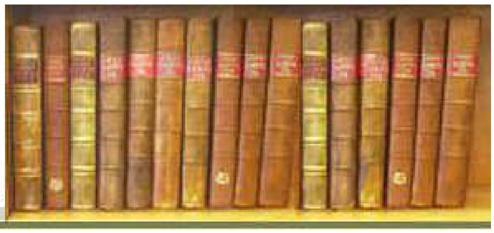
SAJESBM
The Southern African Journal of Entrepreneurship and Small Business Management



www.sajesbm.com

Constraints on decision making regarding post-commencement finance in business rescue

Marius PRETORIUS*
Department of Business Management
University of Pretoria, South Africa

Wanya DU PREEZ
Gordon Institute of Business Science
University of Pretoria, South Africa

* Corresponding author
Department of Business Management
University of Pretoria, 0002
South Africa
marius.pretorius@up.ac.za

ABSTRACT

Since its introduction, business rescue has become a critical consideration in business strategy decision making. One of the critical components of business rescue, which appears largely unsuccessful to date, involves securing post-commencement finance (PCF) to restore the company's financial health. Despite extensive theory in the literature on failure, there is a void regarding post-commencement finance. Specialist practitioners and financiers with extensive experience in rescue and turnaround were interviewed in this study. Findings showed that many critical factors and reasons for lack of interest are due to the newness of the South African Companies Act 71 of 2008 (introduced May 2011). These include business rescue filing being left too late; the poor financial state of the business that files for rescue; and the significant impact on the outcome by some of the key players (especially the financiers and business rescue practitioners). Better understanding of this aspect would be beneficial for creditors, rescue practitioners, shareholders, government regulators, court officials and educators alike.

Key words: business rescue, post-commencement finance, turnaround, decision making.

INTRODUCTION

According to a Chinese proverb, “When you fall into a pit, you either die or get out”. For businesses in rescue, “not dying” often depends on post-commencement finance (PCF), as this often defines the possibility of “getting out”.

Financial distress is the trigger, the measure and the result of a business in need of a rescue. When businesses become “over-leveraged” or financially distressed, for reasons within or beyond their control, access to finance becomes increasingly difficult; if not virtually impossible. The difficulty of accessing PCF forces distressed businesses to operate on a cash basis or confront the possibility of liquidation or forced sale of their assets. This has been evidenced in the recent financial crisis, where the raising of post-commencement finance/post-petition finance has become a major obstacle for businesses that require rescue or reorganisation (Vriesendorp & Gramatikov, 2010). Therefore, financing is a critical component of the success of business rescue, and is of the utmost importance in the turnaround attempt.

The number of liquidations and insolvencies is an important barometer of the general health and fortunes of businesses in the country. In South Africa, the total number of firms that have been liquidated/declared insolvent increased from 3225/1642 respectively in 2005 to 3992/4020 in 2010, which represents a respective increase of 23% and 144% (Statistics South Africa, 2012) over a period of five years. The considerable increase in liquidations over the past few years confirms a growing trend of financial distress among South African companies.

International Insolvency reform over the past 20 years; supported by policy makers, politicians and practitioners; has focused mainly on corporate rescue, through the development of legislation focused on business reorganisation (Vriesendorp & Gramatikov, 2010). This was first seen in countries such as the United States (US) (Chapter 11 of the Bankruptcy Code, 1978) and the United Kingdom (UK) (Cork, 1982), which were leading the way by establishing corporate rescue regimes in their respective countries. As a result of this, countries such as Canada have followed the US, and Commonwealth countries such as Australia have developed their own rescue legislation to support businesses in distress, and to regulate the claims of creditors in these situations. Today almost all modern democracies have established statutory corporate rescue procedures with the purpose of providing protection for insolvent (financially distressed) businesses and potentially afford distressed companies a ‘second chance’. Today, it seems increasingly important for a business to obtain turnaround finance at the beginning of the process of financial distress, as this is directly linked to the likelihood of success of the turnaround.

This paper starts by exploring the relevant legislation and defining the concept of post-commencement financing. Secondly, it links PCF to different regimes internationally as guidelines. Thirdly, it explains the qualitative research design. Fourthly, it reports the findings, tracking substantiation and insights from the subjects to supplement the theory and literature. Finally, we draw conclusions and propose a framework for PCF with recommendations for policy guidelines.

THE SOUTH AFRICAN CASE

South Africa introduced the new South African Companies Act 71 of 2008 (Republic of South Africa, 2008), which came into effect in May 2011. It contains Chapter 6: “Business rescue and compromise with creditors” (Republic of South Africa, 2008). This chapter effectively replaced the judicial management procedures from the Companies Act of 1973, perceived as a failed regime. The aim and purpose of the new chapter is to provide companies in financial distress with an opportunity to reorganise and restructure, and therefore maximise their chances of continuing to trade.

According to Lotheringen (2013: pers com), in the first 28 months since the introduction of the new rescue legislation, 1202 businesses opted for the route of business rescue instead of liquidation. Furthermore, a projected 5300 jobs have been saved through successful business rescue proceedings (CIPC, 2013). At present, however, it is not possible to determine the number of jobs associated with unsuccessful business-rescue proceedings (implied ending in liquidation)

In any rescue regime, a degree of financial support is required from the commercial environment through the provision of additional funding and agreement by existing creditors to postpone or compromise their claims. Ironically, when rescue is most needed, businesses struggle to obtain additional credit, or the creditors themselves are financially stressed (Vriesendorp & Gramatikov, 2010). Therefore one of the critical components of the business rescue plan involves securing turnaround finance to meet short-term trade obligations (such as working capital requirements), covering turnaround/restructuring costs, and restoring the company's balance sheet to solvency.

Recent research suggests that the lack PCF is one of the five main reasons why business rescues in South Africa have failed (Pretorius, 2012). Obtaining turnaround finance and returning the business to liquidity presents a challenge for financially distressed organisations, and therefore the first port of call is normally internal funds (assets or 'slack' of various nature) which are mostly non-existent. Distressed organisations in South Africa also seem to have experienced increased difficulty in attracting turnaround finance in the form of loan capital and private equity capital. Thus inability to obtain the necessary funding may contribute to the ultimate demise of their turnaround prospects. It may even be the main contributor to the turnaround process.

The importance of PCF in business rescue is substantiated by the act, which enhances the preferential priority of PCF. Section 135 of Chapter 6 of the Companies Act No. 71, 2008 provides for PCF, which ranks in preference above existing unsecured claims against the debtor company (Republic of South Africa, 2008). The ranking of PCF is an attempt by the legislators to stimulate turnaround financing for these distressed businesses. A similar concept is prevalent in the equivalent US Chapter 11 provisions, which provide for debtor-in-possession (DIP) financing.

Pelser (2012) has stated that one of the largest stumbling blocks for the new regime is the inability to secure capital. Initial exploration of a sample of business rescue plans (Pretorius, 2012) suggests low levels of post-commencement financing, and therefore the status quo needs to be investigated and compared with best practice for international standards.

Post-commencement financing

Fundamentally, securing financing is essential to a successful business turnaround. A key requirement that need to be expanded on in the rescue plan is the magnitude and nature of the financing required to rescue the business, which is referred to as post-commencement finance. The definition of post-commencement financing is expressed as follows in the Companies Act 71 of 2008, Chapter 6, Section 135 (Republic of South Africa, 2008:240):

> (1) To the extent that any remuneration, reimbursement for expenses or other amount of money relating to employment becomes due and payable by a company to an employee during the company's business rescue proceedings, but is not paid to the employee, the money is regarded to be **post-commencement financing**; AND
>
> (2) During its business rescue proceedings, the company may obtain **financing other than as contemplated is subsection (1)**, and any

> such financing – (a) may be secured to the lender by utilising any asset of the company to the extent that it is not otherwise encumbered; and (b) will be paid in the order of preference set out in subsection (3)(b).
>
> (3) After payment of the practitioner's remuneration and costs referred to in section 143, and other claims arising out of the costs of the business rescue proceedings, all claims contemplated in subsection (1) will be treated equally, but will have preference over all claims contemplated in subsection (2), irrespective whether or not they are secured; and all unsecured claims against the company; or in subsection (2) will have preference in the order in which they were incurred over all unsecured claims against the company.
>
> (4) If business rescue proceedings are superseded by a liquidation order, the preference conferred in terms of this section will remain in force, except to the extent of any claims arising out of the costs of liquidation.

It can be deduced that unpaid claims by employees related to employment or reimbursements of expenses during the rescue process are considered PCF, which carries a super-priority status in the act. Furthermore, the ranking of claims in terms of the Section 135 provisions is as follows (Republic of South Africa, 2008):

1. The business rescue practitioner's remuneration and costs (as per section 143) arising from business rescue proceedings (section 135(3)); then
2. All other claims from costs of business rescue proceedings; then
3. All PCF claims related to employment once business rescue has commenced; then
4. Secured lenders/creditors pre-business rescue; then
5. All secured PCF claims related to third-party lenders/creditors (section 135(3)(a)(i)); then
6. Insolvency Act preferences; then
7. Unsecured claims by PCF or lenders/creditors during business rescue in the order in which they were incurred (section 135(3)(b)); then
8. Remuneration of employees which became due and payable before business rescue commenced (section 144(2)); and then
9. All unsecured claims against the company.

Recent case law has sought to clarify the position of secured creditors through the judgement handed down by Judge Kgomo in the South Gauteng High Court on 10 May 2013. The case of Merchant West Working Capital Solutions (Proprietary) Limited v. Advanced Technologies & Engineering Company (Proprietary) Limited & Gainsford states clearly that the claim of secured creditors who advanced funds prior to the start of business rescue now ranks after the claims of post-commencement financiers (secured and unsecured). This may be an encouraging development for the distressed investing industry. This judgment is under review.

This study aims to better understand the apparent absence of post-commencement finance for business rescue in South African companies, as opposed to the findings of international research, where post-commencement finance is actively raised. The above motivation leads to a crucial research problem, which this research attempts to answer, namely: What is the status (i.e. nature and extent) of post-commencement finance in South Africa? More specifically, questions that need to be answered through this research include:

1) What are the types and sources of financing required for a business that has filed for business rescue?
2) What are the critical success factors for advancement of financing by the creditors/lenders?
3) What are the reasons for lenders' lack of interest in financing businesses which have filed for business rescue?

The research was designed to identify and report perceptions of subjects about PCF to gain insight into the causes associated with the apparent lack of such funding.

International guidelines on post-commencement finance

Business decline is a normal part of business, generally negatively perceived by affected parties and firms; this is partly why this legislation that supports debtor concerns has been instituted. Often affected parties involved in rescue understand neither the complexity of business decline (Pretorius, 2009), nor the various reasons that have been suggested for failure, with their many signs indicating the different causes. These include diminishing resources, poor management, strategic issues, operational issues and combinations thereof. The many variables that determine how business failure occurs influence the decision making of the rescue process.

Scientific literature on rescue from developing countries such as South Africa is almost non-existent (Pretorius & Holtzhauzen, 2013:469) compared with that from the US, UK, Australia and Canada. Understandably, rescue practitioners protect their strategies as "intellectual property", as they represent their competitive advantage. The international literature incorporated in this study involved all scientific resources from ABI-Inform, Ebsco-host, Proquest, ScienceDirect, Blackwell and other databases for titles published.

POST-COMMENCEMENT FINANCE THEORY/LITERATURE REVIEW

Various country regimes associated with their approaches to PCF are described in Table 1. It is necessary to look at the contextual differences to better understand how the key issues are addressed by each regime.

Table 1: Comparison of PCF related rescue issues in the US, UK, Canada, Australia and South Africa

	USA	UK	CAN	AUS	RSA
Philosophy	Debtor friendly	Creditor friendly	Debtor friendly	Debtor friendly	Debtor friendly

Approach	"Chapter 11" Very sophisticated and evolved industry (lots of case law) Prescriptive process and predictable Upfront consultative process Mature distressed investing market Strictly court driven with specialist solvency/rescue courts and specialised judges	"Company Voluntary Arrangement" Viability assessment done upfront before filing Laws and practice well settled and institutionalised High level of certainty Mature distressed investing market Strictly court driven with specialist solvency/ rescue courts and specialised judges	Similar to UK and US	"Deed of Company Arrangement" Consultative process with total consensus upfront (incl. PCF) Personal financial commitment from Administrator Strictly court driven with specialist solvency/ rescue courts and specialised judges	
Official	Turnaround CEO (Trustee) Not a practitioner, but rather part of management (fiduciary obligation)	Administrator (similar to liquidator) Does not take over running of business	Monitor (not a practitioner) – also trustee	Administrator (also liquidator)	Business rescue practitioner
Rescue culture	Debtor friendly (company is in possession) Management have power and responsibility to keep business afloat Extremely transparent and robust process Parties support and embrace the process, positive with little reputational damage	Creditor friendly and large-bank driven – Banks play a major role in influencing and leading rescue (can remove Administrator)	-No specific mention	Formalised effective court-driven process Personal financial accountability of Administrator High levels of commitment and certainty	

Concept of PCF exists?	Yes, referred to as DIP Financing	No specific mention	Informally adopted DIP Financing with application of Balances of Prejudices Test	No specific mention	Yes
PCF Priority	Super-priority status after secured claims	N/A	Super-priority status ahead of other creditors including pre-filing bank lenders	N/A	Preferential ranking after BRP's remuneration and costs, and costs of BRP proceedings
PCF	DIP Financing (through the court) Super-priority status Pre-packaged finance agreed upfront prior to filing (collateral required) Process is well established, standardised, formalised, prescriptive and sophisticated Specialised DIP Financing firms	Financing agreed upfront No formalised concept such a PCF No priority status (rare that other creditors rank ahead of bank) Secured creditors do not have voting rights as already secured	Super-priority status Secured creditors have voting rights Similar rankings to USA	PCF Agreed upfront Super-priority status Trade Creditors are majority of debt holders Secured creditors have voting rights	Focus of this research

Source: Based on Du Preez (2012)

What post-commencement finance typically entails

Du Preez (2012) has reported that the typical financiers of PCF are banks, creditors and the shareholders. Most of these parties would want to investigate the company to establish whether they believe in its viability and whether they want to provide the business with another chance of survival. For financiers, the nature and extent of PCF mostly depends on the type of business and its current financial situation, and what the risk appetite of the lender is. Typical providers are the following:

- Banks

The traditional bank is the best-known lending institution. Banks are generally conservative lenders who price for high risk. It is highly unusual for banks to take an equity stake in a business, as that is not their core mandate. Banks historically do not have specialist rescue units or a separate business rescue product, as business rescue is not their core focus; therefore all these cases are dealt with as part of their normal credit processes. Recently banks have started address this discrepancy.

- Trade creditors

The second potential type of financier is trade creditors or suppliers of a business. Often trade creditors continue to supply on revised terms (e.g. cash on delivery) if they see the long-term potential/benefit of the business relationship (or if they might be crippled by the loss of this client). Sometimes trade creditors supply credit in order to retrieve as much of their money as possible from the process. Trade creditors are ideal for certain short-term working capital needs. In some cases, where the company in business rescue is a strategic partner or key competitor, the trade creditors may take equity in the business or buy the whole business in order to obtain a strategic asset or access to a customer base through a debt-equity swop.

- Customers

Customers are a source that is often overlooked; however, this depends on the type of business. Again, the customers might like the product so much that they are prepared to put in some financing, or they may need the product as it is crucial for their business (Du Preez, 2012).

- Shareholders

Shareholders can act as a potential financier of PCF, particularly if they are also serving in management/directorship positions (for example in owner-managed businesses). However, the tendency of directors to file too late for rescue drastically reduces shareholders' appetite to advance funding. This is even more challenging in the case of a public company, due to the sheer number of shareholders that need to be considered and affected parties to be managed.

- Development Finance Institutions

Due to the nature of the mandate and key strategic objectives of a Development Finance Institution, such institutions as the Industrial Development Corporation (IDC) and the Development Bank of South Africa (DBSA) are ideal candidates to advance PCF in rescue situations. They often become involved where there is a broader developmental or social agenda at stake. However, what inhibits these organisations from being effective in this case is the time that they currently take to authorise the provision of financing, and the level of bureaucracy built into their internal processes. This limits the freedom and agility that the BRP requires as part of the role.

- Alternative financiers: distressed lenders and private equity firms

The last major category (Du Preez, 2012) of financiers is broadly referred to as "alternative financiers" and includes organisations such as private equity (PE) firms, venture capital (VC) firms and distressed lenders (DL).

The future of PCF might lie with these firms, as the traditional financiers do not currently display a sufficient appetite for PCF. These entities generally have a higher risk appetite. Such entities would typically buy out distressed debt and/or have PE/VC funds available to utilise for this purpose. The potential incentive for them to enter this industry is the higher risk-return investment, buying debt or assets at depressed prices, higher payment priority in terms of the PCF rankings, and potential debt-to-equity swaps in cases where they have identified a viable business with long-term prospects.

Du Preez (2012) has reported that the presence of distressed lenders in South Africa is either non-existent or unknown, and few products have been designed to accommodate the high level of risk associated with this type of financing. Therefore BRPs and management do not currently have ready access to this financing option. However, interest in the field is growing as investors become more comfortable with the concept and the risks involved.

Some PE funds have been in discussions about establishing distressed funds, but so far none have been forthcoming.

Typical problems associated with PCF

As the new business rescue regulations came into effect only in May 2011, it is too early to evaluate the impact and effectiveness of post-commencement finance. Traditional funding options (particularly loan funding) for distressed businesses are limited, because existing lenders are attempting to manage their existing risk exposure and do not want to risk more than they have already invested. Existing lenders wants to mitigate their risk exposure by reducing rather expanding the exposure. Furthermore, if additional funds were advanced, the traditional lenders would require unencumbered assets or surety, which are often not available to a business once it has moved into financial distress.

With the advent of the regulations around PCF, new options for obtaining new investment and distressed funding have been released. A significant consideration for any investor is to receive a return on the investment; therefore opportunities for private equity firms to intervene are pronounced. However, the private equity market in South Africa is very small and underdeveloped and needs to be supported in terms of creating and stimulating demand for distressed debt.

As can be concluded from the above review and because the implementation of the Companies Act in South Africa is so recent, there is little or no literature available on PCF, and therefore little guidance on its current extent. Identifying key prerequisites for PCF is therefore critical in order to increase its occurrence.

RESEARCH DESIGN

Research approach

The research approach was exploratory and qualitative in nature, aimed at improved understanding of the status of PCF. It aimed to identify and explain the embedded knowledge and experience of specialist rescue practitioners and specialists who had been involved in many informal turnarounds and rescues as bank officials.

As noted in the literature review, the theory base for post-commencement financing (and international equivalents) has emerged from a developed-world paradigm, and little research has been done in a South African or similar developing market, due to the short time since the adoption of the legislation. A qualitative, largely exploratory approach was therefore considered most appropriate for this research study, given that the study aimed to help to build theory related to post-commencement financing in distressed businesses that operate in a South African context.

A process of deduction was used to test theoretical propositions, and a research strategy designed to do this was utilised (Saunders & Lewis, 2012). The propositions (set out in Table 2 and following text) provided a conceptual framework and guided data collection and analysis. The research sought support (or lack of support) in the results that emerged from the data, leading to conclusions. Content, narrative and comparative analysis was then utilised to draw conclusions.

Research process

The research study took the form of a two-phase qualitative study, in which a thorough review of the literature culminated in propositions which were tested.

Phase One involved a detailed review of the turnaround literature to build an understanding of concepts relating to the study and to provide justification for the research topic.

Specifically, the following data was sourced: international best practice for post-commencement finance; the different phases of financing required; the related success factors; and reasons for lenders' lack of interest in financing distressed businesses. The results were used to formulate initial propositions, which were then tested through semi-structured interviews. The propositions informed the interview protocol used for data collection, and were used to guide analysis.

The following inclusion criteria for literature sources were applied: mention of PCF or distress funding; explanations of different country regimes and requirements for granting PCF. As for major seminal works, the date was not seen as a limitation, especially when an article was referenced widely; relevance and contribution to the body of knowledge on post-commencement finance was paramount. Each article was scrutinised for confirmation of concepts, as well as additional concepts and variances under different conditions and contexts, especially regimes. When analysed, this research identified key concepts using grounded theory research.

Phase Two involved a series of face-to-face semi-structured expert interviews with 18 experts in the field of business rescue, in order to explore the propositions submitted. The reasoning the research used was mostly inductive, to explore the subjects' understanding, experience, interpretation and knowledge building for the different experiences they reported on.

Key scientific beliefs of researchers

In attempting to answer these questions, the researchers were aware of their own methodological values, beliefs and philosophical assumptions. These assumptions could influence how they conducted the research; they stated them in order to understand the 'intellectual climate' in which they conducted the research.

Ontological positions

These comprise the researchers' views on the very nature and essence of research. Researcher A is an objective realist who believes that knowledge arises from facts associated with the cases and the context. If the researcher found repeated mention of applications, preconditions, causes and responses, he could "generalise" them. His interest was mainly in business strategy during decline.

Researcher B is a constructionist practitioner who believes that situations can be explained, especially when one has participated in their processes. People's views, actions, reactions, interactions, social relations, social and cultural practices, rules and values reflect the experiences that guide their decision making. Therefore, understanding such subjective experiences and interpretations may uncover unknown relationships and lead to improved insights into the experience of BRPs. Her interest was mainly in business principles applicable to the turnaround and rescue situations.

The personal experiences of the subjects and their views on the different questions and problem statements were interesting to the researchers. The specialists shared their experiences willingly and responded openly to all the questions the researchers asked during the interviews.

Epistemological positions

The theory of knowledge (epistemology) of the researchers diverged to some extent. This allowed for interplay on how much can be concluded about social phenomena and how knowledge can be demonstrated.

Researcher A worked primarily from a scientific paradigm and secondarily from a consultant paradigm. He had had experience of rescues and business failures himself. He had worked as an academic and also as a strategy and turnaround consultant. This influenced his search for factual directives, patterns and answers in order to correct future situations of a similar nature.

Researcher B worked from a business-rescue practice paradigm and looked for a description of this relevant issue as part of her master's dissertation.

Thus, both authors were subject to their own biases and therefore chose structured data-gathering methods.

Research method

The detailed methodology is described as follows:

Research setting

Eighteen industry specialists with practical experience were purposively selected to participate in this study through interviews. Interviews, times and venues were arranged to conveniently suit the subjects. Subjects were reassured that there would be total anonymity and that the results would only be used for the research project. Subjects participated voluntarily. It was found that they were relaxed when answering the questions, since these were based on their field of expertise. It is believed that these positive interview conditions led to unbiased sharing and meaningful conclusions drawn from the discussions of their perceptions and experience.

Sampling

Respondents were identified through the researchers' own contacts and purposively selected based on accessibility and perceived experience of subjects. The criteria used to select subjects purposively from the population were based on the following qualifiers:

Business rescue practitioners:

- They had all been involved, directly or indirectly (formally or informally) in turning around a distressed organisation or business unit (having led, or been a member of, a turnaround team).
- They had extensive rescue experience, having worked in a business venture for more than three years, long enough to fully appreciate the dynamics and see the interactions and results of such turnarounds.
- They were well seasoned and generally experienced business people, as the research aimed to extract knowledge and wisdom from the "grey hair" of industry.
- They were each licensed as a Senior Business Rescue Practitioner by CIPC (Companies and Intellectual Property Commission).

Members of financing institutions

- They all had senior corporate rescue experience.
- They had senior decision-making power in the organisation – mainly banking.
- They had all been involved, directly or indirectly (formally or informally) in turning around a distressed organisation or business unit.
- They were well seasoned and generally experienced business people.

The researchers approached the subjects individually, requesting their participation. The experts (subjects) met all the above criteria, having driven turnaround situations in their past and present work situations, and being recognised by reputation in the industry.

Saturation was observed and the sample size was deemed to be more than sufficient, based on the benchmark of six to twelve interviews being the ideal sample size for qualitative research (Guest, Bunce & Johnson, 2006).

Data collection methods

The methods are described according to the process followed.

Interview protocol

The interview protocol design was based on information gathered from the literature review and the propositions developed from this. The final interview guide posed six broad questions, all of which were open-ended, and they were then followed up by more detailed questions. Table 2 shows how each of the questions related to the individual propositions.

Table 2: How the research interview questions related to the propositions

Propositions	Questions
Proposition #1: Internationally there are clear directives for post-commencement finance.	What are the key directives internationally around post-commencement finance?
Proposition #2: Post-commencement finance for business rescue in South Africa is almost non-existent.	In your experience, what is the current nature and extent of post-commencement finance for business rescue in South Africa?
Proposition #3: Post-commencement finance varies over clear phases.	What are the different phases of post-commencement finance that a business in distress needs?
Proposition #4: Prerequisites for successful post-commencement finance can be identified.	Are there known prerequisites for successful post-commencement finance that you have obtained through your experience? If so, what are they?
Proposition #5: The reasons for lenders' (venture capitalists, banks, other institutions) lack of interest in post-commencement finance are clear.	What would you describe as the reasons for lenders' (banks, private equity firms, other institutions etc.) lack of interest in post-commencement finance?

Data collection

Semi-structured interviews were used for the data collection in Phase Two of the study. Each interview lasted for approximately 60 to 90 minutes. All interviews were recorded on a voice recorder, and the recordings were later transcribed into written documents. Each transcription took an average of four hours to complete and a further four hours to analyse.

Data analysis

Though there was only one key source of evidence (the subjects), the researchers used "investigator triangulation" (Yin, 2003:98) to extract as much richness as possible. From the many views expressed, specifically the subjects' own version of their experiences, insights and interpretations, the researchers identified and recorded aspects relevant to the research propositions using in-depth interview notes, evaluating and checking the researcher interpretations. A combination of content and narrative analysis was used to test and refine the theory-based propositions (Yin, 2003).

The interview transcripts were organised around themes emerging from the interviews. Content analysis was used to analyse the data collected from the interviews (Leedy &

Ormrod, 2001). In line with Marshall and Rossman (2006), the researchers identified salient themes, recurring ideas or language, patterns of belief that linked people and settings together, and categories/themes into which segments of text were placed.

A qualitative data-analysis tool called Atlas.ti Data Analysis Software version 7.0 was used to organise, code, label and analyse the data into logical categories/constructs and themes and to index the different pieces of data for easy retrieval.

Strategies used to ensure quality data

The researchers checked quality as the interviews progressed. Here they asked the subjects, as the key informants, to judge the researchers' interpretations of the different issues. As the focus of this study was mainly explanatory, the interview process focused on how things were perceived as the specialists described them, thus using "explanation building" to improve internal validity (Yin, 2003:34).

FINDINGS

The first research objective was to describe the nature and extent of PCF in South Africa, to lead to the identification of key drivers and inhibitors of PCF. The second research objective was to provide reasons for the current extent of PCF in South Africa. The findings are discussed based on the propositions set.

Findings linked to Proposition 1: Internationally there are clear directives for post-commencement finance

The detailed analysis of responses by the specialist subjects yielded some salient results pertaining to their thinking about PCF and its impact on business rescue. During the interviews, it became clear that the BRPs and the financiers held some similar views, but with varying denotations and terminology. Instances where the outlook on approaches was similar were therefore grouped in the relevant categories. However, there were also very starkly contrasting opinions, which have been outlined in the results.

Firstly, clear directives for PCF can be identified internationally, and used as a yardstick for best-practice principles on distressed financing in South Africa. Results from the expert interviews revealed that key international prescriptions can be identified across the four jurisdictions analysed.

Secondly, the super-priority status of PCF, an upfront consultative process with all stakeholders (including an agreement on pre-packaged finance prior to filing) and the strictly court-driven process with highly specialised court judges were cited most frequently by subjects as the most common directives for PCF. Interestingly, 13 of the 18 subjects reported directives from the US corporate rescue regime. This is probably because Chapter 11 is the best-known and most successful rescue system internationally. Eight BRPs and seven financiers mentioned practices in Australia, while the UK and Canadian regulations were the least known.

The subjects identified a number of best-practice considerations for PCF locally. The consultative nature of the processes, the early engagement with key stakeholders and the super-priority status of PCF were cited many times, and were therefore identified as the main international prerequisites for PCF.

The specific rescue culture of a country was also deemed important, impacting on the nature of rescue proceedings and the dealings among the different parties involved.

Based on the above, the research found support for the proposition that clear international directives for PCF could be identified.

Findings linked to Proposition 2: Post-commencement finance for business rescue in South Africa is almost non-existent.

Most subjects stated that the current extent of PCF in SA is small to non-existent. This is a concern, as the ability to successfully raise PCF has a major influence on the overall successful outcome of a business rescue, stressed by seven BRPs and four financiers. Upon further enquiry as to the reasons for the low levels of PCF in South Africa, the subjects shared the reasons detailed in Table 3. These are reported for the two groups of subjects, including how many subjects cited each one.

Table 3: Reasons for the apparent current non-existence of PCF in South Africa

Ranking		Mentioned by # BRPs	Mentioned by # FINs
1st	**Newness of legislation**: Lack of understanding of business rescue legislation; do not want to take a risk on the "unknown". Processes not clear, many loopholes and inefficiencies.	4	3
2nd	**Lack of case law and legal precedents**: creates uncertainty and is expensive to test.	6	4
3rd	**Negative role of the banks:** Powerful role of banks in business rescue – sway proceedings in their favour due to majority vote.	2	-
	Banks use loan documentation inappropriately – state that you are in breach if you file for business rescue; you have to consult with them first before filing (contra to Act).	2	
	Banks are uncompromising and unreasonable during PCF negotiations as they already have security, don't want to take a loss.	1	
4th	**Companies are incorrectly filing for BR**: wrong reasons, wrong size, receiving wrong advice, poor timing.	3	
5th	Poor quality rescue plans.	3	-
6th	**Abuse of the system**: Companies are deliberately filing for BR as delaying tactic to buy time, ulterior motives. Erodes trust of financiers (related to factor 4 above)	-	3
7th	Viability of business is poor	-	1
8th	**Lack of security** and available unencumbered assets	-	1

[Note: BRP = Business Rescue Practitioners; FIN = Financiers]

The main reasons for the lack of PCF shared by most subjects therefore centre mainly on the fact that the legislation is still very new, ill understood and incorrectly applied in practice, as well as the lack of case law to interpret the act, and incorrect filings due to the wrong interpretation of the law. In addition, the powerful influence of the banks, and their lack of cooperation in the process, has a negative impact on the outcome of PCF negotiations.

Subjects reported that in the few instances when PCF is advanced, they have observed in what format or shape it is provided, as well as who the typical financiers are. Uncertainties were raised regarding the definition and interpretation of what constitutes PCF, including lack of clarity on the definition of insolvency. It is critical that such uncertainty be clarified in order to provide potential financiers with the confidence that their funding will be recognised as a higher priority debt and the certainty that it will be repaid.

It can therefore be concluded that support was found for Proposition 2, i.e. that the current extent of PCF in South Africa is almost non-existent.

Findings linked to Proposition 3: Post-commencement finance varies over clear phases

The general response to this question from BRPs and financiers alike was that the different phases would be determined by, and detailed in, the business rescue plan itself, therefore it would include all financing required, from filing (day one of business rescue) until the closure of rescue proceedings. It would also be further affected by the particular context of the business itself, and the product or service that it provides.

Currently there is a perceived high risk for a lender advancing financing in the period immediately after filing but before approval of the plan. The probable reason for this is that should the plan not be approved, there is no clarity about whether this loan would constitute PCF and whether the lender would be repaid. Although this appears incorrect in terms of the definition of PCF in the act, the view of certain of the financiers reinforces this perception.

Table 4 lists the three key phases of PCF that were identified during the interviews, and the period covered by each phase. It was noted that each phase might be financed by a different lender.

Support for Proposition 3 was therefore found that PCF varies over clear phases.

Table 4: Key phases of PCF identified by subjects

Phase #	Phase Name	Period
1	Critical and Emergency Funding	Immediately post-filing to first meeting with creditors – associated with working capital to keep the business operating
2	Pre-Plan Funding	After Phase 1 funding has been stabilised to pre-rescue plan approval
3	Post Plan Exit Funding	After rescue plan until business has come out of financial distress

Findings linked to Proposition 4: Prerequisites for successful post-commencement finance can be identified

During the interviews a range of prerequisites for success were shared by both financiers and BRPs. There were many correspondences between the two groups of subjects; however, there were also numerous items identified that were unique to a particular group. These differences have been emphasised in Table 5, which lists the seven key directives that were identified, the number of times the item was mentioned during interviews, and how many subjects cited each prerequisite. Ranking was arbitrarily based on the number of mentions.

Table 5: Prerequisites for successful PCF identified by subjects

Ranking	Prerequisites for success (number of mentions)	Mentioned by # BRPs	Mentioned by # FINs
1	The availability of security (34)	8	6
2	Positive impact of the profile and actions of the business rescue practitioner (32)	6	7
3	A sustainable plan based on a viable business (30)	9	6
4	Distressed businesses involving and engaging financiers upfront, prior to filing for business rescue (22)	6	3
5	Earlier filing for business rescue by distressed businesses (15)	6	3
6	Good relationship of financier with management and the BRP: trust, openness and transparency (8)	4	6
7	Existence of another financial backer/potential buyer (7)	2	3
	Other considerations: The risk of losing more if they do not provide funding; the need to protect or preserve their existing security; the need for the value and commercial viability of additional financing to be visible; and certainty of being repaid.	-	-

As can be seen from Table 5, fourteen of the subjects felt that the most important criterion for success was having sufficient security available while a further 13 subjects felt that the role of the BRP had an immense impact on the ability to successfully raise PCF. Lastly, 15 subjects stated that a critical success factor was the existence of a viable business case (model), supported by a sustainable rescue plan.

Thus support was found for Proposition 4: Prerequisites for successful post-commencement finance can be identified.

Findings linked to Proposition 5: The reasons for lenders' lack of interest in post-commencement finance are clear.

The response to this proposition was the most voluminous and comprehensive of all the questions posed to subjects. The reasons for the failure in the quest for PCF also invoked the most passion and frustration by subjects. Table 6 lists 11 reasons for the apparent lack of interest of lenders in PCF, the number of times each was mentioned, and how many subjects from each group cited each reason.

Table 6: Reasons for lack of interest in PCF by lenders as identified by subjects

Ranking	Reasons for lack of interest (number of mentions)	Mentioned by # BRPs	Mentioned by # FINs
1st	Negative impact of the profile and actions of the business rescue practitioner (51) *	7	6
2nd	Business rescue filing by distressed businesses for wrong purpose and too late (46) *	7	6
3rd	Inadequate business rescue culture and perceptions of business rescue in South Africa (45)	8	5
4th	Concerns and uncertainty regarding the priority ranking of PCF (38)	6	4

5th	Banks being conservative and risk-averse due to regulations such as Basel (23)	4	7
6th	Financiers reluctant to risk losing money (21)	6	4
7th	Lack of cooperation by banks during business rescue proceedings (20)	7	5
8th	Distressed business not involving and engaging financiers prior to filing for business rescue (13) *	2	3
9th	Inadequate state of the relationship of financier with management and the BRP (5) *	2	2
10th	Non-availability of security (4) *	2	1
11th	Financiers lacking confidence in the rescue plan based on a viable business (4) *	-	3
	Other: Lack of accurate and reliable information; Opposing interests; Lack of regulation of industry; Mistrust of the business rescue system; The degree of opaqueness in the interpretation of the act, Company size; Lack of awareness, education and understanding of business rescue; Financiers not wanting to lead the precedence-setting process; Banks not wanting to lose control of the process.		

(*****) Previously identified in Proposition 4 as a prerequisite for success

Six of the prerequisites for success discussed in Proposition 4 closely correlate to the reasons reported for lack of interest by financiers. The remaining reasons centre on factors such as the influence of the banks, the South African rescue culture and uncertainties that exist in the industry with regard to PCF rankings.

Thus support was found for Proposition 5: The reasons for lenders' lack of interest in post-commencement finance are clear.

KEY OBSERVATIONS FROM THE FINDINGS

The research findings presented are consistent with the extant literature. However, this study contributes to the broader theory and expands the subject by identifying the specific complexities in the PCF landscape, as well as current practices identified by those practically involved in the industry.

During data collection, most subjects stated that the current extent of PCF in SA is small to non-existent. This is a concern, because the ability to successfully raise PCF has a major influence on the overall success of a business rescue. The key observations are discussed and explore insights into the status of PCF as well as success factors to consider for raising PCF in the future.

Critical pre-filing procedures: early consultation, viability assessment and pre-packaged financing

The first contribution relates to all the critical pre-filing procedures that are required to take place to ensure a higher probability of securing PCF. These elements seem not to have received the attention they deserve in the literature, but serve as a rich, all-inclusive theme in the overall findings. The key message emerging from these findings stresses that in order for PCF to be obtained successfully, some critical processes need to be followed before a business files for rescue. These include upfront consultation and collaboration with key stakeholders (especially financiers) in order to advise them of the situation, discuss alternatives and options and therefore ensure the buy-in from all parties prior to filing. In line with the findings of Pretorius (2013a), it is also critical for the BRP to perform a feasibility and viability assessment prior to accepting the engagement and prior to filing, in order to determine whether the company is an appropriate case (reasonable prospect) for business rescue. Lastly, and most importantly, as a result of the above two steps, the future post-commencement financier should be identified, and consensus obtained early on regarding the nature, timing and extent of PCF. These findings concur with international directives and best practice for PCF.

The impact of the newness of the legislation: lack of understanding and awareness, deficiency of case law and legal precedents, and incorrect filing by companies

The second contribution of this study relates to the impact of the nascent legislation, and the subsequent effects: lack of knowledge about the law, the absence of legal cases to guide interpretation of the act, and the "wrong" companies filing for rescue due to the previous two factors.

The absence of sufficient awareness, knowledge and understanding of business rescue has resulted in many players being reticent about participating in the industry because of the many loopholes and inefficiencies that still exist in the law, and the uncertain interpretation thereof. The current perceptions of business rescue further compound its perceived ineffectiveness. This has been exacerbated by the scarcity of case law and legal precedents, which creates uncertainty in the industry. In addition, business rescue is an expensive process for the different players to pursue and test. Furthermore, companies usually file too late in their distress timeline, when all possible turnaround and rescue options or efforts would have already been exhausted. Financiers are generally interested only in companies which still have a viable business model in place, with potential and realistic future prospects. The previously creditor-friendly culture in South Africa, solely protecting the interests of creditors, will also take a long time to change into a debtor-friendly culture focused on corporate renewal.

Finally, as a result of the above three factors, it has been observed that many businesses that should not be filing for rescue (due to their size or their being more suitable for liquidation) are doing so mainly as a delaying tactic. Much of this has to do with these businesses either abusing the moratorium or receiving incorrect advice from financial and legal advisors. Often their motives are associated with alternative objectives rather than with rescuing the business.

All of these factors unfortunately erode the trust of the financiers. A relationship of trust, openness and transparency with management and the BRP is critical for the confidence of the financier in the distressed business.

Ambiguities in the legislation and uncertainties in the industry

A direct consequence of the liability of newness gives rise to the third major contribution of this study. A host of ambiguities has been identified, and the opaqueness of the act gives rise to uncertainty in its interpretation; for instance, the definition of post-commencement funding, the definition of insolvent, the ranking of priorities, what constitutes a successful business rescue, and more.

A crucial concern that was raised is the fact that PCF in the local legislation does not enjoy super-priority status in debt rankings especially being ranked after employment. This criterion is a key requirement in the international directives and best practice for PCF. Without this provision for super preference, there is little or no incentive for non-traditional financiers (e.g. distressed lenders or private equity firms) to advance funds, as the risk is too high and the returns too low.

Furthermore, the lack of regulation of the industry, and more specifically the management of BRPs as a profession, is concerning for all stakeholders and leads to mistrust in the system.

It is therefore critical that these aspects be clarified in order to provide potential financiers with confidence to participate in the industry, as well as certainty that their funding will be recognised as a higher-priority debt during business rescue.

The availability of security and related losses for financiers

The fourth major contribution sheds light on a critical factor that is almost a fail-safe criterion for a business to be able to raise PCF: the extent of unencumbered assets available as security for the financier. This is a critical non-negotiable factor for almost all (traditional) financiers to provide PCF, as it provides them with the certainty that they will be repaid and/or not lose a substantial amount of their funds if the business is liquidated.

Therefore financiers might also advance funding in order to protect or preserve their existing security as well as to increase their level of confidence and certainty of being repaid. Non-traditional financiers are typically interested in the value and commercial viability of additional financing provided at attractive returns.

The role of the BRP in the ability to raise PCF: experience, knowledge and ability to prepare a sound rescue plan

The fifth significant contribution presented by this study is the significant impact of the role of the BRP in the ability of the distressed business to obtain rescue financing. It was evident from the findings that an experienced and competent BRP with collaborative networks and a thorough understanding of the business-rescue provisions and associated industry is much more effective at raising PCF than a BRP who does not possess the required competencies and qualities. An apparent impact of the above is the effect that the BRP competencies (Pretorius, 2013b) have on the quality and soundness of the rescue plan presented to creditors. In practice many rescue plans are unsustainable and not based on a viable business. Lack of accurate and reliable information also further aggravates the problem (Pretorius & Holtzhauzen, 2008:100).

Dominant (and potentially adverse) role of the banks

The sixth contribution of this study pertains to the impact that banks have had on the ability of BRPs to raise PCF. As banks are usually the major creditor (and therefore have a majority vote during business rescue proceedings), they often have a significant influence on the outcome of the rescue plan, the PCF raised and ultimately the success of the business rescue. Banks have been perceived and blamed as too conservative and risk-averse and therefore not cooperative during proceedings. Banks will also seldom provide additional financing, unless another financial backer or potential buyer of the business has already committed to the distressed business.

Some of the reasons provided for this are that because of the highly regulated industry in which they operate, they are uncompromising and unreasonable during PCF negotiations; they always want to make sure they do not lose any money or dilute their security, nor lose control of the process, and that no other creditor is better off than the bank as the main creditor. This paper, however, does not question the internal decision making structures of banks but only report the perceptions of the subjects.

DISCUSSION AND IMPLICATIONS FOR INDUSTRY

The discussion expands some key insights obtained from this research. Firstly, the subjects confirmed that there were clear and crucial directives for PCF found internationally that could be utilised as best-practice principles for the utilisation and application of PCF in South Africa. The data from the study largely supported the literature in identifying these directives, but also stressed that some elements appear to be more important than others, depending on the context (e.g. priority of the ranking and early finalisation of PCF), and that formalisation of procedures by the court is critical for consistency and clarity of processes.

Secondly, it was confirmed that the current extent of PCF in South Africa is almost non-existent, with various reasons being cited for this. Uncertainties and ambiguities in the legislation were identified as a key contributor, confirming unquantifiable risk as a key deterrent to investment.

Thirdly, the responses confirmed that there are distinct phases of PCF, with specific financing requirements in each phase. They also provided more detail on the typical financier, as well as the approximate time frame of financing required. The purpose is to provide clarity on what vital financing requirements exist in each phase, and therefore identify who is potentially well placed to support the business financially in each of these phases.

Fourthly, a list of prerequisites for the successful raising of PCF during business rescue procedures was identified. This could assist management, BRPs and financiers alike and increase the availability of PCF in future. The interviews provided rich evidence about the prerequisites that govern all parties to ensure the securing of PCF on a more regular basis.

Finally, the research uncovered insights regarding the availability of PCF to ensure a fresh understanding of the business rescue landscape in South Africa. The overall findings showed not only that there are prerequisites for finding PCF internationally, as explained in the literature, but that there are many key success factors to be found locally in order to ensure the successful implementation of business rescue proceedings. The findings are significant and noteworthy for the management of businesses, BRPs and financiers.

There are several factors that may influence the availability of PCF, and these can be summarised broadly as follows. Early engagement with key stakeholders and a pre-assessment of the business are critical to identify the nature of funding required, and to obtain commitment for financing from a proposed lender. According PCF priority status is crucial to attract financiers, but this needs to be supported by sufficient and available security, a sound rescue plan and a sustainable business model. Crucial in all of these steps is the role of the BRP, who has to build credibility, confidence and trust with all key parties in order to win their support and persuade them to believe in the future potential of the business. Open, regular and transparent communication is essential in all dealings described.

Some of the reasons for the current failures in raising finance are symptomatic of the fact that the legislation is barely 28 months old, and has not had sufficient time to settle, mature and develop into concrete guidelines and processes.

Framework proposed

The primary enhancers and inhibitors of PCF are presented as a framework to illustrate the key success factors that promote PCF, as well as disincentives for PCF in South Africa. There is an overlap with the key international directives for PCF. This framework could be used by management, BRPs and academics alike to increase the likelihood that approved PCF will become available.

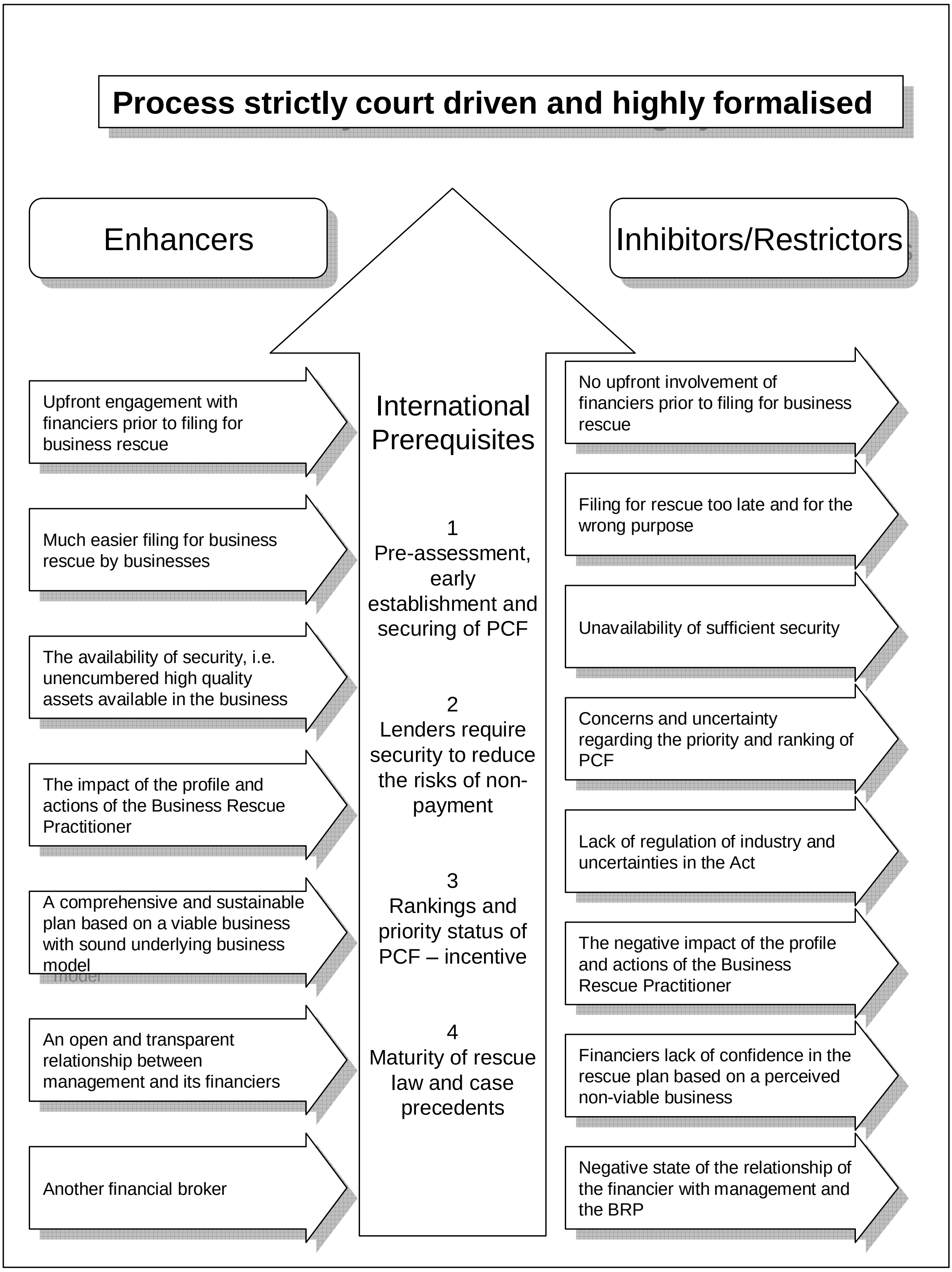


Figure 1: Primary influencers of enhanced PCF (own compilation)

LIMITATIONS, FUTURE RESEARCH AND IMPLICATIONS

Research limitations

Research methods and strategies are always subject to limitations. Three are specific to this research:

- Bias from the researchers in interpretation of the data, as explored in the methodology section
- The timing of the research, which took place within the first two years of the new regime. The landscape may therefore change in another two years. However, the principles are in line with international literature and general works on business failure.
- Finally, as the sample is not representative of the population (universe), non-probability sampling may result in a finding that is not representative of the population. However, sufficient saturation was achieved for the results to be generalised.

Recommendations for future research

The topic of this research is relatively new in academic terms, and consequently the research design was exploratory in nature. Therefore the research has focused on building theory, rather than on testing that theory. Future avenues for research might include an explanatory study utilising either qualitative or quantitative methods, and utilising real-life business-rescue case studies (successful or not) that have been completed since May 2011.

The research project has been aimed at uncovering insights regarding the current PCF levels and best-practice principles to ensure success. Future research to quantify the status of PCF might be useful to confirm and validate the findings of this research.

Finally, the relation between business plan quality and access to PCF would probably be of great benefit to the industry. Such research is under way.

Implications for business

The SA business rescue legislation is an important tool to support businesses in financial distress, but it has had limited success since its recent enactment. Consensus is that the legislation itself and its purpose are sound; however the interpretation and implementation thereof result in the inability of businesses and practitioners to raise PCF, and ultimately business rescue fails as a whole.

The legislation has the potential to support the South African Government in achieving the macro-economic and social goals for South Africa, by reducing the incidence of liquidation and business failure and thereby preserving the country's levels of employment. Companies, BRPs, financiers and government alike should offer collective support to facilitate and promote the development and stimulation of this crucial corporate renewal industry. This could be done by taking cognisance of the recommendations outlined for each party in this paper, as well as by utilising the framework proposed.

It would be naïve to believe that the road to an established and successful business rescue industry would be without its challenges and constraints; however, the most visionary players will not view these as inconveniences to overcome but rather embrace these as opportunities to leap ahead of competitors and carve out competitive advantage.

"A pessimist sees the difficulty in every opportunity; an optimist sees the opportunity in every difficulty" (Winston Churchill).

ACKNOWLEDGEMENTS

The authors are indebted for their time and effort to the subjects who participated in the interviews.

REFERENCES

CIPC (Companies and Intellectual Property Commission). 2012. Law Society of South Africa/Unisa Workshop, 21 September. Johannesburg: CIPC.

Cork, S. K. (1982). Report of the review committee in insolvency law and practice. Retrieved November 5, 2012, from http://discovery.nationalarchives.gov.uk/SearchUI/details?Uri=C11294862

Du Preez, W. 2012. The status of post-commencement finance for business rescue in South Africa. Johannesburg: Gordon Institute of Business Science. Unpublished

Guest, G., Bunce, A. & Johnson, L. 2006. How many interviews are enough? An experiment with data saturation and variability. Field Methods 18(1): 59–82.

Leedy, P.D. & Ormrod, J.E. 2001. Practical research: planning and design. 7th edition. Upper Saddle River, NJ: Merrill/Prentice Hall.

Lotheringen, A. 2013. Personal communication, 17 June. Port Elizabeth.

Marshall, C. & Rossman, G.B. 2006. Designing qualitative research. Thousand Oaks, CA: Sage.

Pelser, H. 2012. SA's business rescue track record. (September 4). Available at: http://www.moneyweb.co.za/mw/content/en/moneyweb-industrials?oid=609761&sn=2009+Detail [Accessed 20 September 2012].

Pretorius, M & Holtzhauzen, G.T.D. 2008. 'Critical Variables of venture turnarounds: a liabilities approach', Southern African Business Review, 12(2):87-107.

Pretorius, M. 2009. Defining business decline, failure and turnaround: A content analysis. South African Journal of Entrepreneuship and Small Business Management NS 2(1.1): 1-16.

Pretorius, M. 2012, July 11. Business Rescue Plans (unpublished research).

Pretorius, M. & Holtzhauzen, G.T.D. 2013. 'Business rescue decision making through verifier determinants – ask the specialists. South African Journal of Economics and Management Sciences**.** 16 (4), December 468-485.

Pretorius, M. 2013a. Tasks and activities of business rescue practitioners. South African Business Review 17(3) December (forthcoming).

Pretorius, M. 2013b. A competency framework for the business rescue practitioner profession. Paper presented at South African Institute of Management Scientists conference held 16-17 September. Potchefstroom, South Africa.

Republic of South Africa. 2008. South African Companies Act 71 of 2008. Government Gazette 421 (32121). Available at: http://www.info.gov.za/view/DownloadFileAction?id=98894 [Accessed 22 February 2012].

Saunders, M. & Lewis, P. 2012. Doing research in business and management. Harlow, Essex: Pearson Education.

Statistics South Africa. 2012. Statistical Release P0043: Statistics of liquidations and insolvencies (Preliminary). Available at: www.statssa.gov.za [Accessed 5 November 2012].

Vriesendorp, R.D. & Gramatikov, M.A. 2010. Funding corporate rescue: The impact of the financial crisis. INSOL International Insolvency Review 19(3): 209–237.

Yin, R.K. 2003. Case study research: Design and methods. Thousand Oaks, CA: Sage.