

## Question 1

Lesego is a director of One Stop Groceries (Pty) Ltd. When the company needed to appoint a new marketing agent to advertise its products in Gauteng, Lesego persuaded the board to appoint 'The Best CC' by convincing them that The Best CC would be ideal for this task. However, Lesego did not disclose the fact that his brother had a substantial member's interest in The Best CC. The Best CC was appointed, but a few months later it became clear that One Stop Groceries (Pty) had suffered substantial losses in Gauteng because its products were not being advertised effectively, since The Best CC had no experience in this type of work. A number of shareholders in One Stop Groceries (Pty) Ltd now want to hold the company's directors liable for breach of their duty to act in the best interest of the company and their duty to care, skill and diligence by appointing an inexperienced close corporation as their marketing agent.

Advise Lesego and the other directors of One Stop Groceries (Pty) Ltd on whether they can escape liability on the basis of the business judgment rule.

### *Duties as Directors*

Section 76 requires a director to act in good faith and in the best interest of the company<sup>1</sup>. A director should act with the degree of care, skill and diligence that may reasonably be expected of a person carrying out such functions and having the same skill and experience of that director – the reasonable man/woman test.

Directors are required to disclose any "personal financial interest". They may not use their position as director or information gained as a director to make a secret profit or gain advantage for themselves or someone else or to cause harm or detriment to the company.<sup>2</sup>

### *Business judgment rule*

According to the business judgment rule (section 76(4)), the director will be regarded as having acted in the best interest of the company and with the required degree of care, skill and diligence if the director:

- Took reasonable steps to become informed about the matter;
- had no material personal financial interest in the subject matter of the decision or had no reasonable basis to know that any related person had a personal financial interest in the matter, or disclosed his/her interest;
- made or supported a decision in the belief that it was in the best interest of the company.

A director will also escape liability where he or she had a rational basis for believing, and actually believed that the decision was in the best interest of the company<sup>3</sup>.

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<sup>1</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 108 <sup>1</sup>

<sup>2</sup> The Companies Act, no 71 of 2008, an explanatory guide, DTI

<sup>3</sup> Learning Unit 3, UNISA, provisions of the Companies Act.

### *Application of facts and conclusion*

As Lesego and his brother are related persons, it is clear that Lesego had a material personal interest in the appointment of The Best CC. The other members of the board relied upon the information that Lesego gave them, and had a rational belief that the decision was in the best interest of the company.

Accordingly, as Lesego did not disclose his interest, he cannot rely upon the business judgment. The other members of the board, acting in good faith, may rely upon the business judgment rule.

### **Question 2**

The board of directors of Green Fields Ltd ('the company') approaches you for advice. The board has resolved to issue shares to the following persons:

- the newly appointed chief executive officer of the company;
- a new director, Mr Brown, who will be joining the board of directors in three months' time; and
- certain employees of the company in terms of an employee share scheme.

However, the board of directors is uncertain whether approval from the shareholders of the company is required to issue these shares. The board is further unsure about how the payment for these shares is to be determined. The board is particularly concerned about the consequences if they do not comply with the requirements of the Companies Act. Advise the board of directors of Green Fields Ltd on the above matters. Refer to particular sections of the Companies Act where applicable.

The issue of shares relates to section 41 of the Act.

The Companies Act regards the decision to issue shares as a management decision, i.e the board of directors have the power to issue shares without the approval of the shareholders, unless the Memorandum of Incorporation ("MOI") imposes specific limitations.

The board will however need shareholder approval when the issue of shares is to:

*A special resolution is required when shares are issued to:*

- 1- where the shares are issued to directors (including future directors), or to certain prescribed officers of the company;
- 2 – where the shares are issued to a person related or inter-related to the company or a director or prescribed officer of the company;
- 3 – where the shares are issued to a nominee of a director or prescribed officer of the company<sup>4</sup>.

*An ordinary resolution is required when shares are issued to:*

- 1 – Under an agreement underwriting the shares;

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<sup>4</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D

- 2 – in the exercise of a pre-emptive right to be offered and to subscribe shares;
- 3 – In proportion to existing holdings, and on the same terms and conditions as have been offered to all the shareholders of the company or to all the shareholders of the class or classes of shares being issued;
- 4 – pursuant to an employee share scheme; or
- 5 – pursuant to an offer to the public<sup>5</sup>.

The board of directors also has the authority to increase the authorized shares of the company<sup>6</sup>. Section 40 provides that the board may only issue shares for adequate consideration. The board must determine what an adequate consideration for the shares would be<sup>7</sup>.

Shares may also be issued in exchange for future services or payments. When shares are issued for future services or future payment, the shares must be issued immediately and should be held in trust until the future obligations are fulfilled<sup>8</sup>.

Where the voting power of a class of shares that is to be issued is equal to or exceeds 30% of the total voting power of all the shares of that class held by shareholders immediately before the transaction or series of transactions, a special resolution by all the shareholders is required<sup>9</sup>.

As per Section 44 of the Act, to the extent that the MOI provides otherwise, the board may authorize the company to provide financial assistance by way of a loan, guarantee, the provision of security or otherwise to any person for the purposes of any securities of the company, should certain conditions be complied with.<sup>10</sup>

#### *Application of facts and conclusion*

In this particular instance, Green Fields Ltd will need to obtain shareholder approval for the issue of shares, via a special resolution for the issuance of the shares to the newly appointed chief executive officer of the company and for the new director. Approval by means of an ordinary resolution is required for the issue of the shares to certain employees of the company in terms of an employee share scheme.

The shares need to be issued for adequate consideration. The board must determine what an adequate consideration for the shares would be. The board may authorize the company to provide financial assistance to the receivers of the shares, if necessary, should conditions be complied with in terms of section 44 of the Act.

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<sup>5</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D

<sup>6</sup> Learning Unit 5, UNISA, provisions of the Companies Act

<sup>7</sup> Learning Unit 5, UNISA, provisions of the Companies Act

<sup>8</sup> Learning Unit 5, UNISA, provisions of the Companies Act

<sup>9</sup> Learning Unit 5, UNISA, provisions of the Companies Act

<sup>10</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D

### QUESTION 3

Chris, Barbara and Tumo are directors of Zero Degrees (Pty) Ltd. Chris is regarded as a savvy businessman, whose sharp negotiation skills have earned the company good profits since the company was incorporated ten years ago. Chris is approached by Ben, a director of Ninety Nine Degrees (Pty) Ltd to make his negotiation skills available on a government contract that promises to yield substantial profits for Ninety Nine Degrees (Pty) Ltd and to Chris in his personal capacity. Zero Degrees (Pty) Ltd has also made a bid on the contract. Chris agrees, and proceeds to render his services to Ninety Nine Degrees (Pty) Ltd.

In your opinion, does Chris have an obligation to tell the board of Zero Degrees (Pty) Ltd about his personal gains, or is this a case of ‘every person for himself’?

#### *Duties as Directors*

Section 76 requires a director to act in good faith and in the best interest of the company<sup>11</sup>. A director should act with the degree of care, skill and diligence that may reasonably be expected of a person carrying out such functions and having the same skill and experience of that director – the reasonable man/woman test.

The common law position is that directors have a fiduciary relationship with the company. This relationship applies to all directors of companies.<sup>12</sup>

Section 75 provides that directors are required to disclose any “personal financial interest” if they conflict with those of the company<sup>13</sup> (unless this information falls within section 76(2)(b), namely that the information is: immaterial to the company, generally available to the public; or known to the other directors.)<sup>14</sup> They may not use their position as director or information gained as a director to make a secret profit or gain advantage for themselves or someone else or to cause harm or detriment to the company.

As indicated in the case of *Robinson v Randfontein Estates Gold Mining Co Ltd*, “Where one man stands to another in a position of confidence involving a duty to protect the interest of that other, he is not allowed to make a secret profit at the other’s expense or place himself in a position where his personal interest conflicts with his duty.”<sup>15</sup>

#### *Application of facts and conclusion*

Chris is a director of Zero Degrees (Pty) Ltd and is therefore in a fiduciary relationship with the company. Chris is accordingly not permitted to use his position to make a secret profit to the disadvantage/harm of Zero Degrees (Pty) Ltd.

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<sup>11</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 108 <sup>11</sup>

<sup>12</sup> Learning Unit 3, UNISA, provisions of the Companies Act.

<sup>13</sup> Learning Unit 3, UNISA, provisions of the Companies Act.

<sup>14</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 118

<sup>15</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 121 <sup>15</sup>

Chris has also not disclosed his financial interest/conflict of interest to Zero Degrees (Pty) Ltd that he will be assisting another company with the same bid. This is in breach of his fiduciary duty towards Zero Degrees (Pty) Ltd and this company may hold Chris personally liable to recover any losses as per this breach.

#### **Question 4**

Loan Sharks (Pty) Ltd (“the company”) provides unsecured loans to mineworkers and communities around the platinum belt in Marikana. The company’s revenue has shrunk as a result of a crippling 5 month labour strike in 2014. During this labour strike, most of the company’s clients did not receive any wages, and therefore were unable to repay their loans with the company.

This will probably create cash flow problems for the company in the future, as it will not have enough cash in hand to service its own creditors.

In order to pre-empt a looming financial disaster and to remain financially stable, the company has laid off many of its employees. The company has also learnt that its creditors, of which Fin Bank is an extremely important one, are very worried about the situation and are contemplating taking steps against Loan Sharks (Pty) Ltd. Because the situation of the company does not comply with the statutory requirements for commencing with business rescue, the board of the company resolved instead to deliver a proposal to creditors in terms of which the company offers to settle 80% of all the claims of its creditors as full and final settlement. The board of the company expects that most of the creditors will accept the offer, but that it will be rejected by some individual creditors. You are approached by the company’s board, who asks you to advise them whether there is a procedure in the Companies Act which can be used to make the offer to the creditors and upon their acceptance of the offer will bind dissenting creditors. In your advice to the company, clearly identify the procedure that can be used and by whom the proposal may be made in terms of the procedure. Also clearly explain the manner in which the proposal must be made, the procedure that needs to be followed for the proposal to be adopted, and the court’s role during this procedure.

#### *Compromise – section 155*

*What is a compromise and who may apply for this procedure:*

A compromise is an agreement between a company and its creditors in terms of which the creditors agree to accept less than their full claims against the company e.g. accepting 50 cents in the rand in full settlement of what is due to them.<sup>16</sup>

A company may use this option even if the company is not financially distressed, but not if the company is engaged in business rescue proceedings<sup>17</sup>.

*Who may propose a compromise and what is the procedure?*

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<sup>16</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 263

<sup>17</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 263

A company's board of directors or the liquidator of the company (if the company is being wound up) may propose a compromise to all creditors.<sup>18</sup>

A proposal for a compromise must be made by delivering a copy of the proposal and notice of a meeting to consider the proposal to the Commission and to every creditor of the company or every member of the relevant class of creditors whose name and address is known to, or can reasonably be obtained by the company.<sup>19</sup>

A proposal for a compromise will be regarded as adopted, if it is supported by a majority in number, representing at least 75 per cent in value of the relevant voting creditors.<sup>20</sup>

#### *What should the compromise contain?*

Such a proposal must contain all information reasonably required to decide whether or not to accept or reject the proposal.<sup>21</sup> The proposal must be divided into three parts, namely:

1. Part A – Background;
2. Part B – Proposals; and
3. Part C – Assumptions and conditions<sup>22</sup>.
4. Other accompanying requirements:
  - Projected balance sheet and statement – which must include a notice of any significant assumptions on which the projections are based, and may include alternative projections based on varying assumptions and contingencies;
  - Certificate by authorized director or prescribed officer of company – stating that any factual information provided in the proposal appears to be accurate, complete and up to date; and any projections provided are estimates made in good faith on the basis of factual information and assumptions<sup>23</sup>.

#### *Effects of approval and role of court:*

A compromise will not be enforceable until it has been made an order of court. This requires one application to court – it is not necessary to ask the court's permission to arrange a meeting where the proposed compromise will be discussed and voted on.

In terms of s155(7(b)), the court may sanction the compromise if it considers it just and equitable to do so. The court must have regard to:

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<sup>18</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 264

<sup>19</sup> Learning Unit 10, UNISA, provisions of the Companies Act

<sup>20</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 270

<sup>21</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 270

<sup>22</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 264

<sup>23</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 264<sup>23</sup>

- The number of creditors of any affected class of creditors who were present or represented at the meeting and who voted in favour of the proposal; and
- In the case of a compromise in respect of a company that is in liquidation, a report by the Master.<sup>24</sup>

If the compromise is approved by the court, a copy of the order must be filed with the Commission by the company within 5 business days. A copy of the order must also be attached to each copy of the company's Memorandum of Incorporation that is kept at the company's registered office or elsewhere as contemplated in section 25.

The order of court sanctioning a compromise is final and binding on all the company's creditors but does not affect the liability of any person who is a surety of the company.<sup>25</sup>

## QUESTION 5

Tim was a director of Beta (Pty) Ltd, of which he and his brother Gilbert were the only two shareholders. Tim tried to circumvent certain regulations governing the export of traditional sports supplements by calling the consignment natural vitamins. He was subsequently tried and was convicted of fraud in 2013. As a result, he was disqualified from acting as a director of the company, and was removed from the office. Tim, however, believes that he has mended his ways and wants to be reinstated as a director of Beta (Pty) Ltd. He has made an application to the court to be reinstated. Gilbert, however, strongly objects to Tim's being reinstated as a director.

Advise Tim on his chances of success, with reference to the common law, relevant case law and the provisions of the company's Act.

In spite of this disqualification, s 69(11) gives a court a discretion to grant an exemption. As per section 69(8) (b)(iii) a disqualification in terms of this section ends at the later of 5 years after the date of removal from office, or at the completion of the sentence imposed for the relevant offence, or at the end of one or more extensions, as determined by a court from time to time, on application by the Commission.

The relevant persons will have to make an *ex parte* application to court for permission to act as a director. The applicant will have to prove to the court that he has been rehabilitated from his wrongful ways and can be trusted with responsibilities of directorship.

This case is similar to *Ex parte Barron*, where the applicant applied to court for authorization to act as a director. The court held that the factors that affect the discretion of the court are:

- The type of offence;
- Whether or not it was a first conviction;
- The type of punishment imposed;
- Whether it was a public company; and

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<sup>24</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 267

<sup>25</sup> Learning Unit 10, UNISA, provisions of the Companies Act

- The attitude of shareholders and whether all the shareholders supported this application.

In this case the court acted more leniently towards a private company than a public company.

In *Ex Parte Tayob* the applicants had been convicted of bribery. They brought an application one year after their conviction – the court concluded that too little time had passed to prove that the applicants had rehabilitated from their dishonest ways.

#### Conclusion:

Matters counting in the accused's favour is the fact that this is his first offence – also the court acts more leniently towards a private company. Matters counting against the accused is the short time frame passed and the fact that the other shareholder, a family member, does not support the rehabilitation.

### **QUESTION 6**

McNuggets Ltd issued shares for which the consideration was payable in future instalments. The subscribers still owe the consideration of 5% of the shares originally allocated to them. The company now wants to waive the debt owed by each subscriber to the company, as the company's yearly financials showed a huge profit.

Critically discuss the requirements that have to be met in terms of the Companies Act if the company wants to write off the outstanding part of the issue price. (no need to discuss financial assistance).

Section 40(2) of the Companies Act provides that before a company issues any particular shares, the board must determine the consideration for which, and the terms on which, those shares will be issued e.g the board must decide what value the company will receive in exchange for issuing shares to the holder of those shares – must be for adequate consideration to the company, as determined by the board.

When shares are issued for future payments, such shares are held in trust until the future event occurs. While the shares are held in trust, voting or appraisal rights are not exercisable.

### **QUESTION 7**

Explain whether it is possible for a valid resolution of shareholders to be passed without convening a meeting of shareholders.

It is possible to take decisions without convening a meeting. If the company wishes to take an ordinary resolution in such a way, the company must submit a proposed resolution to every person who is entitled to vote on the resolution.

The shareholders are then entitled to exercise their vote in writing within 20 days from receiving the proposed resolution and to return the written vote to the company. Such a resolution is adopted if it is supported by persons entitled to exercise sufficient voting rights



for it to be adopted as an ordinary or special resolution, at a properly constituted shareholders meeting. If adopted, it has the same effect as if it had been approved by voting at a meeting.

Within 10 days after adopting a resolution, the company must deliver a statement describing the results of the vote. No business that is required to be conducted at the annual general meeting of the company may be conducted without convening a meeting.

## **QUESTION 8**

Thandi is one of the five directors of Surfs Heaven (Pty) Ltd. The other directors are of the opinion that Thandi is neglecting her duties as director because she is out surfing all the time. The board of directors has therefore taken a resolution to remove her as director. Thandi is very unhappy about this and believes that she is in fact promoting the company by surfing regularly. She wants the matter to be reviewed.

- 8.1 Advise Thandi on the grounds upon which a director may be removed by the board of directors as well as on whether the matter may be reviewed.
- 8.2 Explain how your answer would have differed (if at all) if the board of directors of Surfs Heaven (Pty) Ltd had consisted of only Thandi and one other director.

A director may be removed by shareholders and in some circumstances, by the board of directors. A director may be removed by an ordinary resolution adopted at a shareholders meeting.

In terms of s71(2), the notice of a shareholders' meeting to remove a director, and the resolution, must be given to the director prior to considering the resolution to remove the director. The period of notice that should be given is equivalent to that which a shareholder is entitled to receive when convening a meeting.

The director must be allowed the reasonable opportunity to make a presentation, in person or through a representative, to the meeting, before the resolution is put to a vote.

If a company has more than 2 directors and it is alleged by a shareholder or by a director that the director of the company has become ineligible or disqualified, a director may be removed by a resolution of the board of directors if:

- A director has become incapacitated to the extent that the director is unable to perform the functions of a director and is unlikely to regain that capacity within a reasonable time; or
- The director has neglected or been derelict in the performance of the functions of director.

Where the board has taken a resolution to remove the director, the director may apply to a court to review the determination of the board. An application for review must be brought within 20 business days from the date the decision is taken by the board. The court may confirm the determination of the board, or remove the director from office, if the court is satisfied that the director is ineligible or disqualified, incapacitated, or non-resident, or has been negligent or derelict.

8.2 The above rules do not apply to a company that has fewer than 3 directors. In the case of a company that has fewer than 3 directors, any director or shareholder may apply to the Companies Tribunal to determine any matter referred to above.

### **QUESTION 9**

The Memorandum of Incorporation of Guns 'n Roses (Pty) Ltd ('the company') provides that the main business of the company is the manufacturing and sale of toy guns. Mr Hoodlum, one of the directors, has been authorised by a board resolution to act on behalf of the company. While acting on behalf of the company Mr Hoodlum concludes a contract with Mr Brothel for the purchase of a nightclub. Mr Brothel has no knowledge of the contents of the Memorandum of Incorporation of the company. Mr Orthodox, a majority shareholder of the company, is upset about the purchase of the nightclub. Mr Orthodox approaches you for legal advice and requires you to advise him on the following:

Is the contract concluded by Mr Hoodlum and Mr Brothel valid and enforceable against the company? Give Reasons.

Section 19(1) provides that a company has all the legal capacity and the powers of a natural persona except to the extent that a juristic person is incapable of exercising any such power. The company is also not restricted by its main business. Although the company's MOI may impose restrictions on the legal capacity of the company, any such restrictions would not render invalid any contract that conflicts with these restrictions. The company cannot rely upon the ultra vires doctrine in terms of section 19(4). Thus the contract is valid and binding on the company and the other party to the contract.

### **QUESTION 10**

Tom, Jerry, Garfield, and Mickey form a new company with the name Cat and Mouse Limited. Tom is appointed as an executive director of the company, while Jerry, Garfield, and Mickey are appointed as non-executive directors of the company. They have been informed that the company must appoint an audit committee and decide that they will all be members of the audit committee. They also wish to appoint Minnie, the company secretary, to sit on the audit committee. With reference to the Companies Act 71 of 2008, advise Tom and Jerry of the following:

1. Who is required to appoint the first members of the audit committee? (2)
2. May Tom, Jerry, Mickey and Minnie be members of the audit committee? (5)
3. Briefly discuss the duties that the audit committee is required by the Companies Act 71 of 2008 to perform in Cat and Mouse Limited. (3)

### *Audit committee*

1. Members of an audit committee are appointed by shareholders. The members are required to be directors of the company.<sup>26</sup> The members are appointed at the annual general meeting.<sup>27</sup>
2. As per section 94, each member (there needs to be at least 3 members) of an audit committee must:
  - be a director of the company; and
  - may not be involved in the day-to day running of the company's business (or during the previous year); and
  - may not be a prescribed officer/full time employee of the company (or during previous 3 years)

A member of an audit committee must be a non-executive independent director of the company.<sup>28</sup>

Tom as executive director is involved in the day-to day running of the business. Minnie is not a director of the company. Accordingly Tom and Minnie will not be legible to be appointed to the audit committee; however Jerry, Garfield and Mickey are eligible to be appointed to the audit committee.

3. The duties of the audit committee (in accordance to section 90), must:
  - nominate an independent auditor for appointment;
  - determine the fees to be paid to the auditor and the terms of engagement;
  - ensure that the auditors appointment complies with legislation and policies;
  - determine the nature and scope of any non-audit services that the auditor may provide to the company and to pre-approve these services;
  - prepare a report to be included in the annual financial statements explaining how the audit committee carried out its functions, that the audit committee is satisfied with the independence of the auditor and to comment on the general accounting practices of the company;
  - receive and deal with any concerns relating to accounting practices and internal audit of the company or any related matter;
  - make submissions to the board concerning the company's accounting policies; and
  - Perform any other functions as determined by the board.<sup>29</sup>

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<sup>26</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 143

<sup>27</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 285

<sup>28</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 285

<sup>29</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 286

## QUESTION 11

Peter, Nonhlanhla and Simon are the directors of Nguni Hide Tanneries Ltd, a company which tans and sells the hides of Nguni cattle. The board is considering the repurchase of some of its own shares by the company, or by using a subsidiary of the company to accomplish this. They are not sure if the company may do this, and if so, how to go about it and they consult you for advice. Advise them on the position regarding:

- the repurchase of its own shares by the company itself; and
- by using a subsidiary; and,
- the consequences should they not comply with the requirements of the Companies Act, 2008 in this regard.

### *repurchase of own shares*

1. A company may acquire its own shares if the decision to do so satisfies the requirements of section 46 i.e. must be authorized by the board and must meet the liquidity and solvency test<sup>30</sup>. A share buyback is regarded as a distribution.<sup>31</sup>
2. A subsidiary of a company may acquire shares in that company, subject to the conditions:
  - no more than 10% of all the issued shares of any class of shares of the company may be held by, or for the benefit of, all the subsidiaries of that company taken together; and
  - no voting rights attached to those shares may be exercised while the shares are held by a subsidiary of the company, also
  - after the company/subsidiary has acquired the shares, there must be shares left other than convertible or redeemable shares; and
  - there must be shares in issue that are held by shareholders other than by the company's subsidiaries<sup>32</sup>.
3. Should a company fail to fulfil its obligations in terms of a repurchase agreement, the company must apply for a court order to apply for the suspension of the acquisition of the shares - whereby the court may make an order that is just and equitable in view of the financial circumstances of the company to ensure that the person to whom the company is required to make the payment, should receive such payment as soon as possible.<sup>33</sup>.

If the company acquired shares without meeting the necessary requirements, the agreement between shareholders and the company still remains enforceable, however

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<sup>30</sup> Learning Unit 6, UNISA, provisions of the Companies Act

<sup>31</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 87

<sup>32</sup> Learning Unit 6, UNISA, provisions of the Companies Act

<sup>33</sup> Learning Unit 6, UNISA, provisions of the Companies Act

the company does have the option of applying to court within two years after the acquisition to have the repurchase reversed.<sup>34</sup>

## QUESTION 12

Tlou is a director of Animal Park Ltd, a listed public company. Tlou and his friend Tau keep regular e-mail contact. Tlou knows that Tau usually reads his e-mails at 7h00 every day. Tlou sent Tau a message at 6h00 saying that Animal Park Ltd will post good results and that the results will be published at 10h00 on the same day. On that particular day, Tau, for some unknown reason, only read his e-mails at 9:30. However, at 9h00, Tau had instructed his broker, Phiri, to buy 1000 shares in Animal Park Ltd because he had a feeling that the company was going to publish good results. Discuss whether Tau and Tlou have committed any of the insider trading offences under the Financial Markets Act of 2012.

[10]

### *Insider trading*

Insider trading is the trading of securities based on information that is not yet made public<sup>35</sup>, which if obtained as public knowledge, would have a material effect on the price or value of the security. There is no definition of insider trading in s 1 of the Financial Markets Act (“FMA”).

Section 78 of the FMA provides that an insider who knows that he has inside information and, who deals directly or indirectly in the securities listed on a regulated market to which this information relates, commits an offence.<sup>36</sup>

Tau instructed his broker to purchase shares before he became aware of Animal Parks (Ltd)’s good results and before they became published. Although inside information had been forwarded to him, he was not aware that he was in possession of such information before he purchased further shares and accordingly did not act upon such information. Tau has therefore not committed any offence.

It is an insider-trading offence to disclose inside information to another person.<sup>37</sup> Tlou has forwarded ‘inside’ information to Tau before these results were made public. Tlou has committed an offence in terms of the FMA.

## QUESTION 13

Batau Ltd is an unlisted mining public company that has over 1000 shareholders. One of its current shareholders, Mbedzi (Pty) Ltd, wishes to acquire all the issued shares in the company.

The board of directors of Mbedzi (Pty) Ltd has heard that all the shareholders except Lerato, who holds 9% of the issued shares in Batau Ltd, are very keen on selling their shares.

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<sup>34</sup> Learning Unit 6, UNISA, provisions of the Companies Act

<sup>35</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 223

<sup>36</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 225

<sup>37</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 227

Mbedzi (Pty) Ltd does not wish to acquire anything less than 100% ownership of Batau Ltd but the board of directors of Mbedzi (Pty) Ltd does not wish to structure the deal as a scheme of arrangement.

You are required to give legal advice to Mbedzi (Pty) Ltd on the rules that regulate such a transaction and how it could structure an offer to ensure that it would not have to acquire less than all the issued shares.

### *Compulsory acquisitions*

A compulsory transaction/squeeze out (section 124) is a transaction where a person or offeror attains more than 90% of any class of securities in a company<sup>38</sup>. Batau Ltd is considered a 'regulated company' as it is a public company. A compulsory acquisition falls within the definition of an affected transaction.<sup>39</sup>

If the offer has been accepted by the holders of at least 90% of the class of securities, the offeror may notify the holders of the remaining securities of the class:

- the offeror has been accepted to that extent; and
- the offeror wishes to acquire all remaining securities of that class.

After giving the notice, the offeror is entitled to acquire the securities concerned on the same terms that applied to securities whose holder accepted the original offer.<sup>40</sup>

In effect this would mean that Mbedzi (Pty) Ltd can force the minority shareholders of Batau Ltd to part with their securities as Mbedzi (Pty) Ltd he will become the holder of all the securities in the company.

### QUESTION 14

Discuss and explain fully the meaning and implication of the term "adequate consideration" in section 40 of the Companies Act, 2008.

[10]

### *Adequate consideration*

Section 40 provides that the board may only issue shares for adequate consideration. The board must determine what an adequate consideration for the shares would be<sup>41</sup>.

The determination may only be challenged on the grounds that it constituted a breach of the standard conduct expected of directors and is in breach of their fiduciary duties or in delict.<sup>42</sup>

Negotiable instruments and future services, future benefits and future payments, and even assets are all allowed as consideration for newly issued shares, but shares may only be transferred to the subscriber to the extent that the instruments have become negotiable by the company, or to the extent that the subscriber has fulfilled his future obligations.<sup>43</sup>

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<sup>38</sup> Learning Unit 8, UNISA, provisions of the Companies Act

<sup>39</sup> Learning Unit 8, UNISA, provisions of the Companies Act

<sup>40</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 219

<sup>41</sup> Learning Unit 5, UNISA, provisions of the Companies Act

<sup>42</sup> Learning Unit 5, UNISA, provisions of the Companies Act

<sup>43</sup> Learning Unit 5, UNISA, provisions of the Companies Act

## QUESTION 15

Discuss the various types of shareholders' meetings under the Companies Act 71 of 2008 and the various methods by which such shareholders' meetings may be convened under the Companies Act 71 of 2008. Further discuss the consequences and prescribed procedures under the Companies Act 71 of 2008 if a company fails to convene a shareholders' meeting. [15]

### *Shareholders meetings*

A shareholders' meeting is a meeting of shareholders who are entitled to exercise voting rights in relation to a matter.<sup>44</sup> The board of directors, or any other person specified in the company's MOI or rules, may call a shareholders' meeting at any time, and must be called for in the following circumstances:

- at any time that the board is required to convene a meeting and to refer a matter to decision by shareholders as provided for in the Act or by the MOI e.g. to elect a director; and
- when a meeting is demanded by shareholders, provided that the demand is signed by the holders of at least 10% of the voting rights entitled to be exercised in relation to the matter proposed to be considered at the meeting.<sup>45</sup>

An annual general meeting must be held every year by a public company where specific matters are discussed e.g. appointment of an audit committee.

If the company wishes to make an ordinary resolution without convening a meeting, the company must submit a proposed resolution to every person who is entitled to vote on the resolution. The shareholders are then entitled to exercise their vote in writing within 20 days from receiving the proposed resolution and to return the written vote to the company. A shareholder is entitled to appoint a proxy to attend, participate in, and vote at the meeting on behalf of the shareholder.<sup>46</sup>

An election of a director that could be conducted at a shareholders' meeting may instead be conducted by written polling of all the shareholders entitled to exercise voting rights in relation to the election of that director.<sup>47</sup> A company may also provide for participation in a shareholders' meeting by electronic communication.<sup>48</sup>

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<sup>44</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 107

<sup>45</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 95

<sup>46</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 107

<sup>47</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 102

<sup>48</sup> Learning Unit 1, UNISA, provisions of the Companies Act

In an event that no person is authorized to convene a meeting, any shareholder may request the Companies Tribunal to issue an administrative order for a shareholders' meeting to be convened.<sup>49</sup>

If a company fails to convene a meeting, a shareholder may apply to court for an order requiring the company to convene a meeting on a date, and subject to any terms that the court considers appropriate.<sup>50</sup>

#### QUESTION 16

Meropa Ltd holds 20% of the voting shares in Motheo Ltd, while Thebe Ltd holds 25% of the voting shares in the same company. The remaining 55% of the voting shares in Motheo Ltd are held by Molemo Ltd.

Explain what is meant by "a group of companies" and whether a principal-subsidary relationship exists between Motheo Ltd and any of the other three companies.

[10]

##### *Group of companies*

A group of companies is defined as two or more companies that are related or interrelated. One company is related to another company if:

- one company directly or indirectly controls another company; or
- one company is a subsidiary of another company<sup>51</sup>

A subsidiary is a company that is controlled by a holding company<sup>52</sup>.

A principle-subsidary relationship does exist between Motheo Ltd and the other 3 companies since Molemo Ltd owns more than 50% of the voting shares and is therefore the controlling company. (Motheo Ltd is a subsidiary of Molemo Ltd). As the companies are all related by means of a common controlling company (Molemo Ltd), the companies form part of a group of companies.

#### QUESTION 17

Samson was recently appointed as a business rescue practitioner for Rubber Tyres and Tracks (Pty) Ltd. Some of the affected persons in the company are unhappy because Samson has started drafting the business rescue plan without consulting them. Advise Samson regarding the following matters:

- (a) Is he compelled to consult any persons before drafting the business rescue plan?

(3)

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<sup>49</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 102

<sup>50</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 103

<sup>51</sup> Learning Unit 7, UNISA, provisions of the Companies Act

<sup>52</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 456



- (b) The Companies Act of 2008 prescribes the contents of a business rescue plan. Name the four parts into which the plan must be divided and give one example of the items or aspects that must be included in each of the parts respectively. (8)
- (c) Explain the requirements of section 152 of the Act for the business rescue plan to be finally and validly approved at the meeting called for this purpose. (4)

### *Business rescue*

- (a) The company must notify every shareholder and creditor, as well as any registered trade union representing the company's employees and those employees not represented by trade unions, of:
- the resolution;
  - the date on which it became effective; and
  - the grounds on which the resolution was taken.

Should the company not notify the affected persons as prescribed, the business rescue resolution lapses.<sup>53</sup>

- (b) The plan must contain the following parts:

- Part A – Background

Mainly contains financial information e.g. complete list of the material assets of the company, indicating which assets were held as security by creditors at the start of the business rescue proceedings and a list of the creditors of the company when business rescue proceedings began.

- Part B – Proposals

Here all the proposed measures to assist the company in overcoming its problems and managing its debts are set out e.g. which assets of the company will be available to pay creditors in terms of the business rescue plan;

- Part C – Assumptions and conditions

This part of the plan must indicate any conditions that must be fulfilled before the plan can come into operation e.g. a projected balance sheet and statement of income and expenses for the next three years based on the assumption that the plan will be adopted.

- Certificate

The plan must conclude with a certificate in which the business rescue practitioner states that the information provided in the plan appears to be correct and up to date, and that the projections were made in good faith on the basis of factual information.<sup>54</sup>

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<sup>53</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 239

(c) The business rescue practitioner must convene a meeting of the company's creditors (and if applicable the shareholders) to consider the rescue plan;

The practitioner must explain the plan and inform the meeting as to whether he believes that there is a reasonable prospect of the company being rescued;

The representatives of the employees must also be given an opportunity to address the meeting. The meeting may discuss and propose amendments to the plan before voting on its approval.

If the plan is supported by more than 75% in value of all the creditors who voted, and at least 50% in value of independent creditors who voted, and if no rights of shareholder of any class are altered, the plan is regarded as approved.<sup>55</sup>

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## **ADDITIONAL INFO**

### **1. Fundamental transactions (alter a company)**

Are subject to approval by special resolution.

Fundamental transactions fall into 3 categories:

- Disposals of the majority of a company's assets or undertaking;
- Mergers or amalgamations; and
- Schemes of arrangement

A fundamental transaction will be an affected transaction if the company is a regulated company. A regulated company is:

- A public company;
- A state-owned enterprise (unless exempted); or
- A private company, but only if more than the prescribed percentage of its issued securities has been transferred in the previous 24 months, or the company's MOI expressly provides for it to be treated as a regulated company.

An affected transaction is either:

- A fundamental transaction involving a regulated company;
- An acquisition of multiples of 5 percentages in voting securities;
- A mandatory offer; or
- A compulsory acquisition (so-called squeeze-out transaction)

If a fundamental transaction is also an affected transaction, the Takeover Regulation Panel will have jurisdiction of the transaction as well.

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<sup>54</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 260

<sup>55</sup> Companies and other Business Structures in South Africa, Davis D, Geach W, Mongalo T, Butler D, Loubser A, Coetzee L and Burdette D, page 261

## 2. Persons ineligible or disqualified to be appointed as director:

### Ineligible:

- A juristic person or trust;
- An unemancipated minor or person under a similar legal disability;
- Any person who does not satisfy any required in a company's MOI.

### Disqualified:

- A person who has been prohibited by a court of law from becoming a director;
- A person who has been declared to be a delinquent by a court of law;
- An unrehabilitated insolvent;
- A person who is prohibited in terms of any public regulation from being a director;
- A person who has been removed from an office of trust because of dishonesty;
- A person who has been convicted and imprisoned without the option of a fine for theft, fraud, forgery, perjury.
- A person disqualified in terms of the company's MOI.