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*“Wisdom is the reward you get for a lifetime of listening when you'd have preferred to talk” - Doug Larson*

## **RECKLESS TRADING: A DIRECTOR'S DUTY TO COMPANIES IN FINANCIAL DISTRESS**

In the current global economic climate there has been a sharp increase in companies which have traded under insolvent or financially distressed circumstances, which more often than not has resulted in liquidation. The legislature, in an attempt to assist distressed entities and with a view of curbing the vast amount of liquidations, has accordingly introduced the concept of **business rescue** in Chapter 6 of the Companies Act, 2008 (the “Act”).

The majority of distressed entities in South Africa have however been slow to catch on with **business rescue** and have much to the detriment of shareholders and creditors continued to trade under financially distressed circumstances, which in turn poses the question of what a **Director's** duty is in such circumstances.

Section 129(7) of the **Act** provides that if the **Board** of a company has reasonable grounds to believe that the company is financially distressed, but the Board has not adopted a resolution contemplated in this section (elected not to proceed with **business rescue**), the **Board** must deliver a written notice to each affected person, setting out the criteria referred to in Section 128(1)(f) of the **Act** that are applicable to the company, and its reasons for not adopting a resolution contemplated in this section.

It could be argued that such a notice would, in a commercial sense, be the final nail in the coffin for a financially distressed company as continuing to trade thereafter would prove extremely difficult.

Failure by the **Board of Directors** of to issue a notice as provided for in the **Act** could, if the company is eventually liquidated, potentially result in the **Directors** being held personally liable for damages or losses suffered. In this regard, the **Act** provides that any person who contravenes any provision of the **Act** is liable to any other person for any loss or damage suffered by that person as a result of that contravention.

It remains to be seen whether **Directors** will ultimately be held personally liable for a contravention of Section 129(7) and **Directors** should as a precaution, remain vigilant when considering the viability of **business rescue**, the consequences for not instituting **business rescue** proceedings and the obligations imposed by the **Act** in respect thereof.

*Law & Laughter*

*“When a lawyer tells his clients he has a sliding fee schedule what he means is that after he bills you it's financially hard to get back on your feet.”*

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# BBBEEE UPDATE: ENTERPRISE AND SUPPLIER DEVELOPMENT ELEMENT

Hot on the topic of the amended BBBEEE codes, our previous article focused on the Ownership Element. In this article, attention is directed to the Enterprise and Supplier Development element (“**ESD**”), the second of the three priority elements.

With this element, we see the merging of the Preferential Procurement and Enterprise Development elements in the previous BBBEE codes. **ESD** carries the heaviest weighting of all 5 elements with a total of 40 points of the 105 points, making it the single most important element.

The **ESD** scorecard is based on Statement 400 of the codes of good practice. **ESD** consists of three sub-elements, each with its own weighting points. These elements are **Preferential Procurement** (25 points and 2 bonus points), **Supplier Development** (10 points) and **Enterprise Development** (5 points with 2 bonus points).

A measured entity is required to spend 2% of their net profit after tax annually on **Supplier Development** and a further 1% of the net profit after tax on **Enterprise Development**. The beneficiaries for both are EMEs or QSEs that are at least 51% black owned. However, for *Supplier Development* the beneficiary must be a supplier of goods/services and for **Enterprise Development** the beneficiary must not be a supplier of goods/services. Therefore, the same beneficiary can't be used for both these elements.

**Preferential Procurement** points may be obtained if goods/service are obtained at an **Empowering Supplier** which is accompany that is BBBEE compliant, a “good South African citizen” and complies with at least one (QSEs) or three (Large Enterprises) of the following pre-requisites:

- \* ≥ 25% of cost of sales (excluding labour and depreciation) must be sourced from local suppliers/producers;
- \* 50% of jobs created within the company are for black individuals (subject to no change in the number of black employees from the previous BBEE verification).
- \* ≥ 25% transformation of raw materials/beneficiation
- \* Spend 12 days per annum on skilling a black EME or QSE to increase their operation or financial capacity.

Since **ESD** is a priority element a 40% compliance with each of the sub-elements has to be achieved. Companies should thus seek legal assistance to ensure proper compliance.

## Contact Van Huyssteens

T +27 12 349 2306  
F +086 6151 183

## Address:

De Haviland Crescent Nr. 5,  
III Villaggio Nr.12, Torino Suite  
Persequor Park  
Pretoria, South Africa

## Van Huyssteens appreciates your feedback:

For information or editorial contributions, please e-mail: [commercial@vanhuyssteens.co.za](mailto:commercial@vanhuyssteens.co.za).

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