THE SUPREME COURT OF APPEAL OF SOUTH AFRICA

JUDGMENT

Reportable
Case No: 189/2016

In the matter between:

FIRSTRAND BANK LIMITED **APPELLANT**

and

NORMANDIE RESTAURANTS INVESTMENTS **FIRST RESPONDENT**

DIMITRI PHILIPPOU **SECOND RESPONDENT**

Neutral Citation: *FirstRand Bank v Normandie Restaurants* 189/2016 [2016] ZASCA 178 (25 November 2016)

Coram: Lewis, Cachalia, Tshiqi, Willis and Dambuza JJA

Heard: 10 November 2016

Delivered: 25 November 2016

Summary: Companies Act 71 of 2008: business rescue proceedings: whether a company which is in financial distress has reasonable prospects of being rescued as envisaged in s 131(4)*(a)* of the Act: a final order for winding-up of the company more beneficial for the creditors.

ORDER

On appeal from: Western Cape Division of the High Court, Cape Town (Mantame J sitting as court of first instance):

1 The appeal is upheld with costs including costs of two counsel, where so employed.

2 The order of the high court is set aside and is substituted as follows:

'2.1 The application for an order placing the first respondent, (Normandie Restaurants Investments (Pty) Ltd) under supervision and commencing business rescue proceedings in terms of s 131(1) and (4) of the Companies Act 71 of 2008, under case no:10652/2015, is dismissed with costs.

2.2 The application for the winding-up of Normandie Restaurants Investments (Pty) Ltd, (the respondent under case no: 1997/2015), is granted and Normandie Restaurants Investments (Pty) Ltd is placed under final winding-up, with costs.'

JUDGMENT

Tshiqi JA (Lewis, Cachalia, Willis and Dambuza JJA concurring)

[1] This appeal has its origin in two related applications namely, an application by the appellant, First Rand Bank Limited (the Bank), for the final winding-up of the first respondent, Normandie Restaurants Investments (Pty) Ltd (Normandie) and an application by the second respondent, Mr Dimitri Philippou for an order placing Normandie under supervision and commencing business rescue proceedings as contemplated in Chapter 6 of the Companies Act 71 of 2008, (the Companies Act). Mr Philippou also sought an order declaring and directing, in terms of s 131(6) of the

Companies Act, that the liquidation proceedings instituted by the Bank pending under case 1997/15 – be suspended, until the court had adjudicated upon the business rescue proceedings. The Bank opposed this application. The two applications served before Mantame J in the Western Cape Division of the High Court, Cape Town (the high court). The high court granted the orders sought, dismissed the liquidation application and ordered the Bank to pay the costs of opposing the business rescue application and the costs of the liquidation application. This appeal is with the leave of this court.

[2] Normandie is a property owning company and the registered owner of Erf 46472, Rondebosch, Cape Town. Its only source of income is rental that it obtains from letting the property. Normandie's sole directors are Mr Philippou and his mother, Ms Zoe Philippou and its sole shareholder is the Zoe Philippou Family Trust, of which Mr Philippou is a trustee. Its assets comprise the property and debts owed to it, in particular, by the Zoe Philippou Family Trust, which owes it over R3 million. Its creditors, according to the draft distributions account prepared by Normandie, and attached to the application for business rescue, are:

a) The Bank, in the amount of R2,7 million;
b) The South African Receiver of Revenue (SARS), in the sum of approximately R1,6 million;
c) The City of Cape Town, in the sum of approximately R242 000;
d) An amount owed to an entity known as African Renaissance Trading Company (ARTC) in the amount of approximately R178 882; and
e) A loan account in the amount of R810 861.

[3] The property was previously let by Normandie to an entity known as Zelkar Investments 156 CC, which operated a restaurant under the name and style of Stardust. Normandie was able to meet its payment obligations to the bank from the rent it received from Stardust. Stardust's tenancy came to an end on 31 October 2013 when it moved to larger premises. From that date, Normandie experienced financial difficulties and failed to make proper payments to the Bank around March/April 2014. The dire financial state of affairs of the business is evident from unpaid debit orders from May to December 2014. This was confirmed through

correspondence between Mr Philippou and the Bank in which he requested the Bank to give him a three month moratorium on payments so that he could negotiate a new lease with another prospective tenant.

[4] It is common cause that Normandie concluded a new lease agreement with an entity known as Warthog Pub (Pty) Ltd (Warthog). However, soon after the new lease agreement was concluded, Warthog defaulted in its obligation to pay the rental. This was in part due to Warthog's difficulty in obtaining a liquor licence because the property was not zoned for commercial use.

[5] Meanwhile, Normandie's financial woes continued as its debts remained unpaid. As prefaced, the Bank, in terms of s 344*(f)* read with s 345(1)*(c)* of the Companies Act 61 of 1973 (the 1973 Act), initiated winding-up proceedings against Normandie because it was unable to pay its debts – particularly its debt to the Bank. Normandie opposed the application citing amongst other defences the fact that it had secured Warthog as a new tenant. It also indicated that its financial difficulties resulted in part from the dispute between it and Warthog. It then stated that it was in settlement negotiations with Warthog. If the dispute was settled, Warthog would pay rental in the amount of R37 500 per month. The agreement with Warthog also contained an escalation clause and an option of a ten per cent turnover rental, should the income from the trading activities exceed the base rental income. Normandie further averred that in the event that the settlement negotiations did not succeed, it had been contacted by several brokers who represented leading franchise names such as Ocean Basket and Cattle Baron, who were showing an interest in hiring the premises. It thus requested the court to exercise its discretion in favour of refusing the application for winding-up so that it could secure an alternative tenant in the hope that this would generate sufficient rental income to meet its obligations to its creditors.

[6] The Bank opposed Normandie's attempt to stave off the liquidation. In its answering affidavit it specifically denied that the rental income would be adequate to settle Normandie's indebtedness. It highlighted that the situation had worsened as a result of further arrears and interest that had since accrued, and pointed out that the

whole amount of R2,7 million was, as a result of the ongoing default, then due and payable. The Bank referred to other debts which it alleged were also due and payable to it by Normandie relating to an overdraft cheque facility, Normandie's suretyship obligation to ARTC and a further amount due by Normandie for ARTC's overdraft facility. It stated that all these amounts had been due and payable in July 2014.

[7] Before the application for the winding-up was heard, Normandie applied for a postponement and for leave to file a counter-application for business rescue proceedings. The Bank opposed the application. The court, however, postponed the Bank's application for winding-up and ordered that it be heard together with Normandie's proposed counter application for business rescue. It also granted an order joining Mr Philippou as a second respondent in those proceedings and further directed Mr Philippou to pay an amount of R490 000 into the trust account of the Bank's attorneys, apparently in part-payment of arrear instalments due to the Bank.

[8] Mr Philippou launched the business rescue application on behalf of Normandie. In essence he agreed that Normandie was in financial distress and had failed to pay amounts due and payable to its creditors but alleged that there was a reasonable prospect of rescuing it through the rental it would receive from Warthog. He attached a proposed business rescue plan compiled by potential business rescue practitioners. He also attached an addendum to the original lease agreement concluded with Warthog in terms of which the new commencement date of the lease agreement would be May 2015. In terms of the agreement the base rental would be an amount of R37 230 per month. It also contained an escalation clause and an alternative option of a ten per cent turnover rental, should the income from the trading activities exceed the base rental income. The lease would be for a period of three years with a further option to renew it for another three years. Its other terms provided that the responsibility for all repairs and maintenance of the property would be that of the tenant, including the amounts payable for municipal costs as well as rates and taxes.

[9] The Bank opposed the application for business rescue and filed an affidavit by Mr Swanepoel, a manager in its business recovery department, who contended that there were no reasonable prospects of rescuing Normandie. He referred to the fact that Normandie's indebtedness to the bank as at 23 January 2015 (being the date on which the certificates of balance attached to the founding affidavit in the winding-up application), was in the amount of R3 577 652. He attacked the proposed business rescue plan on the basis that it was incoherent, lacked particularity on how Normandie would pay the debts on a monthly basis, and, in particular, emphasised that the amount of rental from Warthog would be insufficient for payment of the monthly expenses. He also pointed out that there was in any event no prospect that the proposed business plan would be passed as contemplated in s 152(2)*(b)* of the Act, as the Bank, which is a major creditor, would vote against it. In conclusion Mr Swanepoel submitted that the application for business rescue appeared to be no more than an attempt by Mr Philippou to protect his mother's trust (the Zoe Philippou family trust) from Normandie's creditors. In this regard he referred to a loan of R1 422 589 from Normandie to the trust when Normandie was in a financial crisis. The loan was reflected in Normandie's 2011 financial statements. According to Mr Swanepoel this loan was one of the issues that needed further investigation by a liquidator.

[10] In reply, and in an apparent response to the allegation that the rental income would not be adequate for settling the monthly expenses, Mr Philippou stated that any monthly shortfall would be financed by the directors by way of post commencement finance. He also said that further monthly payments of R20 000 would be made by the Zoe Philippou family trust. He conceded, however, that this additional amount, which according to him, would be available for distribution to the creditors, was not reflected in the draft business rescue plan attached to the founding affidavit.

[11] The court a quo granted the application for business rescue finding that after the 'perfection' of the business rescue plan, '…it will meet reasonable prospects of rescuing Normandie… back to its solvency. There will be no prejudice to the affected party as according to the five year plan focus the bank will be guaranteed monthly

distributions'. The court regrettably did not give any reasons for this finding and as a result this court has no idea of what informed the decision of the court a quo. M M Corbett in his article 'Writing a Judgment' (1998) 115 *SALJ* 116 at 118 explained the importance of furnishing reasons in the following manner:

'The true test of a correct decision is when one is able to formulate convincing reasons (and reasons which convince oneself) justifying it. And there is no better discipline for a judge than writing (or giving orally) such reasons. It is only when one does so that it becomes clear whether all the necessary links in a chain of reasoning are present; whether inferences drawn from the evidence are properly drawn; whether the relevant principles of law are what you thought them to be; whether or not counsel's argument is as well founded as it appeared to be at the hearing (or the converse); and so on.'

(See also *National Director of Public Prosecutions v Naidoo & others* [2011] ZASCA 143; 2011 (1) SACR 336 paras 18-20.)

The failure by the judge a quo to furnish the reasons for its finding deprived this court as well as counsel arguing this matter of an opportunity to properly evaluate its factual and legal chain of reasoning.

[12] Turning to the provisions of the Act, s 131(4) of the Act states that a court may make an order placing a company under supervision and commencing business rescue proceedings, if it is satisfied that:

i) the company is in financial distress
ii) . . . ; or
iii) it is otherwise just and equitable to do so for financial reasons,

and there is a reasonable prospect for rescuing the company…'

[13] The parties are in agreement that Normandie was in financial distress, as envisaged by s 128(1)*(f)* of the Act, at the time the application was brought and that it had failed to pay amounts due to the Bank and the other creditors. What Mr Philippou (on behalf of Normandie) had to prove to the court in order to succeed in the application was that it was just and equitable, for financial reasons, to grant the order, and that there was a reasonable prospect for rescuing the business.

[14] A court's assessment of whether there is a reasonable prospect for rescuing a company does not entail the exercise of a narrow discretion but involves a value judgment. Where the 'discretion' exercised by the lower court was one in the loose sense of a value judgment, the limitation imposed on the authority of the court of appeal to interfere does not apply. In that event the court of appeal is both entitled, and in fact duty bound, to interfere if it would have come to a different conclusion. (See *Oakdene Square Properties (Pty) Ltd & others v Farm Bothasfontein (Kyalami) (Pty) Ltd & others* [2013] ZASCA 68; (2013) (4) SA 539 (SCA) (*Oakdene Square Properties*) para 18. See also *Newcity Group (Pty) Limited v Pellow NO (Rezidor Hotel Group South Africa (Pty) Limited First Affected and Party Non-Unionised Employees Second Affected Party)* [2014] ZASCA 162; 2014 JDR 2155 (SCA para 16.)

[15] As the Bank has submitted, a 'reasonable prospect' requires more than a prima facie case, an arguable possibility or mere suggestive speculation. It must be a prospect based on reasonable grounds. (See *Oakdene Square Properties* para 29.) In appropriate circumstances, the interests of the creditors, as opposed to those of the company or its shareholders, should carry more weight. (See *Oakdene Square Properties (Pty) Ltd & others v Farm Bothasfontein (Kyalami) (Pty) Ltd & others* 2012 (3) SA 273 (GJ) at 288G-H.)

[16] An applicant must establish reasonable grounds in accordance with the ordinary rules of pleadings in motion proceedings, ie in the founding affidavit. (See *Oakdene Square Properties* para 3.) Motion proceedings such as these are aimed at the resolution of legal issues based on common cause facts. They are not geared towards deciding factual disputes. To the extent that disputes of fact exist in the affidavits filed by the parties, the matter must be decided on the Bank's version unless it is so far-fetched, or clearly untenable that it can justifiably be rejected merely on the papers. (*Plascon-Evans Paints Ltd v Van Riebeeck Paints (Pty) Ltd* 1984 (3) SA 623 (A) at 635A-D. See also *National Director of Public Prosecutions v Zuma* [2009] ZASCA 1; 2009 (2) SA 277 (SCA) para 26.) What is more, it makes no difference to this approach that, as in this case, motion proceedings have been

dictated by the legislature. Neither does it make any difference where the legal or evidential onus lies. (See *Oakdene Square Properties* para 3.)

[17] The Bank, in its answering affidavit, illustrated convincingly why there were no reasonable prospects of rescuing Normandie. It had not been paid for over a year and Normandie's interest obligations to the Bank were, at the time, in the region of R37 000 per month comprising: R28 112,09 in respect of the loan account; R3 012,40 in respect of the overdraft account; R4 303 in respect of a loan account to ARTC; and R1 590,36 in respect of ARTC's overdraft. The amount available from the rental is R37 320 per month and the balance available after payment of the Bank's interest obligations would be a mere R320. That amount would clearly be inadequate as it would not be able to cover payment of the Bank's capital amount or any reasonable instalments flowing therefrom and would also not cover payment for SARS's admitted liability in the amount of R1,6 million.

[18] Mr Philippou has alleged that the SARS liability would be negotiated by the business rescue practitioners but there is no basis to conclude that SARS will agree to re-negotiate the debt. He has also undertaken to settle Normandie's indebtedness to the City of Cape Town personally, but has not given reasons why he had not, if he was in a position to, done so earlier. He has also undertaken to pay the fees of the business rescue practitioners personally but this does not affect Normandie's overall financial predicament.

[19] Section 128(1)*(b)* envisages that measures to be taken in order to facilitate the rehabilitation of the company should provide for *temporary* supervision, and for a *temporary* moratorium of the rights of the claimants against the company. They are not meant to provide companies with a mechanism with which to delay payments to creditors with no feasible plan of ever paying its debts, or a means of restructuring its debts over lengthy periods of time.

[20] The temporary measures envisaged by the Act are aimed at maximising the likelihood of the company continuing in existence on a solvent basis and at creating a

better return for the creditors and shareholders. As stated in *Oakdene Square Properties* (para 31):

'The development of a plan cannot be a goal in itself. It can only be the means to an end. That end, … must be either to restore the company to a solvent going concern, or at least to facilitate a better deal for creditors and shareholders than they would secure from the liquidation process.'

The measures proposed in the business rescue plan will, in my view, not provide for a temporary solution as envisaged in s 128(1)*(b)*.They do no more than plan a long-term debt management process.

[21] I am also not persuaded that the objectives envisaged in s 128(1)(b)(iii) of the Act will be attained if Normandie is placed in business rescue. As mentioned, s 128(1)(b)(iii) of the Act envisages a plan aimed at rescuing 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, and where this is not possible, to maximise return for the company's creditors or shareholders than would otherwise be the case from the immediate liquidation of the company. If the full rental were to be applied to the capital owing to the Bank, it would take Normandie approximately eight years to pay it. In the meantime interest accruing on the decreasing capital balance and the SARS debt, together with any possible penalties that may be imposed, would accumulate and remain unpaid with no plan in place on how to pay them. If only the interest due to the Bank is paid, then the full capital amount would remain outstanding and there is no indication of how and when the capital amount would be paid. The City and the Debt Restructuring Practitioners would be dependent solely on Mr Philippou's *bona fides* and his ability to pay from his own resources. Regarding the liability to SARS, Normandie's counsel submitted that the company hopes to negotiate a settlement with SARS but there is no indication that SARS will be amenable to such a compromise. The fact that SARS has not opposed the application does not in itself show that they will do so.

[22] Counsel for Normandie, when confronted with this difficulty, contended that it could be resolved through re-financing of the debt with another financier. He was,

however, unable to state that such an option has ever been pursued, could proffer no explanation as to why this was not done earlier and could obviously not state, with any confidence, that such attempts would be successful. The fundamental difficulty, of course, is that this assertion was made by counsel, from the Bar without any support for it in the papers.

[23] The other fundamental problem for Normandie is that the Bank is understandably unwilling to grant Normandie any further indulgence concerning its debts. On the contrary, Mr Swanepoel has stated that the Bank will use its position as a major creditor to vote against the adoption of the business rescue plan. To this Mr Philippou has intimated that the business rescue practitioners would have to utilise the provisions of s 153(1)*(a)*(ii) read with s 153(7) of the Act to approach the court in order to set aside the vote against the plan. In so saying he overlooks the fact that such an application is not for the asking and the company would have to prove to the court that the stance by the Bank was unreasonable. In the event that the company does not succeed in setting aside the vote against the adoption of the plan, the business rescue proceedings will come to an end. In *Oakdene Square Properties* (para 38), this court said:

'If the majority creditors declare that they will oppose any business rescue scheme… I see no reason why that proclaimed opposition should be ignored. Unless, of course, that attitude can be said to be unreasonable or mala fide. By virtue of s 132(2)*(c)*(i) read with s 152 of the Act, rejection of the proposed rescue plan by the majority of creditors will normally sound the death knell of the proceedings. It is true that such rejection can be revisited by the court in terms of s 153. But that, of course, will take time and attract further costs. Moreover the court is unlikely to interfere with the creditors' decision unless their attitude was unreasonable'

[24] I accept that in appropriate cases placing a company under supervision and in business rescue is preferable to the option of liquidation. I also align myself with the following dictum in *Koen & another v Wedgewood Village Golf & Country Estate (Pty) Ltd* 2012 (2) SA 378 (WCC) para 14, where the court stated:

'It is clear that the legislature has recognised that the liquidation of companies more frequently than not occasions significant collateral damage, both economically and socially, with the attendant destruction of wealth and livelihoods. It is obvious that it is in the public

interest that the incidence of such adverse socioeconomic consequences should be avoided where reasonably possible.'

This matter is, however, different in that there is no fear that collateral damage would eventuate if Normandie is liquidated. In effect, it owns only one asset and derives its business from the rental only. It has no employees. Placing it under business rescue will accordingly not save any jobs or livelihoods. It will not preserve any services as it does not provide any. It will not reduce the number or type of goods or products available to the public as it does not produce anything.

[25] A further concern with the proposed business rescue plan is that its viability is solely dependent on the continuity of the business relationship between Normandie and a single tenant, Warthog. If for any reason the lease between the two parties came to an end, Normandie and the Bank would be back to where they are presently. This would also be the case if, after the three year period, which is the duration of the rental agreement, Warthog decides not to exercise its pre-emptive right of renewal. Thus, the proposed business rescue plan falls woefully short of providing the information required in terms of s 150(2) and (3) of the Act and providing information on which an assessment of reasonable prospects could be made. (See *African Banking Corporation of Botswana Ltd v Kariba Furniture Manufactures (Pty) Ltd* [2015] ZASCA 69; 2015 (5) SA 192 (SCA) para 32.)

[26] There is accordingly no basis to find that there is a reasonable prospect of rescuing the business. The Bank has submitted that if this court upholds the appeal, the requisites for a winding-up have been established and that a final winding-up order should be made. I agree with the Bank that placing Normandie in liquidation is the only viable option to ensure that it pays its debts. The property will probably be sold and its proceeds will be applied for that purpose. When regard is had to the correspondence between Mr Philippou and the Bank in which he stated that the debit orders would be unpaid, and in which he requested the Bank for a three month moratorium, the inference that Normandie is commercially insolvent is inescapable. In so far as Normandie filed an unliquidated counterclaim to the winding-up application, this does not raise a dispute as to its indebtedness (See *Ter Beek v United Resources CC & another* 1997 (3) SA 315 (C) at 334A-C) and it cannot be set

off against the Bank's claim. (See *Standard Bank of South Africa Ltd v Renico Construction (Pty) Ltd* 2015 (2) SA 89 (GSJ) para 9 and *Standard Bank of South Africa v R-Bay Logistics* CC 2013 (2) SA 295 (KZD) paras 61 and 62.) The counterclaim thus has no bearing on whether an order for the winding-up should be granted or not.

[27] This then brings me to whether a provisional, as opposed to a final winding-up order should be granted. As mentioned, a company will in terms of s 344*(f)* of the 1973 Act, be liable to be wound up when it is unable to meet its debts. No useful purpose would be served by granting a provisional order. All the relevant issues have been canvassed by both parties in the papers. There are no employees who could be affected by the order, SARS issued a notice to abide, and the City, which was aware of the application elected not to participate in the matter. The matter has been going on for a long time and nothing has been done to salvage the business from its precarious financial situation. A provisional order would simply delay the inevitable, and would be prejudicial to the interests of the creditors. In the event Mr Philippou manages to devise a plan to save the business from liquidation, this can be done even after a final order has been granted.

[28] I make the following order:

1 The appeal is upheld with costs including costs of two counsel, where so employed.

2 The order of the high court is set aside and is substituted as follows:

'2.1 The application for an order placing the first respondent, (Normandie Restaurants Investments (Pty) Ltd) under supervision and commencing business rescue proceedings in terms of s 131(1) and (4) of the Companies Act 71 of 2008, under case no:10652/2015 is dismissed with costs.

2.2 The application for the winding-up of Normandie Restaurants Investments (Pty) Ltd, (the respondent under case no: 1997/2015), is granted and Normandie Restaurants Investments (Pty) Ltd is placed under final winding-up, with costs.'

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ZLL Tshiqi

Judge of Appeal

APPEARANCES

For Appellant:	J Muller SC
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	Bloemfontein
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