second Schedule item 1

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<sup>4</sup> Ibid section 131(1)(d)



which may be amended by the Minister from time to time by way of notice in the Gazette.<sup>5</sup> Currently, the law provides that he can charge in terms of a scale provided for in the Act.<sup>6</sup>

A corporate rescue practitioner may propose an agreement with the company providing for further remuneration as a contingency fee.<sup>7</sup> Once the proposed agreement is approved by shareholders and creditors it becomes binding on the company.

In order to protect both the financially distraught company from unreasonable exorbitant changes and the corporate rescue practitioner from being underpaid, the Master of the High Court, may, for good cause decrease or increase the corporate rescue practitioner's remuneration.<sup>8</sup> In circumstances where the corporate rescue practitioner's remuneration and expenses are not fully paid, the practitioner's claim for those amounts will rank in priority before the claims of all other secured and unsecured creditors.

#### ➤ **REMOVAL OF A CORPORATE RESCUE PRACTITIONER**

A corporate rescue practitioner may only be removed by a court order; or by the Master of the High Court upon the request of an affected person. A corporate rescue practitioner may only be removed on any of the following grounds:

- (a) incompetence or failure to perform the duties of a corporate rescue practitioner of the particular company;
- (b) failure to exercise the proper degree of care in the performance of the corporate rescue practitioner's functions;
- (c) engaging in illegal acts or conduct;
- (d) if the corporate rescue practitioner no longer satisfies the requirements set out in section 131 (l);
- (e) conflict of interest or lack of independence;
- (f) the corporate rescue practitioner is incapacitated and unable to perform the functions of that office, and is unlikely to regain that capacity within a reasonable time.

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<sup>5</sup> Section 136 of the Act

<sup>6</sup> Second Schedule, item 1

<sup>7</sup> Ibid subsection 2

<sup>8</sup> Subsection 6



On any of the outlined grounds, the court may on its own accord or upon the request of an affected party remove a corporate rescue practitioner. The removal of a corporate rescue practitioner is not taken lightly by the courts due to the sensitivity of the nature of corporate rescue proceedings. In the case of **Kurt Robert Knoop & Anor v Chetaali Gupta & Anor**<sup>9</sup> the court held that,

*The discretion is exercisable if one or more of the grounds for removal set out in s 139(2) has been established on a balance of probabilities. However, proof of a ground for removal alone does not dictate that an order for removal must follow. The power of removal is not combined with a duty to exercise that power... Two general principles will be that removal is not something to be ordered lightly and that the primary reason justifying removal will be actual or potential prejudice or harm to the interests of the company, and those in whose interests the administration was established, creditors in circumstances of insolvency.*

## HOW IS A COMPANY PLACED UNDER CORPORATE RESCUE?

There are two main ways in which a company is placed under corporate rescue namely:-

1. Where the board of a company resolves that the company voluntarily begin corporate rescue proceedings, and
2. By a court order granted upon the application of an affected person to place the company under corporate rescue. Shareholders, creditors or trade unions representing employees of the company are regarded as affected persons.

### 1. CORPORATE RESCUE PROCEEDINGS COMMENCED BY COMPANY RESOLUTION

The Board of a company is responsible for the company's welfare and has the responsibility to promote the success of the company.<sup>10</sup> It is a company's board therefore, that makes a decision of whether or not a company must be placed under corporate rescue. The Act states that where the board has reasonable grounds to believe that a company is financially distressed and there appears to be a reasonable prospect of rescuing the company, it may resolve that voluntary corporate proceedings commence in a bid to save the company.<sup>11</sup>

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<sup>9</sup> 116/2020 ZASCA 163

<sup>10</sup> Section 195 of the Companies and other Business Entities Act [Chapter 24:31]

<sup>11</sup> Section 122 of the Act



## THE PROCEDURE AND TIME LIMITS

The Board's resolution has to be filed with the Master of the High Court and the Registrar of Companies. Upon filing with the Master, a company must, within **five days** give notice of the resolution and its effective date to every affected person. Secondly, the company must appoint a corporate rescue practitioner who satisfies the requirements that have been discussed above. Once a rescue practitioner has been appointed, the company must within **two working days** file a notice of such appointment to the Registrar of Companies. Thereafter, within **five days**, the company must publish a copy of the notice to each affected person. In the event that it is evident that a company is financially distraught and the Board does not resolve to commence corporate rescue proceedings, it should deliver a written notice to each affected person, stating reasons for not adopting a resolution as contemplated.

It is important to note that corporate rescue proceedings are governed by strict timelines which must be adhered to. In addressing the question why the proceedings are regulated that way the court in the case of **Koen & Another v Wedgehood Village Golf & Country Estate (Pty) Limited & Others**<sup>12</sup> held that *"It is axiomatic that business rescue proceedings, by their very nature, must be conducted with the maximum possible expedition. In most cases a failure to expeditiously implement rescue measures when a company is in financial distress will lessen or entirely negate the prospect of effective rescue. Legislative recognition of this axiom is reflected in the tight timelines given in terms of the Act for the implementation of business rescue procedures if an order placing a company under supervision for that purpose is granted"*.

Failure to comply with time limits defeats the very purpose of corporate rescue proceedings. The consequences of failing to adhere to the stipulated time limits are that the resolution filed will lapse and become a nullity. In addition, a company may not file a further resolution for a period of three months unless an application for extension of time limits is made and granted by the court.

## OBJECTIONS TO COMPANY RESOLUTION

Section 123 of the Act deals with instances where a person may object to a company resolution placing the company under corporate rescue. It is provided that at any point after the adoption of a resolution but before the adoption of corporate rescue plan, an affected person may apply to a court for an order setting aside the resolution or setting aside the appointment of a corporate rescue practitioner. Reasonable grounds must be given in support of such an application. It can be argued that the reason for that is to minimize the delays in corporate rescue proceedings. Equally important, a director of a company who once voted in support of the resolution cannot later object to it unless they provide the Court with satisfactory proof that they voted in good faith on the basis of information that has subsequently been

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<sup>12</sup> 2012 (2) SA 378 (WCC)



found to be false or misleading<sup>13</sup>. In assessing such matters, the courts do what is just and equitable in any given circumstances.

## 2. CORPORATE RESCUE PROCEEDINGS COMMENCED BY A COURT ORDER

An affected person may apply to a Court at any time for an order placing the company under supervision and commencing corporate rescue proceedings.<sup>14</sup> The corporate rescue proceedings are deemed to have commenced with effect from the date that the court application is filed.

### THE APPLICATION

The application contemplated by the Act must show clearly to the Court that the company is financially distressed and there is a chance of survival for the company in question. The South African Courts have made it clear that emphasis must be placed on the company's chances of survival. In the case of **Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 Ltd**<sup>15</sup> the court held that; *"...it is difficult to conceive of a rescue plan in a given case that will have a reasonable prospects of success of the company concerned continuing on a solvent basis unless it addresses the cause of the demise or failure of the company's business, and offers a remedy therefore that has a reasonable prospect of being sustainable. A business plan which is unlikely to achieve anything more than to prolong the agony, i.e. by substituting one debt for another without there being light at the end of a not too lengthy tunnel, is unlikely to suffice."*

The standard of proof that is required when one is making an application seeking an order to commence corporate rescue proceedings is therefore very high. It can be argued that the reason why the courts are strict in this regard is to try and strike a balance between the interests of shareholders (company owners) and their creditors. Corporate rescue proceedings are not a shield for shareholders who are trying to evade their responsibilities and obligations to creditors.

### THE EFFECTS OF THE COURT APPLICATION

It is necessary to highlight that once an application of this nature is filed, it suspends any liquidation proceedings which had commenced against the company. The application must be served on

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<sup>13</sup> Section 123(2) of the Act

<sup>14</sup> Section 124 of the Act

<sup>15</sup> 2012 (2) SA 423 (WCC)



company, the Registrar of Companies and the Master of the High Court. Each affected person must be notified of the same and be allowed to participate in the court proceedings. The rationale behind this is that every person affected must be awarded a chance to protect their rights and interests. After considering the application, the court, if satisfied that the company is financially distressed and it is just and equitable to do so, may grant an order placing the company under supervision and commencing corporate rescue proceedings.

## **DURATION OF CORPORATE RESCUE PROCEEDINGS**

Section 125(3) of the Act stipulates that proceedings must be completed within a time period of three months. If proceedings do not end within the stipulated time, the corporate rescue practitioner may apply for extension of the proceedings and must; then prepare a report on the progress of the corporate rescue proceedings which must be updated at the end of each subsequent month until the end of those proceedings. The progress report must be delivered to each affected person and the court if the proceedings were commenced by a court order and to the Master.<sup>16</sup>

### **WHEN DO CORPORATE RESCUE PROCEEDINGS BEGIN?**

Corporate rescue proceedings begin when the company files a resolution to place itself under supervision or when an affected person applies to the court for an order placing the company under supervision. Proceedings also begin when a court makes an order placing a company under supervision during the course of liquidation proceedings.<sup>17</sup>

### **WHEN DO CORPORATE RESCUE PROCEEDINGS END?**

Corporate rescue proceedings end when the court sets aside the resolution or order that began those proceedings or has when the court has converted the proceedings to liquidation proceedings. Corporate rescue proceedings may also end when the corporate rescue practitioner has filed a notice of the termination of the corporate rescue proceedings with the Master. Section 125(2)(c) provides that proceedings may also end when a corporate rescue plan has been proposed and rejected and no affected person has acted to extend the proceedings. Also proceedings end, when a plan has been adopted and the practitioner has subsequently filed a notice of substantial implementation of that plan.

## **EFFECTS OF CORPORATE RESCUE PROCEEDINGS**

### **GENERAL MORATORIUM ON LEGAL PROCEEDINGS AGAINST COMPANY**

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<sup>16</sup> Section 125(3) of the Act

<sup>17</sup> *ibid*



No legal proceedings may be instituted in any forum against a company that is under corporate rescue. This includes enforcement of orders against the company or any property belonging to it. The moratorium has been described as the cornerstone of corporate rescue proceedings. The rationale for the moratorium is to provide the company under corporate rescue with the much needed breathing space or a period of respite to enable the company to restructure its affairs. The moratorium allows the practitioner, in conjunction with the creditors and other affected parties, to formulate a business rescue plan designed to achieve the purpose of the whole process.<sup>18</sup> In the event that any right to commence proceedings or otherwise assert a claim against a company is subject to a time limit, the measurement of that time must be suspended during the corporate rescue proceedings.<sup>19</sup>

#### **CIRCUMSTANCES UNDER WHICH LEGAL PROCEEDINGS MAY BE INSTITUTED AGAINST A COMPANY**

Legal proceedings may be instituted against a company under corporate rescue under the following circumstances:

- (a) with the written consent of the practitioner; or
- (b) with the leave of the Court and in accordance with any terms the Court considers suitable; or
- (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;
- (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.

#### **EMPLOYEES**

Employees of the company continue to be so employed on the same terms and conditions except to the extent that changes occur in the ordinary attrition or if the employees and the company in accordance with applicable labour laws, agree on different terms and conditions. The Act goes on to provide that any retrenchment of any such employees contemplated in the corporate rescue plan is subject to the Labour Act (chapter 28:01) and any other applicable employment related legislation.<sup>20</sup>

#### **CONTRACTS**

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<sup>18</sup> Murray N.O & Anor v Firstrand Bank Ltd t/a Wesbank 2015 (3) SA 438 (SCA)

<sup>19</sup> Section 126(3)

<sup>20</sup> Section 129(1) of the Act



During corporate rescue proceedings, the practitioner may entirely, partially or conditionally suspend for the duration of the corporate rescue proceedings any contractual obligations that the company may have entered into at the commencement of the proceedings or may become due during the proceedings. In addition, the practitioner may make an urgent application to the court for an order to entirely, partially or conditionally cancel the contractual obligations of the company. Any party whose agreement that has been suspended or cancelled, or any provision which has been suspended or cancelled may assert a claim against the company only for damages.

## SHAREHOLDERS

Any alteration in the classification or status of any issued securities of a company during corporate rescue proceedings, other than by way of transfer of securities in the ordinary course of business is invalid except to the extent that the court directs or as contemplated in an approved corporate rescue plan.

## DIRECTORS

The company's board is deemed dissolved and the directors may not exercise the functions of directors. Furthermore, the directors may only exercise management function within the company in accordance with the express instructions or directions of the corporate rescue practitioner. They however have the duty to assist the corporate rescue practitioner at all times and provide him with any information about the company's affairs. If a director takes any action on behalf of the company after the commencement of corporate rescue proceedings, such an action will be void unless approved by the corporate rescue practitioner.

## CORPORATE RESCUE PLAN

A corporate rescue plan is the blueprint for how the company is going to be resuscitated. The corporate rescue plan is prepared by the corporate rescue practitioner and must be published within forty-five business days from the date the corporate rescue practitioner is appointed. Corporate rescue plans are regulated by Section 142 of the Act. They must contain the following:

**ASSETS-** a complete list of all the material assets of the company, as well as an indication as to which assets were held as security by creditors when the corporate rescue proceedings began.

**CREDITORS-**a complete list of the creditors of the company when the corporate rescue proceedings began. as well as an indication as to which creditors would qualify as secured, statutory preferent and concurrent in terms of the laws of insolvency, and an indication of which of the creditors have proved their claims

The plan must also include the probable dividend that would be received by creditors, in their specific classes if the company were to be placed in liquidation, a complete list of the holders of the company's issued securities. A copy of the written agreement concerning the practitioner's remuneration. In



addition it must contain proposals indicating the duration of the moratorium, the extent to which the company is to be released from the payment of its debts, the ongoing role of the company and the treatment of any existing agreements and the benefits of adopting the corporate rescue plan. The plan must be completed with a statement

### **ADOPTION OF THE PLAN AND IMPLICATIONS**

A corporate rescue plan is adopted when a vote for preliminary approval is conducted and it is supported by the holders of more than 75% of the creditors voting interests. If the plan is not approved at this stage it is deemed rejected. A corporate rescue plan that has been adopted is binding on the company and on each of the creditors of the company and on every holder of the company's securities regardless of whether they were present at the meeting, voted in favour of the plan or in the case of creditors, had proved their claim. The company through the corporate rescue practitioner must therefore take all the necessary steps to satisfy the conditions on which the plan is contingent and implement the plan. When the plan has been substantially implemented, the corporate rescue practitioner must file a notice of substantial implementation of the corporate rescue plan.<sup>21</sup>

### **FAILURE TO ADOPT A CORPORATE RESCUE PLAN**

Section 145 provides that if a corporate rescue plan has been rejected, the practitioner may seek a vote of approval to prepare and publish a revised plan or apply to a court to set aside the result of the vote. If the corporate rescue practitioner fails to do the above, any affected person may do so. If no person takes any of the above actions, the corporate rescue practitioner must promptly file a notice of the termination of corporate rescue proceedings.

## **CONCLUSION**

The concept of corporate rescue was introduced to replace judicial management in which the courts played a central role and fell short of efficacy. The move to introduce a way that does not merely rescue potentially successful parts of a company but rescues the whole company shows progress in Zimbabwe's company laws. The strengths of the enacted laws on corporate rescue include that it allows a company to voluntarily commence corporate rescue proceedings without applying to the court, saving its already strained financial resources. Furthermore, the law provides strict timelines which should be observed during the proceedings. This strikes a balance between the interests of the company and any affected persons. Timelines give the company a chance to revive itself while at the same time taking into cognizance the interests of creditors who need to be paid. Moreover, the general moratorium provides a company under corporate rescue with breathing space allowing it to fully works towards its full resuscitation. Lastly, corporate rescue proceedings aim to fully save the

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<sup>21</sup> Section 144 of the Act



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financially distressed company and not just parts of it. The laws protect the employees of such a company, their employee status does not change during corporate rescue proceedings.

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