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(1) Reportable: [redacted]/No
(2) Of interest to other Judges: Yes/[redacted]
(3) Revised ✓ 29/3/13

REPUBLIC OF SOUTH AFRICA

SOUTH GAUTENG HIGH COURT, JOHANNESBURG

CASE NO: 12/45437

In the matter between:

NEWCITY GROUP (PTY) LIMITED	Applicant
and	
ALLAN DAVID PELLOW N.O.	First Respondent
GONASGREE GOVENDER N.O.	Second Respondent
LEBOGANG MICHAEL MOLOTO N.O.	Third Respondent
LEBOGANG MORAKE N.O.	Fourth Respondent

[In their capacities as joint provisional liquidators of CRYSTAL LAGOON INVESTMENTS 53 (PTY) LIMITED (IN PROVISIONAL LIQUIDATION)]

CHINA CONSTRUCTION BANK CORPORATION (JOHANNESBURG BRANCH)	Fifth Respondent
ABSA BANK LIMITED	Sixth Respondent

And in the matter between:

CASE NO: 16566/12

CHINA CONSTRUCTION BANK CORPORATION JOHANNESBURG BRANCH	Applicant
and	
CRYSTAL LAGOON INVESTMENTS 53 (PTY) LTD	First respondent
CORNELIUS FOURIE MYBURGH N.O.	Second Respondent
ABSA BANK LIMITED	Affected Party

JUDGMENT

VAN EEDEN AJ:

1. Mr Chaim Cohen ("Cohen") is the sole shareholder and director of the applicant, Newcity Group (Pty) Limited ("Newcity"). Cohen is also the sole director of Crystal Lagoon Investments 53 (Pty) Limited (in provisional liquidation) ("Crystal Lagoon"). Newcity is the sole shareholder in Crystal Lagoon. It is a creditor of Crystal Lagoon and as such qualifies as an affected person in terms of s 128 of the Companies Act No 71 of 2008 ("the Act"). In terms of s 131 of the Act, Newcity applies that Crystal Lagoon be placed under supervision and that business rescue proceedings be commenced. Apart from citing the joint provisional liquidators, Newcity joined China

Construction Bank Corporation ("CCB") as the fifth respondent and ABSA Bank Limited ("ABSA") as the sixth respondent.

2. Crystal Lagoon is the owner and operator of the hotel known as the "Park Inn by Radisson". It is commercially insolvent inasmuch as its current cash flows are insufficient to pay the debt owed by it to CCB, although its other debts can be paid as and when they become due. The debt to CCB arose from a property development facility agreement and currently amounts to some R230 million. The last payment Crystal Lagoon made to CCB in respect of this loan was December 2011.

3. Although Newcity joined ABSA as a respondent, it denies that Crystal Lagoon is indebted to ABSA. It thus disputes that ABSA is an affected person.

4. The matter has some history:

4.1. During April 2011 Crystal Lagoon defaulted on its obligations to CCB and, as already stated, the last payment made to CCB was during December 2011.

4.2. On 27 January 2012 Cohen passed a resolution placing Crystal Lagoon into business rescue in terms of s 129 of the Act.

4.3. On 3 February 2012 CCB demanded repayment of all amounts due to it as at 1 January 2012, being an amount of R215 973 902.23.

4.4. On 17 February 2012 a business rescue practitioner was appointed for Crystal Lagoon. During the first meeting of affected persons on 29 February 2012 the business practitioner advised that five separate entities had expressed an interest in investing in the hotel.

4.5. At the second meeting held on 20 March 2012 the business practitioner was granted an extention within which to deliver the business rescue plan until 13 April 2012. He failed to deliver such a plan and requested a further extention until 4 May 2012. The latter request for an extention was not agreed to and he once again failed to deliver the business rescue plan.

4.6. On 10 May 2012 CCB launched an application to set aside the resolution which placed Crystal Lagoon in business rescue.

4.7. Crystal Lagoon opposed CCB's application, but never filed an answering affidavit. Instead, on 26 June 2012 when CCB's application was enrolled, the business practitioner and Crystal Lagoon appeared at the hearing and indicated their intention to oppose the application. CCB was consequently forced to remove its application from the unopposed motion roll.

4.8. On 27 August 2012 ABSA launched an application to intervene in CCB's application to set aside the resolution placing Crystal Lagoon in business rescue.

4.9. On 18 October 2012 CCB again enrolled its application to set aside Cohen's resolution for hearing on 23 October 2012. On the day before the hearing Cohen's attorney informed CCB's attorney that Crystal Lagoon's answering affidavit would be delivered the following day. Instead, no answering affidavit was delivered and the parties agreed upon an order, which entailed that the business rescue proceedings launched by Cohen were set aside and Crystal Lagoon was placed under a provisional winding up order returnable on 4 December 2012.

4.10. On 4 December 2012, being the return day of the provisional winding up order, Newcity handed the current application to place Crystal Lagoon under business rescue to CCB's attorney at Court and by agreement the provisional winding up order was extended until Tuesday 11 March 2013. Costs were reserved and time periods for the exchange of further affidavits were ordered.

5. On 15 March 2013 the matter was argued before me whereafter, again by agreement between the parties, I extended the provisional winding up order to 9 April 2013 and reserved judgment in the application for business rescue.

6. Newcity's application is based on the provisions of s 131 of the Act. In terms thereof an affected person may apply to a Court *"at any time for an order placing the company under supervision and commencing business rescue proceedings"*. It follows that Newcity was entitled to launch these proceedings, notwithstanding the fact that Crystal Lagoon was placed in provisional winding up by consent. It remains, however, to be explained why the provisional winding up was agreed to, if business rescue remained a reasonable prospect.

7. Section 7(k) requires a court to balance the rights and interests of relevant stakeholders. S 131(4) vests the court with a discretion to order, or refuse, business rescue sought under s 131(1) when certain jurisdictional requirements are present, or to dismiss the application together with any further necessary and appropriate order, including an order placing the company under liquidation. The jurisdictional requirements are stated in s 131(4)(a). These are that –

(i) the company is financially distressed;

(ii) the company has failed to pay over any amount in respect of an obligation under or in terms of a public regulation, or contract, with respect to employment-related matters; or

(iii) it is otherwise just and equitable to do so for financial reasons.

8. Of these three grounds only the first, namely that the company is financially distressed, is allowed under s 129(1) where the board of a company may resolve that the company voluntarily begins business rescue proceedings and place the company under supervision. Each of jurisdictional requirements (i), (ii) and (iii) is qualified by a further, and thus overriding requirement, which is that *"there is a reasonable prospect for rescuing the company"*. Regardless of which jurisdictional requirement is present, in each instance there must also be a reasonable prospect for rescuing the company. I am in respectful agreement with the reasoning adopted by JP Coetzee AJ in **Petzetakis'** case,[1] but I should point out that there seems to be a contradiction in the section itself. One understands the logic of requiring a reasonable prospect for rescuing the company in respect of jurisdictional requirements (i) and (iii), but is seems unnecessary and impossible to require it in respect of (ii). I agree with the comments in Henochsberg on the Companies Act 71 of 2008 in this regard. It remains to be seen how the absence of a *"reasonable prospect for rescuing the company"* will derail an application for business rescue based on jurisdictional requirement (ii).

9. In the liquidation application launched by CCB two affidavits were handed up in court. The one affidavit was filed on behalf of unionised employees and the other on behalf of non-unionised employees of Crystal Lagoon. Both affidavits reflect that the employees are in favour of business rescue and it appears that jurisdictional ground (ii) is absent. It was admitted by CCB that

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1 AG Petzetakis International Holdings Ltd v Petzetakis Africa (Pty) Ltd & Others (Marley Pipe Systems (Pty) Ltd & Another Intervening) 2012 (5) SA 515 (GSJ) [13].

Crystal Lagoon is unable to pay its debts as they become due and payable within the immediately ensuing six months. It was thus demonstrated that Crystal Lagoon is financially distressed and that the requirement set out in (i) is present.

10. It remains to be determined whether there is a reasonable prospect for rescuing the company and, if so, whether the Court should exercise its discretion to grant the order. The Act makes it clear that business rescue is preferred to liquidation. S 128(1)(b) explains that business rescue means proceedings to facilitate the rehabilitation of a company that is financially distressed by providing for –

10.1. the temporary supervision of the company, and of the management of its affairs, business and property;

10.2. a temporary moratorium on the rights of claimants against the company or in respect of property in its possession; and

10.3. 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 so to 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.

11. There are conflicting views on how a court should determine whether *"there is a reasonable prospect for rescuing the company"*. Eloff AJ gave a judgment on the complex problem of applications for business rescue when he had little, if any, precedent to follow. His views were expressed in the **Southern Palace** matter[2] and were approved in a number of cases.[3] I quote two paragraphs of his judgment:

> *"24. While every case must be considered on its own merits, it is difficult to conceive of a rescue plan in a given case that will have a reasonable prospect 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 therefor 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. One would expect, at least, to be given some concrete and objectively ascertainable details going*

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2 Southern Palace Investments 265 (Pty) Ltd v Midnight Storm Investments 386 Ltd 2012 (2) SA 423 (WCC).

3 E.g. Koen and Another v Wedgewood Village Golf & Country Estate (Pty) Ltd and Others 2012 (2) SA 378 (WCC); Zoneska Investments (Pty) Ltd t/a Bonatla Properties (Pty) Ltd v Midnight Storm Investments Ltd (Reg no:2007/019270/06) and Another (Grayhaven Riches 9 Ltd and others as Interested Parties; First Rand Bank Ltd as Intervening Creditor) [2012] 4 All SA 590 (WCC); AG Petzetakis International Holdings Ltd v Petzetakis Africa (Pty) Ltd & Others (Marley Pipe Systems (Pty) Ltd & Another Intervening) 2012 (5) SA 515 (GSJ); Nedbank Ltd v Bestvest 153 (Pty) Ltd; Essa and Another v Bestvest 153 (Pty) Ltd and Others 2012 (5) SA 497 (WCC).

beyond mere speculation in the case of a trading or prospective trading company, of:

24.1 *The likely costs of rendering the company able to commence with its intended business, or to resume the conduct of its core business;*

24.2 *the likely availability of the necessary cash resource in order to enable the ailing company to meet its day-to-day expenditure, once its trading operations commence or are resumed. If the company will be reliant on loan capital or other facilities, one would expect to be given some concrete indication of the extent thereof and the basis or terms upon which it will be available;*

24.3 *the availability of any other necessary resource, such as raw materials and human capital;*

24.4 *the reasons why it is suggested that the proposed business plan will have a reasonable prospect of success.*

25. *In relation to the alternative aim referred to in s 128(1)(b)(iii) of the new Act, being to procure a better return for the company's creditors and shareholders than would result from the immediate liquidation thereof, one would expect an applicant for business rescue to provide concrete factual details of the source, nature and extent of the*

resources that are likely to be available to the company, as well as the basis and terms on which such resources will be available. It is difficult to see how, without such details, a court will be able to compare the scenario sketched in the application with that which would obtain in an immediate liquidation of the company. Mere speculative suggestions are unlikely to suffice."

12. Van der Merwe J felt that this line of reasoning placed the bar too high. In **Propspec Investments**[4] he stated as follows:

"11. I agree that vague averments and mere speculative suggestions will not suffice in this regard. There can be no doubt that, in order to succeed in an application for business rescue, the applicant must place before the court a factual foundation for the existence of a reasonable prospect that the desired object can be achieved. But with respect to my learned colleagues, I believe that they place the bar too high.

12. In my view, a prospect in this context means an expectation. An expectation may come true or it may not. It therefore signifies a possibility. A possibility is reasonable if it rests on a ground that is objectively reasonable. In my judgment, a reasonable prospect means no more than a possibility that rests on an objectively reasonable ground or grounds.

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4 Propspec Investments (Pty) Ltd v Pacific Coast Investments 97 Ltd & Another 2013 (1) SA 542 (FB) [11], [12] and [15].

15. *In my judgment it is not appropriate to attempt to set out general minimum particulars of what would constitute a reasonable prospect in this regard. It also seems to me that to require, as a minimum, concrete and objectively ascertainable details of the likely costs of rendering the company able to commence or resume its business, and the likely availability of the necessary cash resource in order to enable the company to meet its day-to-day expenditure, or concrete factual details of the source, nature and extent of the resources that are likely to be available to the company, as well as the basis and terms on which such resources will be available, is tantamount to requiring proof of a probability, and unjustifiably limits the availability of business rescue proceedings."*

13. Mr J J Brett SC and Mr D Mahon appeared for the applicant. Mr Brett stressed that it was unnecessary for the applicant to provide a business rescue plan. That was so, it was submitted, because of the provisions of s 140(1)(d), which details that the business practitioner's duty is to develop a business rescue plan to be considered by affected persons. It seems to me that Mr Brett's submission is unassailable. It is not a requirement that the applicant attach a business rescue plan to the founding affidavit. The applicant should base the application for business rescue upon a strategy that has a reasonable prospect of achieving one of the two objects stated in s 128 (1)(b)(iii), i.e. it must advance facts that can be developed into a business rescue plan that, if approved, will maximise the likelihood of the company continuing in existence on a solvent basis or, if it is not possible to 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. If such a strategy is not advanced in the application for business rescue, a court would hardly be satisfied that a reasonable prospect for rescuing the company exists.

14. All the courts seem to agree, as do I, that a company can only be rescued if there is a reasonable prospect that one of these objects will be attained on the basis of facts, not speculation. The requirement of a reasonable prospect in s 133 denotes two uncertain future events, namely the eventual rescue of the company or a better return as contemplated in s 128(1)(b). If objectively there is a reasonable possibility or likelihood of those uncertain future events occurring, the jurisdictional requirements have been satisfied, and the court can exercise its discretion. One can envisage that in some instances the modicum of evidence required will be less than in others, such as where the application is brought by somebody without in-depth knowledge of the affairs of the company. Keeping these considerations in mind, I cannot fault the guidelines provided by Eloff AJ. In fact, I find them well considered and helpful. At the same time I agree with both Van der Merwe and Eloff AJ that the bar should not be placed too high, given the legislator's preference of business rescue over liquidation. The test should be flexible and the circumstances of each case will determine whether the available facts give rise to a reasonable prospect or not. The court is vested with a discretion to

grant or refuse the relief sought. I agree with the view of CJ Claassen J in **Oakdene Square Properties**,[5] which I think is to the same effect.

15. The founding affidavit, simply put, reveals that current cash flows generated by the business are unable to pay the debt owed to CCB, rendering the company insolvent. The hotel operations seen in isolation are cash flow positive and all creditors other than CCB are paid as and when payment becomes due. For some or other reason the hotel manager, Rezidor Hotel Group South Africa (Pty) Limited ("Rezidor") has not been paid since the provisional liquidation, but the hotel operations generate sufficient cash flow for them to be paid as well. Rezidor filed an affidavit, but does not seek any relief. The Rezidor affidavit reflects that in the year ending 2011 a R7 million gross operating profit was recorded and in the year ending 2012, a R17.6 million gross operating profit was recorded. Although Cohen disputes the correctness of these amounts, he also made out a case that Crystal Lagoon's earnings before interest, taxation, depreciation and amortization for the period January to December 2012 amounted to some R14.6 million. Despite some severe criticism about his motives, Cohen has not offered an explanation for not making at least partial payment to CCB.

16. Cohen sought to blame Rezidor for the hotel's income being insufficient to meet the CCB loan. He states that Rezidor's poor management is the cause

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5 Oakdene Square Properties (Pty) Ltd and Others v Farm Bothasfontein (Kyalami) (Pty) Ltd and Others 2012 (3) SA 273 (GJS) [18].

of this problem. Furthermore, he states that if Crystal Lagoon can obtain *"third party funding"*, it can overcome its financial predicament.

17. The essence of the attempt to demonstrate that there is a reasonable prospect for rescuing the company, seems to be contained in these paragraphs of the founding affidavit:

> *"71. It is apparent from what is stated above that the primary obstacle to the rescue of Crystal Lagoon is the International Management Agreement with Rezidor which is presently extant. Quite apart from the provision of any funding, the removal of Rezidor as the hotel operator and the substitution therefore with Extrabold would provide Crystal Lagoon with a source of income which will enable Crystal Lagoon to service the debt owed by it to CCB.*
>
> *72. I am advised that a duly appointed business rescue practitioner would be able to suspend either or both of the loan agreements concluded with CCB and the International Management Agreement concluded with Rezidor. Indeed, I am further advised that upon application to Court, the business rescue practitioner would be able to cancel the International Management Agreement concluded with Rezidor. This would enable Crystal Lagoon to be rescued even in the event that no third party funding is procured.*
>
> *73. However, in the event that Crystal Lagoon is able to procure such funding, it would, obviously, provide for a situation which would be*

> *far more acceptable to CCB. Furthermore, I am advised that the prospects of procuring such funding are far greater in circumstances where Crystal Lagoon is under business rescue because of the preferent nature of creditors who provide post-commencement finance."*

18. The central theme of the founding and replying affidavits advance the replacement of Rezidor as manager and the obtaining of so-called third party funding as the two main considerations that create a reasonable prospect for rescuing the company.

19. Rezidor manages the hotel in terms of an International Management Agreement attached to the replying affidavit, which is to endure for a period of twenty years. Cohen's complaints against Rezidor notwithstanding, it is common cause that Rezidor has received no formal notice of breach and demand to remedy breaches in terms of the agreement. Rezidor's affidavit reflects that it will oppose any attempt to cancel the agreement and the papers do not advance any grounds upon which it can realistically be claimed that the agreement may be cancelled. The suggestion that if the management is taken over by Extrabold, it will lead to the satisfaction of the objects of business rescue, cannot be sustained. A reading of this very tentative proposal reflects an immediate expense for Crystal Lagoon of at least R10 million and there is no indication how Crystal Lagoon would fund that expense. Furthermore, on 14 February 2013 Mr Cohen advised CCB of the nature of the Extrabold structure, and that reflects a shortfall of R720 000

in the first year. Crystal Lagoon will not be able to service the CCB debt if Rezidor is replaced as manager.

20. Any attempt to replace Rezidor, presumably in terms of s 136 of the Act, is likely to lead to litigation to resist it or to a claim for damages. Whilst there may have been reason for dissatisfaction with the services rendered by Rezidor (I express no opinion in this regard), it is obvious to me that there are presently no objective grounds for dissatisfaction. The heads of argument and replying affidavit filed on behalf of Newcity reflect an acceptance of Rezidor's affidavit, detailing its proper management of the affairs of Crystal Lagoon. Rezidor's affidavit reflects that the real risk to Crystal Lagoon's business is the fact that its excessive borrowings cannot be serviced by the hotel operations. There is no indication of how this problem can be remedied. Be that as it may, the proposal to replace Rezidor with a different manager does not create a reasonable prospect that will rescue the company.

21. The remaining consideration to demonstrate a reasonable prospect for rescuing the company relates to the so-called *"third party funding"*. It was submitted that a third party could possibly come to the rescue of Crystal Lagoon by providing capital or by absorbing the CCB loan. In order to give some credence to this submission, the replying affidavit makes mention of a great number of so-called interested parties, who were not dealt with in the founding affidavit. A number of those so-called interested parties' approaches pre-date even the first business rescue that commenced during January 2012.

For instance, the approache from Peermont Global (Pty) Limited go back to September 2011.

22. Mr Brett submitted that the references to those expressions of interest, even after the consent to the provisional winding-up order, was to indicate that there is serious interest in the hotel and its business and, given the opportunity, a business rescue practitioner may pursue same.

23. If this application had been launched at the time that Crystal Lagoon first defaulted, I might perhaps have been persuaded that there was a reasonable prospect for rescuing the company by obtaining third party funding. The hotel operations seen in isolation are, after all, profitable and that consideration improves the marketability of the company. But the company was in business rescue and provisional liquidation for more than a year and no viable offer was received. In my view the contention that third party funding may still save Crystal Lagoon cannot be said to create the required reasonable prospect. It is true that there was, perhaps still is, interest, but nothing has materialised, and there is no imminent prospect of third party funding being obtained. Speculation cannot create a reasonable prospect under these circumstances, particularly since Cohen has intimate knowledge of the affairs of the company. He has made numerous efforts to secure such funding. This is clearly not a case of an applicant for business rescue without information about the company's affairs. If there were concrete facts to support this application, Cohen should have put them forward in the affidavits in support of Newcity's application.

24. Mr Brett submitted that creditors or shareholders would obtain a better return if business rescue were ordered. I disagree. No facts from which such an inference can properly be drawn were placed before me. The submissions made in respect of the difference between the costs of liquidators and business rescue practitioners, even if correct, will not lead to a discernable increased return. I also disagree with Mr Brett's submission that it was for the other affected persons to demonstrate that business rescue would not result in a better return for CCB. In my view the applicant for business rescue must demonstrate that business rescue would result in a better return. Thus, if a court is not satisfied that a better return would result, this objective of business rescue in not shown to exist.

25. In my view not one of the two objectives of business rescue is present. Even if one were, I would in any event have exercised my discretion against granting the application given the remoteness of a business rescue plan being approved and the rights and interests of the stakeholders. There is presently no viable business rescue plan – one must still be developed. The passing of more than a year without any solution renders the reasonable prospect of a plan being developed remote. It seems the reasonable prospects of rescuing the company have been exhausted.

26. CCB has co-operated with Cohen and Crystal Lagoon for more that a year to find a solution for the problems. It has indicated that it will oppose plans requiring it to write off a substantial portion of its loan. I don't think CCB can be faulted for adopting such an attitude. On top of this CCB has not been

paid for a very long time, whereas other creditors are. There is no obvious answer as to why Cohen is not causing payment to be effected to CCB. It has been established that other creditors are being preferred. The employees are employed in hotel operations that are effectively managed. It is likely that their employment will continue so that the hotel can be sold as a going concern. As already stated, I do not think it has been demonstrated that Newcity, the shareholder, will receive a better return if business rescue is ordered and the biggest creditor is in favour of liquidation. A creditor will normally know best whether a better return will be achieved by business rescue or not. In my view balancing the rights and interests of these stakeholders require that finality now be reached.

27. Mr A J Eyles appeared on behalf CCB and argued for a final winding-up order. Mr Brett agreed that such an order would be appropriate if the application for business rescue should fail.

28. It was hotly disputed that ABSA is a creditor of Crystal Lagoon. This issue appears to be the subject matter of on-going litigation. Mr L N Harris SC and Mr F Ismail appeared on behalf of ABSA and argued for costs in the event of the application being successful. In view of the dispute it would be better to postpone this issue *sine die.*

29. I make the following orders:

29.1. The application for business rescue is dismissed;

29.2. The applicant (Newcity) is ordered to pay the costs of the fifth respondent;

29.3. The issue of costs as between the applicant and the sixth respondent is postponed *sine die* and the sixth respondent is granted leave to re-approach court on these papers, duly amplified if so advised, for an order in respect of costs;

29.4. The order extending the provisional winding-up order to 9 April 2013 is replaced with a final winding up order of Crystal Lagoon;

29.5. The costs incurred by the fifth respondent as applicant in the application for Crystal Lagoon's liquidation under Case No 12/16566 are ordered to be costs in the winding up.

H VAN EEDEN
ACTING JUDGE

Counsel for applicant: Adv J J Brett SC and Adv D Mahon
Instructed by: Terry Mahon Attorneys

Counsel for fifth respondent: Adv A J Eyles
Instructed by: Bowman Gilfillan

Counsel for sixth respondent: Adv L N Harris SC and Adv F Ismail
Instructed by: Webber Wentzel Inc

Date of hearing: 15 March 2013

Date of judgment: 28 March 2013