THE PROTECTION OF MINORITY SHAREHOLDERS DURING A REORGANISATION OF SHARE CAPITAL WITHIN A COMPANY

by

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1. Introduction

It is a well-known principle of company law that when a person becomes a shareholder of a company, an inherent side-effect thereof is that he agrees to be bound by majority rule. In the ordinary day-to-day running of a company, individual shareholders may be dissatisfied with this general principle and the decisions taken by the majority. The reorganisation of share capital within a company may be somewhat controversial for existing shareholders of the company and could adversely affect their interests within the organisation.

A company can make use of a number of ways to implement a reorganisation of share capital. The reasons behind the company's motivation to do so, however, would differ from case to case. It is also not an anomaly that a reorganisation of existing share capital may cause an acute conflict of the rights and interests of shareholders.[1]

This dissertation will place focus on four of the available methods of reorganisation within a company, and will also examine the appropriate protection mechanisms incorporated into the Companies Act, 2008 (Act 71 of 2008) ("the act") and the remedies available to minority shareholders.

Firstly, this dissertation will critically assess the reorganisation of share capital by way of a scheme of arrangement in terms of section 114 of the act. A scheme of arrangement is a fundamental transaction in terms of the act and as such, consideration needs to be given to a variety of factors when determining and examining shareholder protection. It is important to note that this dissertation is restricted to the internal reorganisation within a single company and will not consider the effects of an exchange of shares during a merger.

[1] Van der Linde "The regulation of conflict situations relating to share capital" 2009 *SA Merc LJ* 33 42.

The second method of share reorganisation which will be examined is a reorganisation by way of a repurchase of shares by a company in terms of section 48 of the act. In dealing with this method, a repurchase of shares will be evaluated in general, as well as more critically with regards to the rights of shareholders during a repurchase.

Thirdly, a reorganisation of share capital could also be implemented by amending the memorandum of incorporation of a company and altering the rights of shares already in issue. Shareholder protection mechanisms and rights in the case of an alteration of the memorandum of incorporation of a company will be examined and discussed in this context.

Lastly, the issuing of shares by a company could create conflict situations between shareholders within the company and could result in a shift in control, as such this means of reorganisation also will be examined.

In addition to the aforementioned methods of reorganisation, this dissertation will also take into account the different prerequisites for each method of reorganisation and look to determine whether these prerequisites seek to act as a form of protection for minority shareholders.

The act, in chapter 7, provides certain general protection mechanisms for minority shareholders. These non-remedy based protections which are available to shareholders in terms of the act will also be examined. These would include providing shareholders with alternative procedures for addressing complaints that they may have[2] as well as enabling them to bring an application to court in order to protect their rights as shareholders.[3] These general remedies are however not the only ones available to shareholders and as such, this dissertation will also consider the appraisal rights available to dissenting shareholders in terms of section 164 of the act, as well as look at relief from oppressive or prejudicial conduct in terms of section 163.

[2] s 156 of the Companies Act 71 of 2008.
[3] s 161 of the Companies Act 71 of 2008.

In conclusion, this dissertation will evaluate whether shareholders are adequately protected during a reorganisation of share capital within a company and also determine whether different mechanisms and levels of protection used in various types of reorganisation procedures are justified.

2. Methods of reorganisation

2.1. Schemes of arrangement

In terms of the act, the board of a company may, unless it is in liquidation or in the course of business rescue proceedings, propose and, subject to obtaining the requisite approvals and adhering to the provisions contained in section 48 of the act (where relevant), implement any arrangement between the company and holders of any class of its securities.[4] Six methods are listed in the act, but this is not an exhaustive list or a *numerus clausus*.[5] The methods mentioned by the act are: a consolidation of securities of different classes; a division of securities into different classes; an expropriation of securities from the holders; exchanging any securities for other securities; a re-acquisition by the company of its securities; or a combination of the aforementioned.[6] However, Latsky says that almost any arrangement between a company and shareholders of a class of securities would be considered to be a scheme of arrangement in the event that the company were to comply with the relevant requirements of the act.[7]

As a result of the dissertation only focusing on the reorganisation of share capital within a company, the method of exchanging a company's securities for the securities of another company will not be considered, as this often relates to the exchange of company shares during a merger. However, within a company, an exchange of securities could also occur,

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[4] s 114(1) of the Companies Act 71 of 2008.
[5] s 114(1) of the Companies Act 71 of 2008. The wording of the section emphasises that companies may propose an arrangement between the holders of any class of its securities by "amongst other things" the methods listed in the act.
[6] s 114(1)(a) – (e) of the Companies Act 71 of 2008.
[7] Latsky "The fundamental transactions under the Companies Act: A report back from practice after the first few years" 2014 *Stell LR* 361 369.

as preference shares could, for example, be exchanged for ordinary shares during a scheme of arrangement.

The examination of schemes of arrangement can be broken into four main subheadings, each of which will be separately analysed, namely: disclosure, approval required, court review/approval and other applicable provisions.

2.1.1. Disclosure

In order to implement a scheme of arrangement, the company is required to retain an independent expert to compile a report to the board of the company on the scheme of arrangement, which report must also be distributed to security holders, and based on this report, security holders can evaluate the proposed transaction in its entirety and make their election to either vote in favour of the scheme or against it.

The independent expert must be sufficiently qualified, and have the relevant experience and competence to understand the type of arrangement proposed, evaluate the consequences of the arrangement and assess the effect of the arrangement on the value of securities and on the rights and interests of a holder of any securities, or a creditor of the company, as well as be able to express opinions, exercise judgment and make decisions independently.[8] The independent expert cannot have any other relationship with the company or with a proponent of the arrangement.[9]

The report should provide security holders with adequate information to enable them to assess the material effects of the proposed arrangement and equip them to make an informed voting decision. It is clear that, regardless of whether it is paid to them or another security holder, security holders may potentially be prejudiced by the repurchase price

[8] s 114(2)(a) of the Companies Act 71 of 2008.
[9] s 114(2)(b) of the Companies Act 71 of 2008.

being either too high or too low, and as such, the report of the independent expert is clearly intended for the benefit of security holders.[10]

It is apparent that this requirement is likely to be expensive for companies as well as time consuming, and may appear to be unnecessary and unfitting in a private company, according to Latsky.[11] Latsky also points out that because the independent expert's report is clearly intended for the benefit of shareholders, it could also be unanimously waived by all shareholders, which would then not be against the public interest.[12] On the other hand, in the event that this requirement is waived, shareholders and directors of the company should be fully informed of the risks thereof and of the rights being waived.[13]

Although not intended for the benefit of creditors, as their specific interests are not addressed therein, in some instances creditors may also be considered as security holders, namely when they are debenture holders, in which case they would also receive the independent expert report.[14]

2.1.2. Approval required

In terms of the relevant approvals required to implement a proposed scheme of arrangement, the provisions of section 115 of the act must be complied with. More specifically, section 115(2)(a) provides that a scheme must be approved by way of a special resolution taken by persons entitled to vote on the matter. A quorum of at least twenty five percent of shareholders must be present, unless a higher percentage is specified in the company's memorandum of incorporation.[15]

[10] Latsky (n7) 369.
[11] Latsky (n7) 370.
[12] Latsky (n7) 371.
[13] Latsky (n7) 371.
[14] Latsky (n7) 371.
[15] s 115(2)(a) of the Companies Act 71 of 2008.

2.1.3. Court approval/review

Despite the special resolution required in terms of section 115(2)(a) having been adopted by shareholders, a company may not proceed with the implementation of the resolution if: (a) the resolution was opposed by at least 15% of the voting rights exercised on that resolution and, within five business days after the vote, any person who voted against the resolution requires the company to seek court approval; or if (b) the court, on an application within 10 business days after the vote by any person who voted against the resolution, grants that person leave to apply to a court for a review of the transaction.[16]

Davids, Norwitz and Yuill, with respect, correctly say that "regulation should strike a balance between encouraging economic activity and prudent risk-taking while appropriately protecting the interests of the many stakeholders in the companies involved, the economy and society at large".[17] Section 115(3) aids the striking of this balance and in itself provides protection to dissenting shareholders, making it obligatory for a company, upon demand by an opposing shareholder, to obtain court approval in the event that the resolution was opposed by at least 15% of the voting rights exercisable on such resolution. In the event that the resolution is opposed by less than 15% of shareholders, the court may grant leave to any person who voted against the resolution to apply to court for a review of the transaction. Section 115(6) of the act advocates that the court will only grant leave in this instance if the court is satisfied that the applicant is acting in good faith, appears to be prepared and is able to sustain the court proceedings and has alleged facts, which if proven, will support an order in terms of section 115(7).[18]

The act specifically provides that if the resolution requires approval by a court, the company must either apply to the court for approval within ten days, or disregard the resolution and treat it as a nullity.[19] Should the company decide to approach the court, or

[16] s 115(3) of the Companies Act 71 of 2008.
[17] Davids, Norwitz and Yuill "A microscopic analysis of the new merger and amalgamation provision in the Companies Act 71 of 2008" 2010 *Acta Juridica* 337 338.
[18] s 115(3) and s 115(6) of the Companies Act 71 of 2008.
[19] s 115(5) of the Companies Act 71 of 2008.

if a shareholder does so under the provisions of paragraph 115(3)(b) of the act, the court may set aside the resolution only in the event that it is "manifestly unfair to any class" of shareholders, or if the vote was "materially tainted".[20]

According to Davids, Norwitz and Yuill, the protection provided by section 115(2) (i.e. the requirement of a special resolution being obtained) generally does not exist in other jurisdictions and is unique to South Africa.[21] They also opine that this section is considered to be a suitable protection where people are more restrained in bringing matters to the courts in order to protect their rights.[22]

According to Luiz, schemes of arrangement began to be used to eliminate minority shareholders, thereby effecting a takeover of the company, thus resulting in the main concern whether minority shareholders were being adequately protected.[23] Latsky opines that the act strikes an equitable balance between the rule of the majority and the protection of minority shareholders in the implementation of fundamental transactions.[24] Davids, Norwitz and Yuill also recognise that "a balance needs to be struck between protecting minority shareholders, on the one hand, and facilitating economically advantageous transactions and not unduly empowering minority shareholders to hold up transactions against the will of the majority on the other".[25] Henochsberg states that the object of the relevant scheme must be the affecting of the respective rights and obligations of the company and the holders of its securities.[26]

As a result of these rights of shareholders being so affected and as a result of the equitable balance aforementioned, upon notifying the company of the intention to oppose the special resolution and being present at the meeting and voting against the resolution, individual shareholders are entitled to exercise their appraisal rights in terms of section

[20] s 7(a) and (b) of the Companies Act 71 of 2008.
[21] Davids, Norwitz and Yuill (n 17) 347.
[22] Davids, Norwitz and Yuill (n 17) 347.
[23] Luiz "Using a scheme of arrangement to eliminate minority shareholders" 2010 *SA Merc LJ* 443 444.
[24] Latsky (n 7) 362.
[25] Davids, Norwitz and Yuill (n 17) 347.
[26] Delport, Vorster, Burdette, Esser and Lombard *Henochsberg on the Companies Act 71 of 2008* (2014) 410.

164 in the event that they are opposed to the scheme being implemented.[27] The appraisal right of dissenting shareholders will then allow for those shareholders to have their shares bought out by the company in cash, at a price reflecting the fair value of the shares.[28] By allowing for the application of appraisal rights, shareholders are protected to the extent that dissenting shareholders can make use of the opportunity to be "bought-out" by the company and need not be subject to the reorganisational implications of the scheme of arrangement on the company. The use and application of appraisal rights as a remedy in the reorganisation of share capital within a company will be discussed in more detail later in this dissertation.

2.1.4. Other applicable provisions

In addition to the above, it is important to note that if a company is regarded as a regulated company in terms of the act, a scheme of arrangement in terms of section 114 would be classified as an "affected transaction" in terms sections 117 and 118 of the act. An "affected transaction" is described to include a scheme of arrangement between a regulated company and its shareholders (contemplated in section 114), and is subject to section 118(3).[29] The importance of the classification as an affected transaction is that the transaction must be regulated by the Takeover Regulation Panel. According to the provisions of section 119 of the act, the Takeover Regulation Panel must regulate any affected transactions in order to "a) ensure the integrity of the marketplace and fairness to the holders of securities of regulated companies; b) ensure the provision of i) necessary information to holders of securities of regulated companies, to the extent required to facilitate the making of fair and informed decisions; and ii) adequate time for regulated companies and holders of their securities to obtain and provide advice with respect to offers; and c) prevent actions by a regulated company designed to impede, frustrate, or defeat an offer, or the making of fair and informed decisions by the holders of that company's securities".[30]

[27] s 115(8) of the Companies Act 71 of 2008.
[28] Cassim FHI, Cassim MF, Cassim R, Jooste R, Shev J and Yeats J *The Law of Business Structures* (2012) 430.
[29] s 117(1)(c)(iii) of the Companies Act 71 of 2008.
[30] s 119(1)(a) – (c) of the Companies Act 71 of 2008.

The provisions of section 119(2) go on to enhance this protection and provide that "the Panel must regulate any affected transaction or offer, and the conduct of the parties in respect of any such transaction or offer, in a manner that promotes the objects set out in subsection (1) and, without limiting the generality of that subsection, ensures a) that no person may enter into an affected transaction unless that person is ready, able and willing to implement that transaction; b) that all holders of i) any particular class of voting securities of an offeree regulated company are afforded equivalent treatment; and ii) voting securities of an offeree regulated company are afforded equitable treatment, having regard to the circumstances; c) that no relevant information is withheld from the holders of relevant securities; and d) that all holders of relevant securities i) receive the same information from an offeror, potential offeror, or offeree regulated company during the course of an affected transaction, or when an affected transaction is contemplated; and ii) are provided sufficient information, and permitted sufficient time, to enable them to reach a properly informed decision".[31]

Chapter 5 of the Companies Regulations, 2011 ("the regulations") governs fundamental transactions and comprises the takeover regulations. An example of the enhanced protection to shareholders enforced by the takeover regulations is that a regulated company must, in terms of regulation 108, appoint members of the board to constitute an independent board of directors which must provide an opinion on the fairness and reasonability of the transaction consideration.[32] This independent board should comprise of at least three independent directors,[33] all of which would need to satisfy the independence requirements set out in regulation 108(8). Members of the independent board would also need to have requisite knowledge, as set out in regulation 109, and must: (a) take reasonable steps to receive all necessary information to come to a fully informed opinion concerning an offer and prepare it for relevant securities holders; (b) meet with appointed advisors to be briefed on all details of the offer; (c) resist being hasty

[31] s 119(2) of the Companies Act 71 of 2008.
[32] Regulation 110 of the Companies Regulations, 2011.
[33] Regulation 108(9) of the Companies Regulations, 2011.

and pressured by time deadlines, allowing enough time to discharge all duties and responsibilities; and (d) become properly informed of offeree regulated company's value per security, or where relevant, the offeror company's value per relevant security.[34]

The opinion of the independent board must comply with the requirements as set out in regulation 110, which includes, *inter alia*, performing a valuation on the offeree regulated company's securities (if applicable) and forming a clear basis for the expression of an opinion to relevant securities holders dealing with value and price compared to the consideration offered.[35]

In addition, Henochsberg submits that the General Principles in paragraph 2 Section C of the Securities Regulation Code on Takeovers and Mergers as promulgated under GN R290 of 18 January 1991, still apply with regard to affected transactions. These principles would include, *inter alia*, that "all holders of the same class of securities of an offeree company shall be treated similarly by an offeror", that "holders of relevant securities shall be given sufficient information and advice to enable them to reach a properly informed decision and shall have sufficient time to do so. No relevant information shall be withheld from them" and that "rights of control shall be exercised in good faith and the oppression of a minority is unacceptable".[36]

It is thus apparent that the function of the Takeover Regulation Panel and the takeover regulations is essentially to enhance shareholder protection in regulated companies during fundamental transactions.

2.2 The repurchase of shares

The act, in section 48, provides for the acquisition by a company of its own shares (also referred to as a "repurchase of shares" or a "share buy-back"), as well as the acquisition

[34] Regulation 109 of the Companies Regulations, 2011.
[35] Regulation 110(3)(a) and 110 (4) of the Companies Regulations, 2011.
[36] Delport et al (n 26) 424.

of a subsidiary company of shares in its holding company. The definition of a "distribution" in section 1 of the act states that a distribution includes "consideration for the acquisition by the company of any of its shares, as contemplated in section 48; or by any company within the same group of companies, of any shares of a company within that group of companies". As such, an acquisition by a company of its own shares for consideration must comply with the provisions set out in section 46 of the act, as well as those of section 48.

It is important to clarify from the outset, however, that a company cannot actually "acquire" its own shares, as a company cannot acquire rights against itself.[37] Henochsberg concurs and says that a company cannot own shares in itself and as such (both in terms of common law and the act) the shares acquired by the company will be cancelled. This is because the meaning of the word "acquire" is to obtain ownership and a company cannot own shares in itself.[38] If one has regard to section 35(5) of the act, it is evident that shares that are issued by the company and which are later acquired by the company have the same status as those that are authorised but not issued, as do shares that are surrendered to the company in the exercise of appraisal rights.

2.2.1 General provisions, subsidiary companies and thresholds

Section 48(2) provides that the board of a company may determine that a company will acquire a number of its own shares or the board of a subsidiary company may determine that it will acquire shares in its holding company. The act sets out certain specific requirements in this regard. Firstly, in aggregate, subsidiaries of a company may not hold more than ten percent of the number of issued shares of the company, and secondly, no voting rights attached to those shares held by the subsidiaries may be exercised while so held.[39]

[37] Cassim et al (n 28) 193.
[38] Delport et al (n 26) 204.
[39] s 48(2)(b)(i) and (ii) of the Companies Act 71 of 2008.

The fact that these shares held by subsidiaries have no voting rights, allows for other shareholders to possibly become controlling shareholders, and may push them over the 35% threshold, thus triggering a mandatory offer in terms of section 123 of the act.[40]

Section 123 of the act applies if a regulated company re-acquires any of its voting securities contemplated in section 48 or in terms of a scheme of arrangement as set out in section 114, and before that acquisition a person was able to exercise less than the prescribed percentage of all the voting rights attached to securities of that company, and, as a result of the acquisition, together with any other securities of the company already held by the person, they are able to exercise at least 35% of all the voting rights attached to securities of that company.[41] This also applies when persons acting alone, or in concert, have acquired 35% or more of the voting rights of the securities issued by a regulated company.[42]

In the event of this 35% threshold being breached, such person must give notice to the remaining securities holders that they are in a position to exercise at least 35% of all voting rights of the company and that they offer to acquire any remaining securities in accordance with the act and regulations. One month after the notice being given, such person must deliver a written offer to the holders of remaining securities to acquire such remaining securities.[43]

There are also other general requirements applicable to both the acquisition of a company of its own shares, and that of a subsidiary in its holding company. The first is that the company is not permitted to acquire its own shares, and a subsidiary is not permitted to acquire shares in its holding company, if the only remaining shares in issue would then be shares held by one or more subsidiaries of the company, or convertible or redeemable shares.[44]

[40] s 123 of the Companies Act 71 of 2008.
[41] s 123(2)(a) to (c) of the Companies Act 71 of 2008.
[42] s 123(2)(a)(i) of the Companies Act 71 of 2008.
[43] s 123(3) and (4) of the Companies Act 71 of 2008.
[44] s 48(3) of the Companies Act 71 of 2008.

The second general requirement, to be found in section 48(8), is split over two parts and provides: (a) that when a decision is made by the board of a company to repurchase its own shares and any shares are to be acquired from a director (or prescribed officer) of the company or a person so related to her, the decision by the board is not sufficient and the decision must be approved by a special resolution of shareholders; and (b) that a decision by the board to acquire a number of its own shares will be subject to the requirements of sections 114 and 115 of the act, which pertain to schemes of arrangement, if the transaction (considered alone or together with an integrated series of transactions) involves the acquisition by the company of more than five percent of the issued shares of any particular class of the company's shares.[45]

Latsky says that an important question to consider in this case is whether such a buy-back can only be done by way of a scheme of arrangement, or alternatively, whether the repurchase is only subject to the requirements of a scheme of arrangement, which for example, would include obtaining the independent expert report and shareholder approval. He goes on to say that the answer is not clear from the act.[46]

According to the commentary on the act by Henochsberg, "there are any number of interpretations in respect of sub-s (8). It can be argued that paras (a) and (b) must be interpreted conjunctively, i.e. if the acquisition is from directors and it is more than 5%, the acquisition must be approved by special resolution and it must be done by way of ss 114 and 115." He then goes on to say that "two possible interpretations [of section 48(8)(b)] are that if 5% of the shares of a particular class are acquired, it must be done by way of an acquisition in terms of ss 114 and 115, while it is also possible that what is intended is that s 115, in addition to the para (a) special resolution will apply in all instances if the 5% threshold is reached, but that s 114 will only apply, in addition to the para (a) special resolution and s 115, if the acquisition is done by way of s 114".[47] This

[45] s 48(8) of the Companies Act 71 of 2008.
[46] Latsky (n 7) 380.
[47] Delport et al (n 26) 204.

renders the provision somewhat confusing. The authors of *Contemporary Company Law* state that "[i]t seems that the distinction is that s 48 is designed to deal with casual, or one-off, decisions to re-acquire shares on a scale that does not amount to a restructuring of the company's capital structure, while s 114 is designed to address wholesale fundamental changes to the company's capital structure".[48] I tend to agree with this conclusion.

2.2.2. Approval required and disclosure:

The drafters of the act clearly intended that something more should be required in order to protect shareholders in the event of a repurchase of shares and provided therefore by the inclusion of the requirement of a *special* resolution, and not only an *ordinary* resolution of shareholders, to approve a repurchase in terms of section 48(8)(a). The requirement of a special resolution implies that the act seeks to protect shareholders in this provision and is aimed at preventing an abuse of powers by directors who may use their positions to benefit themselves.[49]

Van der Linde opines that "a resolution, either by an ordinary or special majority, does not protect dissenting shareholders because they are bound by the decision of the majority. However, the disclosure requirements that usually apply to resolutions provide indirect protection. The effectiveness of a resolution as [a] protection mechanism is enhanced if voting restrictions are imposed on shareholders whose shares are being acquired in a consensual selective offer".[50] She also further advises that a useful measure against abuse would be disclosure, either before or after a transaction.[51]

Henochsberg has said that section 48(8) "may go some way to protect shareholders in a company from abuse of power by the directors, as other reacquisitions are not subject to

[48] Cassim FHI, Cassim MF, Cassim R, Jooste R, Shev J and Yeats J *Contemporary Company Law* Second Edition (2012) 303.
[49] Cassim et al (n 48) 304.
[50] Van der Linde "Share repurchases and the protection of shareholders" 2010 *TSAR* 288 305.
[51] Van der Linde (n 50) 305.

a special resolution".[52] The commentary also suggests that without the required approval from shareholders, any agreement based on a board resolution without the required approval should only be unenforceable, and not be rendered void or invalid.[53]

Repurchases are open to many abuses due to the fact that they are considered to be a distribution of the company's assets, as well as a reorganisation of the issued share capital of a company.[54] Each of these carries with it its own benefits and shortcomings. Notwithstanding this, there are many advantages to allowing a company to acquire its own shares, and, among other reasons, "it is particularly useful in relation to employee share schemes enabling the shares of employees to be repurchased on their ceasing to be employed by the company; it provides a means to avert a hostile take-over; it provides a means whereby a shareholder, or the estate of a deceased shareholder, in a company whose shares are not listed, can find a buyer".[55] According to Seligson, share repurchases are important in company reorganisations, such as with black empowerment and management buy-out transactions and when used in relation to listed companies they could often have the effect of increasing the company's share price by reducing the actual number of shares in issue and also thereby increasing the net asset value per share of this reduced number of issued shares.[56]

If one considers the provisions of section 46(1) and section 48 of the act, a board of directors does not require shareholder authorisation to make a distribution pursuant to a repurchase, and a board resolution to that effect would suffice unless a board resolution is not required, such as in the case of the acquisition being pursuant to an existing legal obligation of the company or an order of court. Cassim states that shareholders are

[52] Delport et al (n 26) 201.
[53] Delport et al (n 26) 201.
[54] Cassim et al (n 48) 296; Van der Linde (n 1) 46. Also see Delport et al (n 26) 201 where it is stated that "the 'abuse of control' elements in the latter sections, have, to a large extent, been excluded from s48 as only a board resolution, as opposed to a resolution of shareholders, is required to effect an acquisition. The acquisition can also be in respect of selected shareholders, and not pro rata all shareholders, which increases potential abuse."
[55] Cassim et al (n 48) 291.
[56] Seligson "Share Buy-Backs under the Companies Act: The Devil is in the Detail!" 2011 *Business Tax & Company Law Quarterly* 1.

generally excluded from deciding on a buy-back in terms of the act.[57] This is thought-provoking because it begs the following questions, “Why is shareholder approval only required when repurchasing shares from directors or related persons?”, “Why is shareholder approval not always required when it comes to repurchases?” and “Does section 48(8) provide sufficient protection to shareholders when a company repurchases shares from directors or related persons?” In addition to the general exclusion of shareholders, there is no requirement contained in the act that shareholders need to be informed of the merits and demerits of an offer to acquire their shares, and “no special safeguards have been enacted”.[58] Seligson says that due to share buy-backs being the exclusive preserve of the board of directors under the act, shareholders might not even know of the buy-back until only after it has occurred.[59]

Van der Linde conducted a comparative study to analyse the protection of shareholders when a company repurchases its own shares in the United Kingdom, New Zealand, the United States and South Africa.[60] Important to note is that van der Linde wrote this article before the act being amended in 2011, which included the insertion of section 48(8) into the act. Her conclusions are interesting in that two main approaches were recognised from the study. In the Commonwealth jurisdictions, the procedure for repurchases is prescribed by statute and focuses on proper disclosure and authorisation. In the United States however, shareholder protection is based on general principles including director liability and abuses associated with particular repurchases during takeovers are regulated at a federal level.[61] New Zealand and the United Kingdom rely on disclosure of the terms of the repurchase to shareholders. New Zealand also requires authorisation which is done through permission in the company’s constitution versus the shareholder resolutions which are required in the United Kingdom. It is submitted that South Africa, with the addition of section 48(8) to the act, now follows the Commonwealth jurisdiction approach in that disclosure and authorisation are required in certain instances.[62]

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[57] Cassim et al (n 28) 193.
[58] Cassim et al (n 48) 303.
[59] Seligson (n 56) 1.
[60] Van der Linde (n 50) 289 – 290.
[61] Van der Linde (n 50) 306.
[62] For a full discussion on the findings of the comparative study, see Van der Linde (n 50) 288 – 308.

2.2.3. Court approval/review

In the event that the a repurchase of shares in terms of section 48(8)(b) is subject to the provisions of section 114 and 115 of the act, the procedure for court approval or review in terms of section 115(3) to 115(7) becomes applicable. As discussed under the first method of reorganisation above, despite the special resolution required in terms of section 48(8)(a) having been adopted by shareholders, a company may not proceed with the implementation of the resolution if: (a) the resolution was opposed by at least 15% of the voting rights exercised on that resolution and, within five business days after the vote, any person who voted against the resolution requires the company to seek court approval; or if (b) the court, on an application within 10 business days after the vote by any person who voted against the resolution, grants that person leave to apply to a court for a review of the transaction.[63]

In the event of court approval being required in terms of section 115(3)(a), the company must either apply to the court for approval within 10 business days after the vote and bear the costs of the application, or treat the resolution as a nullity.[64] Should a court review be requested in terms of section 115(3)(b), the court may only grant such review if it has satisfied itself that the applicant is acting in good faith, appears to be prepared and able to sustain the proceedings and has alleged facts, which if proved, would support an order in terms of section 115(7).[65] The court may order the resolution to be set aside only in the event that it is manifestly unfair to any class of securities holders, or if the vote taken by shareholders was tainted materially by a conflict of interest, inadequate disclosure, a significant and material procedural irregularity or a failure to comply with the provisions of the act, the company's memorandum of incorporation or any other rules of the company.[66]

[63] s 115(3) of the Companies Act 71 of 2008.
[64] s 115(5)(a) and (b) of the Companies Act 71 of 2008.
[65] s 115(6) of the Companies Act 71 of 2008.
[66] s 115(7) of the Companies Act 71 of 2008.

Clearly the application of the provisions of sections 114 and 115 enhance shareholder protection in the case of a repurchase being subject to these provisions in terms of section 48(8)(b).

2.2.4 The JSE Listings Requirements

The Listings Requirements of the JSE Limited ("Listings Requirements") requires shareholder approval for repurchases, and distinguishes between different types of repurchases, providing both for specific and general repurchases. The kind of approval is linked to the kind of repurchase involved, as specific approval is required in the case of a specific repurchase, whereas general approval is required in the case of a general repurchase.[67]

In the case of a specific repurchase, an offer is made to shareholders who are specifically named and also includes the grant of an option in terms of which an issuer may or will be required to repurchase its securities in future.[68] The requirements for a company making a specific offer to shareholders is that it must comply with section 4 and section 48 of the act, authorisation to effect a specific repurchase must be contained in the company's memorandum of incorporation, and the company must obtain approval in terms of a special resolution excluding, in the case of a specific offer, the votes of any shareholder and its associates that would be participating in the repurchase. The company also requires a resolution by the board of directors stating that it has authorised the repurchase, that the company has passed the solvency and liquidity test and that, since the test was performed, there have been no material changes to the financial position of the company.[69]

The provisions of paragraph 11.25 of the Listings Requirements require that a company publish an announcement detailing the full terms of the repurchase and also stating that

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[67] Van der Linde (n 50) 288.
[68] par 5.69 of the *JSE Limited Listings Requirements*.
[69] par 5.69(a), (b), (c) and (d) of the *JSE Limited Listings Requirements*.

a circular containing all the details of the repurchase will be dispatched to shareholders. The board of directors must obtain a fairness opinion if the repurchase is subject to the provisions of paragraph 5.69(e) of the Listings Requirements, being that the transaction constitutes a related party transaction, or if the price at which the securities are purchased is at a premium to the weighted average traded price of such equity securities measured over the 30 business days prior to the date that the price of the repurchase is agreed in writing between the issuer and the party selling the securities.[70] The repurchase will then be subject to the inclusion of a statement by the board of directors in the circular confirming whether the repurchase is fair insofar as the shareholders of the company are concerned and that the board of directors has been advised by an independent expert acceptable to the JSE.

With regards to a general repurchase in terms of the listings requirements, the same requirements must be met. Authority to effect a general repurchase must be granted by shareholders by way of a special resolution at the company's annual general meeting, or at a general meeting and such authority will be valid for a period of fifteen months or until the next annual general meeting, whichever is the earlier.[71] There are certain limitations that apply in respect of a general repurchase for a listed company, in that general repurchases in any one financial year must be less (or equal to) twenty percent of the total issued share capital of the company,[72] and repurchases may not be made at a price greater than ten percent above the weighted average of the market value for the securities for the previous five business days.[73] General prohibitions also apply in terms of specific and general repurchases by a company, and where a company is in a prohibited period (being a financial or cautionary closed period or any period in which there exists a matter of any kind constituting price sensitive information), the company is not permitted to repurchase its shares unless it has a share repurchase programme in place where dates and numbers of shares to be traded are fixed and have been provided to the JSE prior to the commencement of the prohibited period and an independent third party has been

[70] par 5.69(e) of the *JSE Limited Listings Requirements.*
[71] par 5.72(c) of the *JSE Limited Listings Requirements.*
[72] par 5.68 of the *JSE Limited Listings Requirements.*
[73] par 5.72(d) of the *JSE Limited Listings Requirements.*

instructed to execute the repurchase programme prior to the commencement of the prohibited period.[74]

Van der Linde argues that these procedural requirements prescribed for the repurchase of listed shares by the JSE Limited are more successful than those prescribed by the previous act.[75] It is clear from the above that the requirements and prohibitions prescribed by the Listings Requirements impose a heavier obligation upon listed companies to effect a repurchase of share capital, which include the release of an announcement and the distribution of a circular to shareholders, as well as special resolutions by shareholders, depending on the circumstances in each case.

2.3 Amendment of the memorandum of incorporation

According to section 16 of the act, a company's memorandum of incorporation may be amended in three ways. Firstly this may be done in compliance with a court order (which must be effected by a company's board and does not require a special resolution of shareholders), secondly by the board of directors of a company in the manner contemplated in section 36(3) and (4) of the act, and thirdly at any other time if a special resolution to amend the memorandum of incorporation is either proposed by the board, or shareholders exercising at least 10% of the voting rights to be exercised on such resolution and if such resolution is adopted at a shareholders meeting.[76] The act further goes on to say that a company's memorandum of incorporation may provide other, different requirements for an amendment.[77] This is also clear from the wording above providing that "*except to the extent that a company's memorandum of incorporation provides otherwise*", the board may amend the company's memorandum of incorporation.

[74] par 5.69(h) and par 5.72(h) of the *JSE Limited Listings Requirements*.
[75] Van der Linde (n 50) 307.
[76] s 16(1) of the Companies Act 71 of 2008.
[77] s 16(2) of the Companies Act 71 of 2008.

2.3.1. Amendments by special resolution

The amendments to be made by way of a special resolution by shareholders can take the form of either substituting the current memorandum of incorporation for a new one, making alterations to the current memorandum of incorporation by changing the name of the company, by deleting, altering or replacing any of the provisions in the memorandum of incorporation, by the insertion of any new provisions therein, or by making a combination of these changes. [78]

One of the ways in which a company could effect a reorganisation of share capital would be by amending the rights of different classes of shareholders in terms of its memorandum of incorporation. The act sets out the criteria for authorisation of shares, and in section 36, provides that a company's memorandum of incorporation must set out certain details relating to shares, including share classes, the number of shares which the company is authorised to issue, as well as setting out the preferences, rights, limitations and other terms associated with the specific class of shares.[79] The act also states that the authorisation and classification of shares and the other terms associated with each class of shares, which are set out in a company's memorandum of incorporation, may be changed only by way of an amendment of the memorandum of incorporation by special resolution of the shareholders or by the board of the company (as contemplated in section 36(3) of the act), except to the extent that the memorandum of incorporation provides otherwise.[80]

2.3.2. Applicable remedies

Section 37(8) of the act provides that in the case of the memorandum of incorporation being amended to materially and adversely alter the preferences, rights, limitations or other terms of a class of shares, then any holder of such shares, provided that they

[78] s 16(5) of the Companies Act 71 of 2008.
[79] s 36(1) of the Companies Act 71 of 2008.
[80] s 36(2) of the Companies Act 71 of 2008.

notified the company in advance of the intention to oppose the resolution to amend the memorandum of incorporation and were present at the meeting and voted against the resolution, is entitled to seek relief in terms of section 164 of the act. As such, it would appear that a shareholder could only notify a company of its intention to oppose a resolution and actually vote against a resolution if a resolution was indeed a pre-requisite for the amendment to the memorandum of incorporation. In the case of board amendments to the memorandum of incorporation in terms of section 36(3) and (4), no shareholder resolution is required, and as such, the appraisal remedy cannot be relied upon in such cases.[81]

According to Beukes, minority shareholders seeking relief after an amendment to the memorandum of incorporation by way of special resolution which effects changes to share rights, can do so either by way of the appraisal remedy in section 164 or by way of the oppression remedy set out in section 163.[82] Although both remedies afford protection, the outcomes of each would differ. In terms of the appraisal remedy, the shareholder's shares would be bought by the company, whereas in the case the oppression remedy, a number of outcomes may occur, including "an order restraining the conduct complained of, an order to regulate the company's affairs by directing the company to amend its memorandum of incorporation or to create or amend a unanimous shareholder agreement, an order directing an issue or exchange of shares, and an order directing the company or any other person to restore to a shareholder any part of the consideration that the shareholder paid for shares, or pay the equivalent value".[83] It appears that relief to be offered in respect of the oppression remedy is much wider than that of the appraisal remedy.

It is, however not to say that a shareholder would automatically be afforded protection by these remedies as "it is not the amendment of the memorandum of incorporation in itself

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[81] Van der Linde "The regulation of share capital and shareholder contributions in the Companies Bill" 2009 *TSAR* 46.
[82] Beukes "An introduction to the appraisal remedy as proposed in the Companies Bill: Triggering actions and the differences between the appraisal remedy and existing shareholder remedies" 2010 *SA Merc LJ* 482.
[83] Beukes (n 82) 482.

that triggers the appraisal remedy, but the amendment of the memorandum of incorporation pursuant to the alteration of the share rights".[84] The same is true for the oppression remedy as the conduct by the board, or the conduct by shareholders in the case of a special resolution, in making the amendment to the memorandum of incorporation must have been oppressive, unfairly prejudicial to or unfairly disregard the interests of the shareholders.

Henochsberg points out that there is an evident overlap between the remedies provided in sections 163 and 164 of the act if shareholder rights are affected by an amendment to the memorandum of incorporation.[85] An analysis of these remedies will follow later in this dissertation.

2.3.3. Amendments by the board

In addition to the possible amendments to be made by shareholders, the board of directors of a company is granted limited powers to make amendments to the company's memorandum of incorporation. The act in section 36(3), except to the extent that the company's memorandum of incorporation provides otherwise, allows for the board of a company to also increase or decrease the number of authorised shares of any class of shares and to reclassify any classified shares that have been authorised but not issued, classify any unclassified shares that have been authorised but are not issued and to also determine the preferences, rights, limitations or other terms of shares in a class.[86] Should the board of a company wish to make these aforementioned changes, the company must file a Notice of Amendment of its memorandum of incorporation, setting out the changes effected by the board.[87]

The effect of these sections is that the board of a company may, through section 36(3), decide to alter the company's memorandum of incorporation without consulting

[84] Beukes (n 82) 480.
[85] Delport et al (n 26) 568.
[86] s 36(3) of the Companies Act 71 of 2008.
[87] s 36 (4) of the Companies Act 71 of 2008.

shareholders and without a special resolution of shareholders, but only in certain specific and limited circumstances. Shareholders may not even be aware of such changes until they have sight of the Notice of Amendment which must be filed in terms of section 36(4), if ever.

A question which arises is whether shareholder rights may be materially adversely effected by such an amendment to the memorandum of incorporation. It is understandable that, should the board decide to increase the number of authorised shares in a class and those shares are subsequently issued, the rights of the holders of those shares could be largely diluted and the weight of the existing shareholders voting rights would also be significantly affected, not to mention their distribution prospects and rights to return of capital.[88] Van der Linde advocates that by allowing the board power to increase the authorised share capital will increase flexibility in terms of the act, but at the same time decrease the protection of shareholders.[89] However, if these shares are merely authorised and not issued, would this change the rights or terms of pre-existing shares? The answer is no.[90] An increase of authorised share capital does not result in a change in preferences, rights, limitations or other terms of existing shares, however it may affect shareholder interests.[91]

2.4. Issuing of further shares

The power of a company to issue shares is imperative for many reasons, one of which being that shares are used by companies to acquire capital.[92] This power to issue share capital is also important for existing shareholders, as, according to Delport, it could be used by the company to change the current shareholding and result in an upset of the balance of control within the company with regard to existing shareholders or could even shift control to persons outside the company who were not shareholders before the

[88] Van der Linde (n 1) 42.
[89] Van der Linde (n 81) 44. Note that this article was based on the Companies Bill 2008 and not on the Companies Act 71 of 2008.
[90] Van der Linde (n 81) 46.
[91] Van der Linde (n 81) 46.
[92] Delport "Share Issues and Shareholder Protection" 2013 *De Jure* 1056.

issue.[93] A significant dilution of shareholder interests can occur and the rights which attach to the new shares may affect voting rights of existing shareholders or distribution prospects.[94] It would thus appear to be vital that the powers of the board are adequately regulated and that the abuse thereof is restricted.[95] Van der Linde submits that these problems can be addressed by limiting the number of additional share which may be issued, maintaining the balance of power through pre-emptive rights and by subjecting shares issues to shareholder approval.[96]

2.4.1. Powers and approvals

The issuing of shares of a company is governed by section 38 of the act which provides that the company's board may resolve to issue shares at any time, but may only do so within the classes, and to the extent that the shares have actually been authorised by the company's memorandum of incorporation (in accordance with the provisions in section 36 of the act).[97] The company can also issue shares which have not yet been authorised or which are in excess of the number of authorised shares of any particular class but this issuance must be retroactively authorised in accordance with section 36 within sixty days after the issuance date.[98] If such a resolution is not adopted when put to a vote, the share issue will be a nullity to the extent that it exceeds the authorised share capital and the company will have to return to any person the fair value of the consideration received by the company in respect of that share issue to the extent of its nullification together with interest thereon.[99] Any certificate which evidences the shares so issued and nullified and any subsequent entry into the company's share register will be null and void.[100]

[93] Delport (n 92) 1056.
[94] Van der Linde (n 81) 42.
[95] Delport (n 92) 1065.
[96] Van der Linde (n 81) 42.
[97] s 38 (1) of the Companies Act 71 of 2008.
[98] s 38(2) of the Companies Act 71 of 2008.
[99] s 38(3)(a) and (b) of the Companies Act 71 of 2008.
[100] s 38(c) of the Companies Act 71 of 2008.

Delport opines that, by the wording of section 36, pertaining to the authorisation and classification of shares, the board is provided with virtually complete power over the share capital of the company.[101] The provisions of section 38(2) also allow a company to retroactively authorise shares in the event that they were issued in excess of the authorised amount.[102] Henochsberg says that section 38(2) implies that both shareholders and the board have concurrent powers to ratify the authorisation, unless the board's authority to authorise shares in accordance with section 36(2) has been excluded or limited by the company's memorandum of incorporation.[103] As section 36 of the act does not allow for retroactive authorisation, Henochsberg submits that the intention of the act is that the company's memorandum of incorporation must be amended in order to increase the authorised share capital.[104]

2.4.2. Approval required

Delport states that both qualitative and quantitative restrictions are imposed on the power to issue shares in the form of sections 41(1) and 41(2), respectively.[105]

Section 41 regulates shareholder approval for the issuing of shares and in subsection 1 provides that if shares, securities, options or rights are issued to a (a) director, future director, prescribed officer or future prescribed officer of the company; (b) person related or inter-related to the company, or to a director or prescribed officer of the company; or (c) nominee of a person contemplated in paragraph (a) or (b), then the issuance must be approved by a special resolution of the shareholders of the company.[106]

Subsection 1 does not apply however, if the issue of shares, securities or rights is (a) pursuant to an underwriting agreement; (b) in the exercise of pre-emptive rights; (c) in proportion to existing holdings on the same terms and conditions as have been offered to

[101] Delport (n 92) 1060.
[102] s 38(2) of the Companies Act 71 of 2008.
[103] Delport et al (n 26) 172
[104] Delport et al (n 26) 172.
[105] Delport (n 92) 1061.
[106] s 41(1) of the Companies Act 71 of 2008.

all shareholders of the company or a particular class; (d) pursuant to an employee share scheme; or (e) pursuant to an offer to the public.[107]

Furthermore, the act provides in section 41(3) that an issue of shares, requires shareholder approval by special resolution if the voting power of the shares to be issued in a transaction or series of transactions is equal to or greater than 30% of the voting power of all the shares of that class held by shareholders immediately before the transaction(s).[108] As the act does not allow for a special resolution in a class of shares, it can be assumed that shareholders in a class or classes can in fact take the special resolution to the detriment of a particular class as the special resolution must be taken by all shareholders.[109]

2.4.3. Director liability and pre-emptive rights

The act does provide protection mechanisms in the case of share issues. The first is that the act, in section 38(3)(d), provides that a director will be held liable if the director was present at the meeting at which the board approved the shares (or participated in the making of such decision by acting other than at a meeting in accordance with section 74 of the act), and the director failed to vote against the issue of shares, well knowing that the shares had not been authorised in accordance with section 36 of the act.[110] The extent of the directors liability herein is set out in section 77(3)(e)(i) of the act, which specifically provides for a director to be held liable for any loss, damages or costs sustained by the company as a direct or indirect consequence of a director having actually been present at a meeting or participating in the making of a decision in terms of section 74 (directors acting other than at a meeting) and failing to vote against the issuing of unauthorised shares, despite knowing that the shares were not authorised in accordance with section 36 of the act.[111]

[107] s 41(1) of the Companies Act 71 of 2008.
[108] s 41(3) of the Companies Act 71 of 2008.
[109] Delport (n 92) 1062 and Van der Linde (n 1) 48.
[110] s 38(d) of the Companies Act 71 of 2008.
[111] s 73(3)(e)(i) of the Companies Act 71 of 2008.

Secondly, the act also provides for pre-emptive rights in section 39(2) which provides that when a private company proposes to issue any shares (except for shares issued in terms of options or conversion rights or where capitalisation shares are issued), each shareholder is entitled, before any other person who is not a shareholder, to be offered and to, within a reasonable period, subscribe for a percentage of those shares to be issued equal to the voting power of that shareholder's general voting rights immediately before the offer was made.[112] A valid criticism of the use of pre-emptive rights as a protection mechanism is that they depend in the financial ability of the shareholder to afford making a further contribution towards the company.[113] This may not always be fair to shareholders based on their current financial standings.

3. Shareholder protection mechanisms

In addition to certain non-remedy based protections such as disclosure to shareholders, the requirement of ordinary and special resolution and the reliance upon director fiduciary duties provided for in section 76 of the act, the act also provides protection mechanisms to shareholders which are distinguishable from the actual remedies available in the act which may be used by shareholders. These protection mechanisms can be found in chapter 7 of the act. Most notably, section 156 of the act provides shareholders with alternative procedures for addressing any complaints which they may have and also enables them to secure their rights. The section provides that a person may seek to enforce any provision or right in terms of the act, a company's memorandum of incorporation or rules, or a transaction or agreement and my also seek to address an alleged contravention of the act by either making use of alternative dispute resolution, applying to the Companies Tribunal for adjudication, applying for alternative relief to a High Court with jurisdiction, or by filing a complaint with either the Takeover Regulation Panel, or the Companies and Intellectual Property Commission, whichever is relevant and applicable.

[112] s 39(2) of the Companies Act 71 of 2008.
[113] Van der Linde (n 81) 42.

As such, a shareholder whose rights were adversely affected by a reorganisation of shares in a company, either by way of a scheme of arrangement, a repurchase of shares, or an amendment to the memorandum of incorporation, may seek relief from the provisions of section 156. This is quite a broad provision which provides minority shareholders with various forms of protection.

In addition, section 161 allows shareholders to bring an application to court in order to protect their rights. Henochsberg says that the aim thereof is, in addition to other remedies that may be available in terms of the act, or in terms of the common law, to provide securities holders with a means to protect their rights.[114] This section enables shareholders to apply to court for an order determining their rights in terms of the act, the company's memorandum of incorporation or any rules of the company and also allows them to seek any order necessary to protect their rights or rectify any harm done to them by the company by way of any act or omission which contravened the act or the company's memorandum of incorporation. The protection afforded in section 161 is available to shareholders in addition to any other remedy in terms of the act or common law. Importantly, "the mere commission or omission of an act described in this section would not result in the remedy under s 161(1)(b)(ii) becoming available – actual harm for the securities holder should flow from the particular act. The act does not provide an indication of the type of result that would be considered as "harm" and this concept is clearly open to interpretation, but it is submitted that "harm" would include damage suffered by the securities holder".[115]

It would thus appear that this protection mechanism would be available to shareholders in the event of their rights being adversely affected by a scheme of arrangement, a repurchase of shares, or an amendment to the memorandum of incorporation, *only if they actually suffer harm*, an example of which could be where the value of their shareholding is diminished by a certain act or omission of the company.

[114] Delport et al (n 26) 558.
[115] Delport et al (n 26) 558.

4. Specific shareholder remedies

Whilst drafting the act, authors were faced with the task of balancing the encouragement of foreign investments, with offering shareholders every possible appropriate form of shareholder protection.[116] It is clear that a reorganisation of share capital by way of any of the aforementioned methods could likely cause shareholders to require the use of a shareholder remedy. The shareholder remedies of appraisal rights, and the oppression remedy are the most used remedies by minority shareholders and as such will be examined in detail and analysed to ascertain whether it provides sufficient protection to shareholders.

4.1. The appraisal remedy

Appraisal rights are described as being "the right of dissenting shareholders who do not approve of certain triggering events to have their shares bought out by the company in cash, at a price reflecting the fair value of the shares, which value may in certain cases be determined judicially".[117] This is a no-fault remedy and is triggered by the occurrence of a specific event, thus making it not generally available to shareholders.[118]

The previous Act did not provide for appraisal rights, but following the lead of jurisdictions where the option to be bought out by the company is given to minority shareholders, this shareholder remedy was introduced into our company law for the first time when the act came into being.[119] According to Yeats, appraisal rights find their origins in American law and are recognised in Canada, Australia and New Zealand.[120]

[116] Yeats "Putting appraisal rights into perspective" 2014 *Stell LR* 331.
[117] Cassim et al (n 48) 796.
[118] Cassim et al (n 48) 796.
[119] Beukes (n 82) 480.
[120] Yeats (n 116) 331.

4.1.1. Use of the appraisal remedy

Except to the extent that a transaction, agreement or offer relates to a business rescue plan approved by shareholders, dissenting shareholders in a company are provided with the appraisal right remedy in terms of section 164 of the act. Section 164 provides that, in the event that a company has notified shareholders of a meeting to adopt a resolution, either to amend its memorandum of incorporation by altering the preferences, rights, limitations or other terms of any class of its shares (the act emphasises that the manner in which these are amended must be *materially adverse* to the rights or interests of shareholders of that class of shares being altered), or to enter into a fundamental transaction, a statement must be included in such notification informing shareholders of their rights under section 164.[121]

4.1.2. Procedural aspects

The act provides that a dissenting shareholder may give a company written notice objecting to the resolution at any time before such resolution is adopted. It would appear however, that the wording of the act is somewhat flawed, due to the fact that the entire procedure of enforcing appraisal rights only commences once the company has received this notice, thus it should read that a dissenting shareholder *must* give a company written notice objecting to the proposed resolution. The reason for this requirement is to inform and alert the company as to the number of dissenting shareholders to allow the company to estimate the amount of the cash payment to be made by it, as this could constitute a potential drain on the company's cash resources.[122]

The entire procedural aspect of a shareholder "perfecting" its appraisal rights is somewhat lengthy and also rather tedious. It would appear that if the resolution is subsequently adopted, provided that the shareholder neither withdrew its notice to oppose nor voted in support of the resolution (mere abstention will not suffice), the company would then have

[121] s 164(1) and (2) of the Companies Act 71 of 2008.
[122] Cassim et al (n 48) 800.

to provide notice thereof to each shareholder who had given notice of its objection.[123] Shareholders may thereafter demand that the company pay the shareholder the fair value of the shares held, if it has complied with the aforementioned requirements and also only if it holds shares that are materially and adversely affected, in the event of an amendment to the companies memorandum of incorporation.[124] This demand would not constitute the end of the procedure as the act prescribes the manner in which the demand is to be delivered,[125] the procedure once a shareholder has accepted an offer made by the company,[126] as well as the procedure to be followed should an application be made to court to determine the fair value of the shares.[127] Dissenting shareholders are only paid the fair value of their shares if they have in fact perfected the appraisal right by properly carrying out the procedure in the act.

4.1.3. General commentary

According to the authors of *Contemporary Company Law*, the appraisal right has three important objectives.[128] Firstly, it acts as an exit mechanism for dissenting shareholders "whose expectations have been defeated or disappointed – it gives them the right to withdraw from the company by giving up their shares in exchange for their fair value in cash".[129] The authors state that it is beneficial to shareholders to be afforded an option to opt out as they may have become trapped in a company in which they did not initially intend to invest and which has been restructured and which as a result has a completely different set of assets, risks and returns.[130] Not only does this make practical sense for investors, but also economic sense for shareholders. Secondly, the appraisal right is an important remedy for unfairness in the event that minority shareholders are not satisfied with the price offered for their shares. A possibility for unfairness exists because the price

[123] s 164(4) of the Companies Act 71 of 2008.
[124] s 164(5) of the Companies Act 71 of 2008.
[125] s 164(7) of the Companies Act 71 of 2008.
[126] s 164(11) to (13) of the Companies Act 71 of 2008.
[127] s 164(14) to (17) Companies Act 71 of 2008.
[128] Cassim et al (n 48) 797.
[129] Cassim et al (n 48) 797.
[130] Cassim et al (n 48) 797.

is determined by directors negotiating the terms of the transaction. As such, appraisal rights function "as a check on opportunism by directors".[131] This also ties together with the third object, being that "the appraisal right serves as a deterrent or restraint on bad business judgments by directors".[132] This is evident from the fact that the more dissenting shareholders there are in any given transaction, the more likely the board of the company would be encouraged to reconsider the transaction and either relook at the price or back out of the transaction.

The complexity and technicality of the appraisal right process casts a negative light on the entire principle as shareholders may need to obtain legal advice or assistance and this could prove to be costly. According to the authors of *Contemporary Company Law*, "the procedural limitations of the appraisal right detract to a large extent from its effectiveness as a shareholder protection measure".[133] A shareholder could also miss out on the opportunity to exercise its appraisal rights by virtue of its failure to comply with all of the procedural steps timeously. On the other hand, it is stated that the company suffers no real adverse consequences by virtue of its non-compliance.[134] The authors further state that there is an inherent imbalance in the act, operating in favour of the company and harshly against the shareholder.[135]

Although not always necessary to approach a court, Davids, Norwitz and Yuill criticise the appraisal remedy and state that "to the extent that [a shareholder] *is* required to approach the court in order to have the fair value of its shares determined, there may be a considerable delay before it is compensated for its shares, bearing in mind that once it has demanded fair value for its shares from the company, it has no further rights in respect of its shares other than to receive payment".[136] They also criticise the inherent costs involved in litigation, stating that this may be prohibitive to shareholders and all of these factors may discourage shareholders from exercising their appraisal rights, especially

[131] Cassim et al (n 48) 797.
[132] Cassim et al (n 48) 797.
[133] Cassim et al (n 48) 807.
[134] Cassim et al (n 48) 807.
[135] Cassim et al (n 48) 808.
[136] Davids, Norwitz and Yuill (n 17) 360.

smaller shareholders who only have limited funds.[137] I am inclined to agree with this observation.

Judicial involvement during the appraisal right process is however somewhat limited and despite the fact that the act makes provision for shareholders to approach the courts, this option is seldom reverted to by shareholders. The procedure provided for by the act encourages settlement between the company and dissenting shareholders without resorting to “judicial” appraisal.[138] The authors of Contemporary Company Law hope that, in the event that an appraisal right matter does end up in court, courts will interpret the procedural obligations of dissenting shareholders as leniently as possible in order to excuse non-compliant shareholders who at all times acted in good faith in a genuine attempt to comply with the legislative requirements.[139] It seems unfair to disallow shareholders from obtaining fair value of their shares due to a minor non-compliance with the act. This would defeat the entire purpose of the provision. It is interesting to note however, that to date no occasion has arisen for the courts to consider or apply dissenting shareholder appraisal rights.[140] Although the act provides for a shareholder to approach the court to determine the fair value of the shares, it does not provide a remedy for shareholders in the event that the company fails to make payment of this agreed upon amount. Shareholders will be forced to rely on ordinary remedies outside of the appraisal procedure.[141]

Luiz states that legislature has clearly attempted to protect minority shareholders who face the prospect of being eliminated by a scheme of arrangement.[142] Luiz also opines that “although the protection afforded by the 2008 Act to shareholders involved in a scheme of arrangement has changed in that the court is no longer required to specifically approve the scheme, the 2008 Act has taken the need to adequately protect shareholders

[137] Davids, Norwitz and Yuill (n 17) 360.
[138] Cassim et al (n 48) 808.
[139] Cassim et al (n 48) 808.
[140] Yeats (n 116) 338.
[141] Beukes “An introduction to the appraisal remedy in the Companies Act: Standing and the appraisal procedure” 2010 *SA Merc LJ* 190.
[142] Luiz (n 23) 451.

(especially minority shareholders whose shares might be eliminated in terms of the scheme) seriously. Not only are the voting rights of shareholders with a conflict of interest excluded, but the possibility exists for an application to court to review the scheme and set aside the resolution approving it. The existence of the appraisal rights and the potential involvement of the Takeover Regulation Panel strengthen those protections even further".[143]

4.2. The oppression remedy

As minority shareholders are exposed to being oppressed by the rule of the majority and by the conduct of directors in the event of a reorganisation of share capital within a company, another protection mechanism that exists for minority shareholders is the oppression remedy.

4.2.1. Use of the oppression remedy

The act, in section 163, provides shareholders with relief from oppressive or prejudicial conduct by a company. It provides that a shareholder (or director of the company) may apply to the court for relief if any act or omission by the company has a result that is oppressive, unfairly prejudicial to or unfairly disregards the interests of the shareholder (or director). Shareholders may also apply to court if the business of the company is being carried on in a manner which is oppressive or unfairly prejudicial to, or that unfairly disregards the interests of the applicant, or if the powers of a director or prescribed officer of the company are being exercised in such manner.[144] The court may then make any determination (interim or final order) as it considers fit, including but not limited to a restraint order in respect of the conduct complained of. The act lists a number of possible orders that could be made by a court.[145] It is clear that the oppression remedy is judicially driven and shareholders must exercise this remedy by way of an application to the court.

[143] Luiz (n 23) 451.
[144] s 163(1) of the Companies Act 71 of 2008.
[145] s 163(2) of the Companies Act 71 of 2008.

The authors of *Contemporary Company Law* state that "a leading reason for the predominance of the oppression remedy in smaller private companies […] is that in this type of company, shareholders commonly play an active role in the affairs of a company. This often results in disputes of a personal nature among the shareholders".[146] It would have been beneficial for shareholders in a practical sense had the act prescribed actual triggering scenarios for the application of the oppression remedy, as it does for the appraisal remedy. This leads one to question when a shareholder can use this oppression remedy. For a shareholder to rely on the oppression remedy it must be able to prove that a company's actions are unfairly prejudicial and that these actions unfairly disregard the shareholder's interests. It is important to acknowledge that it is the *actual result* of the conduct that must be unfair or oppressive to shareholders and the act or omission referred to in the act is not the determining factor.

Beukes says that "it may be fair to suggest that changes to share rights might be considered materially adverse to the rights or interests of shareholders for the purpose of the appraisal remedy if these changes would have been considered unfairly prejudicial, unjust or inequitable for the purpose of the oppression remedy".[147] Surely it can be assumed that this statement would be true in the reverse as well. If so, triggering actions for the purposes of the appraisal remedy could also be triggering acts or omissions for purposes of the oppression remedy, as long as the result of these acts or omissions are oppressive or unfairly prejudicial to shareholders. The authors of *The Law of Business Structures* say that because the act or omission referred to by the act is so loosely defined, the remedy is capable of extending broadly over the conduct of general corporate affairs.[148] It is almost as if the oppression remedy acts as a "cover-all" remedy to shareholders, in the event that the appraisal remedy is not applicable. Henochsberg states that "it is not expressly required that the interests of the applicant should be disregarded or affected in any particular capacity".[149] This makes the oppression remedy even wider in that it is not only applicable to shareholders.

[146] Cassim et al (n 48) 758.
[147] Beukes (n 82) 481.
[148] Cassim et al (n 28) 418.
[149] Delport et al (n 26) 204.

Although the triggering actions may be similar, the outcomes of these two procedures differs quite substantially in that with the appraisal remedy, shareholders are paid fair value for their shares and can exit the company, whereas with the oppression remedy, a court can make any order it deems fit in the circumstances (as prescribed for by the act, but not limited thereto),[150] and interestingly enough, does not explicitly refer to an order to purchase a shareholders shares.[151]

The test for the oppression remedy is whether the conduct complained of is unfair, rather than unlawful. No legal rights of the shareholder need to be infringed upon by the company, but rather the interests of the shareholder must be unfairly disregarded.[152] A shareholder also cannot use this remedy as a mechanism to obtain relief if he is merely outvoted on a matter or if he loses confidence in the company's affairs.[153]

4.2.2. Availability of the oppression remedy

The availability of this remedy also encourages directors of a company to act within their duties of good faith, especially given the wide powers of the court in respect of this remedy.

Whether the oppression remedy would be available to shareholders in the case of a reorganisation of share capital by way of a repurchase, scheme of arrangement or amendment of the memorandum of incorporation would depend on the facts pertaining to each situation. Of course, if a shareholder's rights or interests have been unfairly disregarded in the reorganisation process, the remedy will be available. The determination point is somewhat unclear and reliance on the court's interpretation of each matter will be important in making this determination. It could be said that shareholders

[150] Beukes (n 82) 482.
[151] Cassim et al (n 48) 774.
[152] Cassim et al (n 28) 420.
[153] Cassim et al (n 28) 421.

are heavily reliant upon the competence of the courts and the judicial involvement of exercising ones rights in terms of section 163 is rather substantial.

4.2.3. Case law analysis

As the equivalent of section 163 in the previous Act was section 252, which similarly provided shareholders who had been victims of a company's oppressive or unfairly prejudicial conduct with a remedy to seek an appropriate court order, the history and development of the oppression remedy in South African courts is a long, and somewhat interesting one. This dissertation will only highlight a few important cases regarding the oppression remedy and will not go into the entire history of case law thereon.

In the case of *Bayly and Others v Knowles*[154], a minority shareholder (who was also a sales and marketing director of the company) was offered a deal by a majority shareholder (who was also the managing director of the company), which would entitle the majority shareholder to purchase the minority shareholder's shares in the company, in return for his resignation as a director. As the minority shareholder had no intention of disposing of his shares, he refused the offer and instead made a counter-offer that would grant him first option to purchase the majority shareholders shares. The majority shareholder refused the counter-offer as he also had no intention of disposing of his shares. Shortly thereafter, when threats and demands took over, and as a result of the conflict, the company stopped payment of the minority shareholder's salary and suspended all of his other benefits, including denying him access to the company's premises. The minority shareholder approached the High Court alleging oppression and requested an order under section 252 to reinstate his benefits. The High Court made an order compelling the majority shareholder to sell his shares to the minority shareholder. The majority shareholder appealed the decision. The Supreme Court of Appeal (the "SCA") held that the minority shareholder's non-acceptance of a reasonable offer for his shares was evident of the fact that he was willing to endure inequitable treatment by the majority shareholder despite having an alternative option. Thus the complaint of oppression was

[154] 2011 (2) SA 172 (SCA).

somewhat unreasonable given this viable alternative. The SCA held that, although a court could, in the right circumstances, make an order forcing a majority shareholder to sell his shares to a minority shareholder, such circumstances were not present in this case. The court further held that the only rational order in this case would be for the majority shareholder to acquire the minority shareholders shares, however such an order was not requested and as such, the court dismissed the application. It is clear from the context of this case that the element of unfairness was not present, given that the offer made by the majority shareholder was not unfair, but rather unacceptable, to the minority shareholder and as such, reliance on the oppression remedy was unfounded.

In the case of *Louw and Others v Nel*[155] the SCA held that section 252 conferred a very wide discretion on the court and that the court thus had the "power to do what it considered fair and equitable in the circumstances, to put right and cure the unfair prejudice which a minority shareholder had suffered at the hands of the majority of the company". It further held that "fairness was the criterion by which the court had to decide whether it had jurisdiction to relief". Furthermore, the court held that an applicant for relief under section 252 had to establish firstly "that a particular act or omission had been committed, or that the affairs of a company were being conducted in the manner alleged, and that such act or omission or conduct of the company's affairs was unfairly prejudicial, unjust or inequitable to him or some part of the members of the company", secondly "the nature of the relief that must be granted to bring an end to matters complained of", and thirdly "that it was just and equitable that such relief be granted".[156] The court held that the court's jurisdiction to make an order only arose after the statutory criteria had been met, and there was a "universal application as to what was fair". Evidently, fairness in each case would be dependent on the relevant circumstances arising in the matter.

The question arose in the case of *Visser Sitrus (Pty) Ltd v Goede Hoop Sitrus (Pty) Ltd and Others*[157] whether a decision taken by directors in accordance with section 76 (that

[155] 2011 (2) SA 172 (SCA).
[156] 2011 (2) SA 173 (SCA).
[157] 2014 (5) SA 179 (WCC).

a director was in breach of his fiduciary duties) of the act could cause the unfair prejudice of shareholders as required by section 163. The court held in this regard that the circumstances would have to be exceptional to be unfairly prejudicial. In this case, a transfer of shares was refused by the directors of the company, however they acted lawfully and rationally in making this decision and had the best interests of the company in mind. It was held that the result of this refusal was not unfairly prejudicial to the shareholder, and as such, relief by way of the oppression remedy was unfounded.

5. Conclusion

It is important to consider reorganisation of share capital as a whole, as well as each method individually as discussed above. Essentially, a company wishing to reorganise its share capital may do so by any of the aforementioned methods, as it may deem fit and appropriate in the circumstances. What is vital for shareholders is to determine in each case the appropriate form of minority protection to pursue, as each of the remedies available may not be conducive to a specific type of reorganisation. For example, where shares are being repurchased by a company by way of a scheme of arrangement, it may not necessarily be oppressive and prejudicial towards minority shareholders and they should rather proceed by way of the appraisal remedy than by way of the oppression remedy. Shareholders need to evaluate whether they wish to remain a shareholder of the company or whether they wish to exit the company altogether. This, in addition to the costs of pursuing the relevant remedy, will also have an impact on the decision of which protection mechanism is to be used.

As discussed above, an important form of protection built into the act would be disclosure as disclosure requirements provide indirect protection to shareholders and are a useful measure against abuse.[158] Shareholder approval in the form of a special resolution also serves to protect shareholders, however it would be apparent that dissenting shareholders are not protected by this as they would be compelled to adhere to the

[158] Van der Linde (n 50) 305.

majority decision.[159] Despite this, dissenting shareholders could then rely on the appraisal remedy, meaning that they do in fact have a remedy in the event of majority rule being followed.

Another important built-in protection mechanism is the court review/approval process provided for in section 115(3) to (7) of the act (which applies to both schemes of arrangement in accordance with section 114 as well as repurchases of shares in accordance with section 48(8)(b)), which significantly enhances shareholder protection, as discussed above.

Regarding the effectiveness of the appraisal right remedy in our company law, I am of the opinion that this remedy provides adequate protection to shareholders where they are entitled to make use of it. Cassim says that the appraisal remedy is diminished by its procedural flaws.[160] I disagree with this statement. Despite the inherent lengthiness of the act in setting out the procedure to be followed, the potential costs involved and despite the possibility of shareholders perhaps erring in carrying out the procedure as required by the act, shareholders are afforded an opportunity to receive fair value for their shares and exit a company, without upsetting the majority shareholders and the need for a company to implement these types of transactions. It is almost a "win-win" situation for the shareholder and for the company. I agree with Beukes who states that "this remedy not only gives a certain advantage to a legal system, but is also essential to the proper protection of minority shareholders. As a result, despite criticism against the existence and scope of the appraisal remedy in other jurisdictions, the proposed introduction of this remedy into South African corporate law must be welcomed".[161] Yeats also says that the inclusion of this remedy in the act is a noteworthy enhancement of minority shareholder protection.[162] I am of the opinion that the appraisal remedy adequately protects shareholders in the event of a reorganisation of capital within a company, to the extent

[159] Van der Linde (n 50) 305.
[160] Cassim "The introduction of the statutory merger in South African Corporate Law: Majority rule offset by the appraisal right (Part 2)" 2008 *SA Merc Law Journal* 176.
[161] Beukes (n 82) 495.
[162] Yeats (n 116) 341.

that a shareholder resolution was voted upon. Perhaps the only improvement to be made to this section of the act would be to simplify the procedural aspects thereof.

Given the broad protection offered by the oppressive remedy in terms of section 163 of the act, it can be said that shareholders will usually have this remedy to fall back on in the event that they are unable to find remedy by the exercising of their appraisal rights, for example, where no resolution is voted on by shareholders. This remedy could be used, for example, where directors amend the memorandum of incorporation in accordance with section 36(3), as very little shareholder protection is afforded in this section. The act, as mentioned above, provides such a wide range of possible orders to be made by a court and I believe that the provisions of section 163(2) do not constitute a *numerus clausus*, making the application thereof even wider. This remedy adequately protects shareholders and can be used by shareholders in the event that a reorganisation of share capital is oppressive, unfairly prejudicial or unfairly disregards the interests of the shareholder.

Considering the arguments above, I am of the opinion that the act provides sufficient protection to shareholders during a reorganisation of share capital within an organisation.

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