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**SELECTIVE REPURCHASES OF SHARES AND PROTECTION OF SHAREHOLDERS
IN TERMS OF THE COMPANIES ACT 71 OF 2008**

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DECLARATION

I hereby declare that the minor dissertation submitted for the LLM degree at the University of Johannesburg, is my own work and has not been submitted to another university or institution of higher education for a degree.

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SUMMARY

Section 48 of the Companies Act provides directors with exclusive powers to conduct repurchases either selectively or proportionately and with or without the shareholders' approval. These exclusive powers, particularly the powers to selectively repurchase shares may prejudice the interest of shareholders in a company. The study is to analyse the provisions of the Companies Act 71 of 2008 to determine whether it adequately protects the interests of shareholders. The analysis will be made in comparison with protective measures contained in the New Zealand Companies Act 1993.

The Companies Act 71 of 2008 does not distinguish between selective or proportionate repurchases. Section 48 of the Companies Act 71 of 2008 sets out the requirements to be complied with by a company when repurchasing any of its shares and in addition it sets out the requirements for repurchases of shares held by directors or prescribed officers and their related persons or repurchases conducted in terms of a scheme of arrangement.

The forms of protection available to shareholders depends on whether a shareholder is a director or whether a selective repurchase is undertaken in terms of a scheme of arrangement. Shareholders will have to rely on protective measures outside section 48 of the Companies Act 71 of 2008, for them to protect themselves, and in particular when a repurchase is not conducted in terms of a scheme of arrangement. The protective measures in repurchases conducted through a scheme of arrangement includes the shareholders' approval requirement, voting restrictions and appraisal right. The protective measures available to shareholders who are directors for a repurchase which does not constitute a scheme of arrangement is the shareholders' approval requirement.

The New Zealand Companies Act appears to better protect the interest of shareholders by requiring that selective repurchases be approved by all shareholders and if not, repurchases are subject to ideal protective measures such as the disclosure requirement, observance of the best interests of the company and shareholder, and that the price paid for shares must be fair to the company and the remaining shareholders.

It is suggested that shareholders should as practical as possible approve selective repurchases, be afforded a right to demand payment of a fair value of shares and that measures must should be provided for in the legislation specifically to protect shareholders in selective repurchases.

KEY WORDS:

Repurchases, selective repurchases, shares, shareholders, interests of shareholders, protection of shareholders, measures directors, scheme of arrangement, Companies Act 71 of 2008, New Zealand Companies Act 1993.



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1. Introduction

A shareholder is entitled to control the direction of a company through voting rights.¹ Shareholders are entitled to receive a share from the company's assets upon the company's dissolution and also has an expectation to receive dividends from the company's declared profits.² These interests stand to be unfairly extinguished by the company's powers and the company's decision to implement a selective repurchase of shares from any of its shareholders.³ The powers given to a company to repurchase shares from its shareholders have been criticised for allowing companies to selectively repurchase shares with some companies using such repurchasing powers for ulterior motives.⁴

In South Africa repurchases were prohibited mainly to protect creditors and shareholders.⁵ The amendment of the Companies Act 61 of 1973 in 1999 allowed repurchases of shares subject to compliance with the solvency and liquidity test.⁶ The Companies Act 61 of 1973 and in particular the changes brought by the Companies Amendment Act 37 of 1999 were criticised for failing to explicitly regulate either proportionate or selective repurchases with a view to specifically protecting the interests of shareholders.⁷ Cassim indicated, in relation to the 1999 amendments of the Companies Act 61 of 1973, that "The provisions of the Act relating to selective share repurchases leave too much scope for mischief. Specific statutory safeguards must be provided to guard against the very real danger of abuse."⁸ This paper seeks to analyse the provisions of the Companies Act, 71 of 2008,⁹ in order to determine whether the Companies Act adequately regulates selective repurchases with appropriate and adequate measures to protect the interests of shareholders.

¹ Cassim *et al Contemporary Company Law* 2nd ed (2011) 213 - 215 discussing the nature of a share.

² Van der Linde "The regulation of distributions to shareholders in the Companies Act 2008" 2009 *TSAR* 483.

³ Blackman *et al Commentary on the Companies Act* (2012) 5-43.

⁴ Bielawski "Selective stock repurchases after Grobow: the validity of greenmail under Delaware and federal securities laws" 1990 *Delaware Journal of Corporate Law* 1. See also Hutchins "Partial and selective reacquisitions of corporate securities" 1979-1980 *California Western Law Review* 264 265.

⁵ Cassim (*Contemporary Company Law*, n 1) 294. The prohibition was in force up until the Companies Amendment Act 37 of 1999.

⁶ Section 85 of the Companies Act 61 of 1973 as amended by section 9 of the Companies Amendment Act 37 of 1999.

⁷ Cassim "The new statutory provisions on share repurchases: a critical analysis" 1999 *SALJ* 760 780. See also Van der Linde "Share repurchases and the protection of shareholders" 2010 *TSAR* 288 309.

⁸ Cassim "The new statutory provisions on company share repurchases: a critical analysis" 1999 *SALJ* 760 776.

⁹ Companies Act 71 of 2008, hereinafter referred to as the Companies Act.

In addition, a brief comparison on how the New Zealand Companies Act¹⁰ regulates selective repurchases in an attempt to protect the interests of shareholders shall be considered, with the New Zealand Companies Act 1993 being considered as it contains measures aimed at protecting the interests of shareholders. The Johannesburg Stock Exchange (JSE) Listings Requirements on selective repurchases will be considered to determine if such requirements afford shareholders of JSE listed companies with some form of protection against the dangers of selective repurchases. In conclusion the paper shall evaluate, with recommendations, whether there are enough measures in the Companies Act to protect shareholders whose interests are threatened by the company's power to conduct selective repurchases.

2. Selective repurchases: meaning and form

A share repurchase is a business transaction in terms of which a company reacquires its shares from one or more of its shareholders, either conducted selectively, proportionately or through an open market offer. A selective repurchase of shares is a repurchase of shares from one or more selected shareholders on terms and conditions unique to the selected shareholder or shareholders.¹¹ Proportionate repurchases occur when a company repurchases shares from all shareholders of a company on the same terms and conditions.¹² A proportionate offer to repurchase shares of a company may have the same effect as a selective repurchase if it was made with the intention that some shareholders will be unable to accept the offer and the offer was eventually not accepted by all shareholders.¹³ An offer on an open market has an element of a selective repurchase due to the possibility that some shareholders may be unable to accept the offer. However an open market offer is not considered discriminatory as the offer is not directed to an identified shareholder.¹⁴

3. Reasons and risks associated with selective repurchases

Repurchases in general can be conducted for positive and for ulterior motives. The positive reasons justifying the empowerment of a company to repurchase its shares may include operational and

¹⁰ New Zealand Companies Act of 1993.

¹¹ Van der Linde "Share repurchases and the protection of shareholders" 2010 *TSAR* 288.

¹² *Ibid* 289.

¹³ *Ibid*.

¹⁴ *Unitrin Inc v American General Corp* 651 A.2d 1361 Del-Supreme Court (1995).

economic reasons.¹⁵ Selective repurchases can assist a company to reduce administrative costs associated with managing a number of shareholders individually holding a very small number of shares.¹⁶ Repurchases are seen as a way of maintaining family control over a company and may enable a company to repurchase shares from retiring employees or from deceased estates.¹⁷ These are some of the positive and perhaps non-contentious reasons justifying the empowerment of a company to repurchase its shares.

In spite of the aforesaid reasons, repurchases are sometimes conducted for ulterior motives. Instances of ulterior motives include a repurchase to eliminate a troublesome or dissenting shareholder and a repurchase in an attempt to avoid a takeover bid.¹⁸ Selective repurchases pose some risk of unfair treatment amongst shareholders. Repurchases can be conducted for the purpose of eliminating participating securities and conferring a benefit in a form of higher profit returns to some preferred shareholders.¹⁹ Van der Linde explains that repurchases pose some risks with regard to pricing of shares, with the lower the price the company pays, the more the benefits to remaining shareholders at the expense of the targeted shareholders while a higher price paid will dilute the value of shares held by non-selling shareholders.²⁰ In essence selective repurchases may be conducted to benefit the selling shareholder or non-selling shareholder depending on the motive behind the decision to repurchase shares.

Thus the ulterior motives and the risks associated with selective repurchases are tangible reasons for advancing a more shareholder protective approach when providing companies with powers to conduct a selective repurchase. The discussion turns to focus on the manner and the form of repurchases as well as protective measures in terms of the Companies Act.

¹⁵ Van der Linde “The regulation of conflict situations relating to share capital” 2009 *SA Merc LJ* 35 41.

¹⁶ Cassim (*Contemporary Company Law*, n 1) 297.

¹⁷ Van der Linde “Share repurchases and the protection of shareholders” (2010) *TSAR* 288 289. See also Cassim *The Practitioner’s Guide to the Companies Act of 2008* (2011) 117. See Blackmann *et al* (n 3) (2012) 5 48-49 for a detailed discussion of repurchase reasons. Cassim (*Contemporary Company Law*, n 1) 296 - 298 for a list of social and economic reasons justifying repurchases.

¹⁸ Van der Linde (*Share repurchases*, n 11) (2010) 288 289.

¹⁹ Brian R Hutchins “Partial and selective reacquisitions of corporate securities” 1979-1980 *California Western Law Review* 264 265.

²⁰ Van der Linde (*Share repurchases*, n 11) (2010) 288.

4. Selective repurchases in terms of the Companies Act 71 of 2008

4.1. Requirements for repurchases

Section 48 of the Companies Act sets out the requirements to be complied with by a company when conducting repurchases. The board of a company may determine that the company will acquire a number of its own shares subject to subsection (3) and (8) as well as the provisions of section 46 of the Companies Act.²¹ A company may not repurchase its shares if as a result of the acquisition a company would no longer have shares in issue other than shares held by its subsidiaries; or convertible or redeemable shares.²²

Section 48(8) of the Companies Act²³ provides that a decision by the board to repurchase the company's shares must be approved by a special resolution of the shareholders of the company if any shares are to be acquired by the company from a director or prescribed officer of the company or a person related to a director or a prescribed officer of the company; and is subject to the requirements of sections 114 and 115 if, considered alone, or together with other transactions in an integrated series of transactions, it involves the acquisition by the company of more than 5% of the issued shares of any particular class of the company's shares. The Companies Act refers to a scheme of arrangement, in so far as it relates to repurchases, as an arrangement between the company and holders of the company's shares to repurchase the company's shares.²⁴

Delport and Vorster submit that a number of interpretations of section 48(8) exist.²⁵ The first interpretation is that section 48(8) may be construed to mean that an acquisition of shares from directors must be approved by a special resolution of shareholders without complying with section 114 and 115 of the Companies Act provided that the acquisition of shares does not exceed 5% of the company's issued shares of any particular class. Secondly, if shares are to be acquired from directors and exceed 5% of the company's issued shares of any particular class, such acquisition must comply with section 114 and 115. Lastly it may be interpreted to mean that any repurchase of shares in excess of 5% of the issued shares of any class of the company's shares requires a

²¹ s 48(2) of the Companies Act.

²² s 48(3) of the Companies Act.

²³ Section 48(8) of the Companies Act as inserted by section 32(e) of the Companies Amendment Act 3 of 2011.

²⁴ s 114(1)(e) of the Companies Act.

²⁵ Delport and Vorster *Henochsberg on the Companies Act 71 of 2008* (2011) 203.

scheme of arrangement irrespective of whether shares are acquired from directors or not.²⁶ The reasons for the distinction between utilising section 48 and section 114 appears unclear in the Act, in particular when a repurchase involves shares of less than 5% of the company's issued shares. Cassim *et al* indicate that section 114 perhaps was aimed at dealing with repurchases that amount to fundamental changes to the company's capital structure.²⁷

A repurchase of shares of less than 5% of the issued shares may still be conducted in terms of section 114 and thus making it a scheme of arrangement. It is also unclear whether a repurchase of shares in excess of 5% of the company's issued shares undertaken through section 48(8)(b) is indeed a scheme of arrangement and thus initiated by implementing an arrangement between the company and its shareholders or whether it is only that the requirements applicable to repurchases in terms of a scheme of arrangement are also applicable to repurchases in terms of section 48(8)(b) of the Companies Act.

Repurchases are also subject to the requirements relating to distributions contemplated in section 46 of the Companies Act. "Distribution" is defined in relation to repurchases as a direct or indirect transfer by a company of its money or its property, other than transfer of its shares, for the benefit of a shareholder as consideration for the acquisition by the company of its shares.²⁸ In terms of the definition of distribution it is clear that a repurchase decision is not a distribution but the actual consideration paid in lieu of the repurchased shares that is a distribution.²⁹ Section 46(1)(a) of the Companies Act provides that a company may not make any proposed distribution unless a distribution is pursuant to an existing obligation of a company or a court order or in terms of a resolution of the board of the company. Further, it must reasonably appear that the company will satisfy the solvency and the liquidity test immediately after completing the proposed distribution.³⁰ The board must acknowledge by resolution that it has applied the solvency and the liquidity test as set out in section 4 of the Companies Act³¹ and reasonably concluded that the company will

²⁶ Ibid 203.

²⁷ Cassim (*Contemporary Company Law*, n 1) 304.

²⁸ s 1 of the Companies Act.

²⁹ s 46(3) of the Companies Act.

³⁰ s 46(1)(b) of the Companies Act.

³¹ Section 4 of the Companies Act provides that a company satisfies the solvency and liquidity test at a particular time if the assets of the company, as fairly valued, equal or exceed the liabilities of the company, as fairly valued; and it appears that the company will be able to pay its debts as they become due in the ordinary course of business for a

satisfy the solvency and liquidity test immediately after completing the proposed distribution.³² The company has a 120 day period from the date of acknowledgement to conclude or implement a repurchase, failing which the board must reconsider the solvency and the liquidity test and pass another resolution acknowledging that the company will be able to satisfy the solvency and the liquidity elements.³³

In essence the Companies Act does not distinguish between selective and general repurchases in terms of its requirements. Failure to make such distinction between selective and proportionate in the Companies Act was despite criticism, wherein Cassim criticised the Companies Amendment Act 37 of 1999 for its failure to draw a distinction between selective and pro-rata repurchases with no special provisions aimed at preventing potential abuses in selective repurchases.³⁴ The Companies Act provides a unique set of requirements to be complied with by a company when repurchasing any of its shares with additional requirements specifically prescribed for repurchases from directors or prescribed officers and their related persons as well as repurchases of more than 5% of any class of shares. The Companies Act also regulates repurchases of shares by a subsidiary of shares held by holding companies. The requirements relating to repurchases of shares by a subsidiary of shares held by holding companies are not discussed herein.

4.2. Protective measures

4.2.1. Approval requirements

The Companies Act distinguishes between types of repurchases in so far as approval is required. All share repurchases require the board's approval and in addition to the board's approval, a shareholders' approval is also required for any repurchase of shares from the directors of a company and for any repurchase of shares conducted in terms of a scheme of arrangement.³⁵ In

period of 12 months after the date on which the test is considered; or in the case of a distribution contemplated in paragraph (a) of the definition of distribution in section 1, 12 months following that distribution.

³² s 46(1)(c) of the Companies Act.

³³ s 46(3) of the Companies Act.

³⁴ Cassim "The new statutory provisions on company share repurchases: a critical analysis" 1999 *SALJ* 760 776. See also Cassim (*Contemporary Company Law*, n 1) 303.

³⁵ Section 48(2) of the Companies Act requires a decision of the board for a company to conduct any type of a repurchase, whereas section 48(8) of the Companies Act also requires a special resolution of shareholders for repurchases from directors and also section 115(2) of the Companies Act requires a special resolution of shareholders for repurchases conducted in terms of a scheme of arrangement. As a reminder the requirements relating to an acquisition of shares by subsidiaries in a holding company were not discussed. Section 65(11)(g) of the Companies

terms of section 65(12) of the Companies Act, a company may in its memorandum of incorporation require a special resolution of shareholders for any repurchase which would otherwise not require a special resolution under the provisions of the Companies Act.

A mere special resolution of shareholders is sufficient for a repurchase of less than 5% of the company's issued shares from directors.³⁶ Section 65 of the Companies Act, which regulates shareholders' resolutions, does not prescribe how shareholders who are also directors should participate in shareholder's resolution contemplated in section 65 of the Companies Act. This may suggest that any shareholder can freely participate in the required special resolution to repurchase shares from directors constituting less than 5% of the company's issued shares held by directors. However it must be noted that with regard to the board decision to repurchase shares, any director of a company is required to disclose any financial interest on any matter to be considered by the board and not to take part in a meeting to consider such resolution unless a matter generally affects all directors.³⁷ Thus any director who has any financial interest in a repurchase resolution to be considered by the board must make disclosure of such financial interest unless a repurchase concerns all directors of a company.³⁸

A special resolution required to approve a repurchase of shares conducted in terms of a scheme of arrangement must be adopted by persons entitled to exercise voting rights on such matter, at a meeting called for that purpose and where sufficient persons are present to exercise, in aggregate, at least 25% of all the voting rights that are entitled to be exercised on that matter, or any higher percentage as may be required by the company's memorandum of incorporation.³⁹ Section 115(4) of the Companies Act provides that any voting rights held by an acquiring party, or a person related

Act provides that a special resolution is required to approve a decision of the board for a repurchase of shares conducted in terms of section 48(8) of the Companies Act, meaning a repurchase from directors and repurchases conducted in terms of a scheme of arrangement.

³⁶ Section 65(9) of the Companies Act provides that for a special resolution to be approved by shareholders, it must be supported by at least 75% of the voting rights exercised on the resolution. In terms of section 65(10) of the Companies Act a company's memorandum of incorporation may permit a lower percentage of voting rights to approve a special resolution; or one or more lower percentages of voting rights to approve a special resolution concerning one or more particular matters, respectively, provided that there must at all times be a margin of at least 10 percentage points between the requirements for approval of an ordinary resolution, and a special resolution, on any matter.

³⁷ Sections 75(2)(a)(i)(aa) and 75(5)(5)(a) of the Companies Act.

³⁸ Ibid.

³⁹ s 115(2) of the Companies Act.

to an acquiring party,⁴⁰ or a person acting in concert with either of them, must not be included in calculating the percentage of the voting rights required to be present, or actually present, in determining whether the applicable quorum requirement is satisfied; or required to be voted in support of a resolution or actually voted in support of the resolution. Thus a shareholder who as a result of a repurchase becomes an acquiring person may not be a party to a voting process for the purpose of considering and adopting a special resolution to repurchase shares in terms of a scheme of arrangement. This may be aimed at preventing and managing potential conflict of interests and it will definitely protect the interests of both remaining and targeted shareholders.⁴¹ It is further aimed at preventing collusion amongst related shareholders to the detriment of other shareholders and this will protect the interests of targeted shareholders.

4.2.2. The solvency and liquidity test

Section 46 of the Companies Act prohibits any direct or indirect transfer by a company of its money or its property for the benefit of a shareholder as a consideration for the acquisition by the company of its shares, unless the company satisfies the solvency and the liquidity test immediately after completing a repurchase. Van der Linde points out that the solvency and liquidity test has different justifications including preventing the company from favouring its shareholders over creditors.⁴² Hutchins says that although the solvency and liquidity test ensures that the company remains in a solvent state, the test is mainly for the purpose of protecting creditors and not shareholders.⁴³ It must be noted that the solvency and liquidity test must be applied in all repurchases.

⁴⁰ Section 1 of the Companies Act defines an acquiring party as a person who, as a result of the transaction, would directly or indirectly acquire or establish direct or indirect control over all or the greater part of a company, or all or the greater part of the assets or undertaking of a company.

⁴¹ Cassim (*Contemporary Company Law*, n 1) 692. It must be noted that section 115(7) of the Companies Act identifies conflict of interest as a ground for setting aside a repurchase conducted in terms of a scheme of arrangement.

⁴² Van der Linde "The solvency and liquidity approach in the Companies Act 2008" (2009) TSAR 224 226.

⁴³ Brian R Hutchins (n 19) 274. See also Cassim "The reform of company law and the capital maintenance concept" (2005) *SA LJ* 284 287.

4.2.3. Disclosure requirements

In general, directors are expected to disclose the affairs of the company to its shareholders. With regard to repurchases conducted in terms of a scheme of arrangement, the Companies Act requires directors to obtain an independent expert report detailing amongst others, the value of the shares affected, the type and the class of shares involved, the identity of affected shareholders, the material effects of a repurchase on the shareholders and directors' interests as well as any benefit and effect on the business and the prospects of a company.⁴⁴ The requirements relating to an independent experts' report may guarantee disclosure of information required to enable a shareholder to take an informed decision when considering whether to accept or reject a repurchase offer. It must be noted that the disclosure requirement by virtue of an independent expert report is only applicable to repurchases that are conducted in terms of a scheme of arrangement.

Despite an expert report requirement for repurchases undertaken in terms of a scheme of arrangement, section 65(4) of the Companies Act provides that any proposal that requires a special resolution of shareholders must be expressed with sufficient particularity, information or explanation material to enable a shareholder to vote on the proposed resolution. As section 48(8)(a) of the Companies Act requires any repurchase from directors to be approved by a special resolution of shareholders, the directors must then disclose with sufficient particularity, in terms of section 65(4) of the Companies Act to shareholders, any valuable information relating to a repurchase of shares from directors not conducted in terms of a scheme of arrangement.

4.2.4. Court recourse

Any repurchase in contravention of sections 46 and 48 of the Companies Act may be set aside by the court within two years after being implemented with such application being brought by the company for an order reversing the acquisition.⁴⁵ The court may order the return of the consideration paid and that the company issue shares to the previous shareholder equivalent to the shares repurchased from that shareholder.⁴⁶ This court remedy will protect the shareholders whose interests were affected by a repurchase. However an order setting aside a repurchase may also pose

⁴⁴ s 114(2)(3) of the Companies Act.

⁴⁵ s 48(6) of the Companies Act.

⁴⁶ s 48(6)(a) and (b) of the Companies Act.

some challenges as the court will be required to balance the interests of a company as well as the interests of a bona fide selling shareholder. As Delpont and Vorster state, compliance with the company's internal requirements for a repurchase is a board issue and any order setting aside a repurchase may impact negatively on the interests of the bona fide third party shareholder who is not privy to the information about the board's compliance with the requirements of sections 48 and 46 of the Companies Act.⁴⁷ Delpont and Vorster also indicate that in some instances it may not be possible to return any consideration paid in respect of share acquisitions.⁴⁸

A company may not implement a scheme of arrangement without an approval of the court if the resolution was opposed by at least 15% of the voting rights that were exercised on that resolution and within five business days after the vote, any person who voted against the resolution requires the company to seek a court approval or alternatively 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 court for a review of the transaction.⁴⁹

The court may grant an application for review if it is satisfied that the applicant acts in good faith, appears prepared and able to sustain the proceedings and has put forward facts which if proved would support an order setting aside the resolution.⁵⁰ A repurchase of shares resolution stands to be set aside by court on review if a repurchase is unfair to shareholders of any class, or if the voting is tainted by conflict of interest, inadequate disclosure or any failure to comply with the Companies Act.⁵¹ In essence a shareholder who voted against a repurchase resolution is entitled to apply for a court review of a repurchase and also entitled to request the company to seek the court's approval before it can implement a repurchase. This is an additional court remedy available in repurchases initiated through a scheme of arrangement.

⁴⁷ Delpont and Vorster (n 25) 208.

⁴⁸ Ibid.

⁴⁹ s 115(3)(a) and (b) of the Companies Act.

⁵⁰ s 115(6) of the Companies Act.

⁵¹ s 115(7) of the Companies Act.

4.2.5. The appraisal remedy

The appraisal remedy protects shareholders by affording them an opportunity to seek a payment equivalent to a fair value for their shares. Section 115(8) read with section 115(1) and 114(1)(e) of the Companies Act entitle any holder of any voting rights in a company to a relief in terms of section 164 of the Companies Act provided that the voting rights holder notified the company of his or her intention to oppose and also voted against the special resolution that authorised a repurchase. In terms of section 164 of the Companies Act, a shareholder is entitled to demand that a company which adopted a resolution to repurchase shares in terms of section 114(4) pay him or her the fair value for all the shares held by him or her in the company, provided the shareholder has objected against the proposal to adopt the resolution to repurchase shares and voted against the adopted resolution.⁵² The company must make an offer to pay an amount considered by the company to be a fair value of the shares.⁵³ If a company fails to make an offer, or makes an offer that a shareholder considers to be inadequate, a shareholder may apply to court for a court to determine a fair value of his shares.⁵⁴

The purpose of an appraisal remedy is to protect both remaining and selling shareholders to an extent that shareholders can demand to be paid a fair price for their shares. Van der Linde submits that the appraisal remedy will offer limited protection in coercive and proportionate repurchases, as it would make no real difference to afford a shareholders a right to sell his or her shares to the company, if the shareholder really did not want to sell his shares.⁵⁵ Despite that the appraisal remedy is only applicable to repurchases conducted in terms of a scheme of arrangement.

4.2.6. Relief from oppressive or prejudicial conduct

A repurchase of shares may be prejudicial to the interests of shareholders. The conduct of a company, directors or other shareholders may unfairly disregard the interests of a shareholder. A repurchase can be conducted with the intention of forcing out a particular shareholder from the company and this may be unfairly prejudicial to a shareholder's interests. A repurchase may entail a change in the control and change in percentage of a shareholder's holding in a company and can

⁵² s 164(3,) of the Companies Act.

⁵³ s 164(11) of the Companies Act.

⁵⁴ s 164(14) of the Companies Act.

⁵⁵ (n 11) 302.

result in unequal treatment prejudicial to the interests of some shareholders.⁵⁶ Delpont and Vorster indicate that shareholders may protect their interests by utilising an action in terms of oppressive or prejudicial conduct enshrined under section 163 of the Companies Act.⁵⁷

Section 163(1) of the Companies Act entitles a shareholder or a director of a company to apply to court for relief if the results of an action of a company are oppressive or unfairly prejudicial to, or unfairly disregards the interests of the applicant; or if the powers of a director are being or have been exercised in a manner that is oppressive or unfairly prejudicial to the interests of the applicant. In relation to repurchases a shareholder may argue that the manner in which directors exercised their powers by selectively repurchasing certain shares and not others is prejudicial to and unfairly disregards his or her interests in a company. The court may, in an application for relief from a prejudicial and oppressive conduct, make amongst others an order restraining the conduct complained of, an order varying or setting aside a transaction to which the company is a party, and an order compensating the company or any party to the transactions.⁵⁸ Thus a remaining shareholder whose interests were affected by a repurchase may well seek an order setting aside a transaction and a selling shareholder may well seek a compensation order in instances where the company repurchased shares at a price below the market value.

The conduct of directors and shareholders may be considered when any relief is sought in terms of section 163 of the Companies Act. The underlying motives of the majority may aid the court in deciding whether conduct is unfairly prejudicial and whether the grant of relief would be just and equitable, but the court would not be able to interfere even if the conduct of the majority was perpetuated by a personal motive unless such conduct was improper.⁵⁹ The court will only intervene if the majority acts in bad faith and in a manner that prejudices the minority and precludes fair participation in the affairs of the company by all shareholders.⁶⁰

⁵⁶ Cassim “The reform of company law and the capital maintenance concept” 2005 *SALJ* 284 287.

⁵⁷ Delpont and Vorster (n 25) 570.

⁵⁸ s 163(2) of the Companies Act lists a number of orders that the court may grant when relief in terms of section 163 is sought.

⁵⁹ *Ben-Tovim v Ben-Tovim* 2001 (3) SA 1074 (C) 1091-1092.

⁶⁰ Delpont and Vorster (n 25) 570.

Section 163 of the Companies Act may assist in protecting the interests of both targeted and remaining shareholders whose interests have been unfairly affected. The success of any action based on section 163 of the Companies Act shall depend on our courts balancing the interests of the company and those of shareholders in a repurchase of shares. Obviously any shareholder who participated and voted in favour of a resolution to repurchase shares will find it difficult to seek any relief in terms of section 163 of the Companies Act as he would have consented to such repurchase. Thus section 163 will definitely not apply to any shareholder who voted in favour of a resolution or who supported a scheme of arrangement to repurchase shares.

4.2.7. Rights of shareholders of regulated companies

When a repurchase results in a change of control of a regulated company,⁶¹ as contemplated in the takeover provisions, section 123 of the Companies Act also protects the interests of remaining minority shareholders. The Companies Act requires that any person or persons acting in concert,⁶² who as a result of a repurchase acquires more than 35% of the voting rights attached to securities, make a mandatory offer to acquire the shares of the remaining shareholders.⁶³ Section 123(3) does not apply if a person acquires beneficial interests with no voting rights. The measures under section 123 affords remaining minority shareholders with an opportunity to be bought out of the company. This measure is applicable to all remaining shareholders of regulated companies after any repurchase of shares with voting rights in terms of section 48 of the Companies Act.⁶⁴

4.2.8. Regulation of repurchases in a memorandum of incorporation

Legislation may best provide for the powers of directors, but the manner of executing some powers may best be prescribed in a memorandum of incorporation of a company. Section 15 of the Companies Act provides that the memorandum of incorporation of a company may impose on a

⁶¹ See section 117(1)(i) of the Companies Act for the meaning of regulated company.

⁶² Section 117(1)(b) of the Companies Act defines “act in concert” to mean any action pursuant to an agreement between or amongst two or more persons in terms of which any of them co-operate for the purposes of entering into or proposing an affected transaction or offer.

⁶³ See section 123(2)(3)(a) read with regulation 86(1) of the Companies Act. In terms of Regulation 86(3) of the Companies Act a persons or persons acting in concert who, as a result of a repurchase contemplated in section 123(2) of the Companies Act, acquires beneficial interests with no voting rights, have no right to make mandatory offers contemplated in section 123 of the Companies Act.

⁶⁴ s 123(2)(a) of the Companies Act.

company a higher standard, greater restriction, longer period of time or any similarly more onerous requirement, than would otherwise apply to the company in terms of an unalterable provision.⁶⁵ Further the company's memorandum of incorporation may require a special resolution to approve any other matter which does not require a special resolution in terms of the Companies Act.⁶⁶ Section 66(1) and (5)(b)(i) of the Companies Act makes it permissible for a company to limit the powers of its directors in a company's memorandum of incorporation.

Though section 48 of the Companies Act is considered as an unalterable provision, a company may still regulate repurchases in its memorandum of incorporation only to the extent that it imposes a greater standards or restrictions.⁶⁷ Thus a company is permitted to regulate repurchases in its memorandum of incorporation including providing for the shareholders' approval of all repurchases as well as appropriate measures to protect shareholders from the dangers of selective repurchases. The memorandum of incorporation may, subject to the provisions of the Companies Act, be utilised to classify repurchases, with those that requires a zero (for instance a repurchase from retiring employees excluding directors), and/or certain percentages (repurchases from directors) and/or an unanimous approval by shareholders (repurchase resulting in significant changes to the company structure). A company may also restrict or negate or limit powers of the directors to conduct repurchases in accordance with the provisions of its memorandum of incorporation.

4.2.9. Duties and liabilities of directors

The Companies Act requires directors of a company when acting in their capacity to exercise their powers and perform their functions for a proper purpose and in the best interests of a company.⁶⁸ Van der Linde however points that although directors must act in the best interests of the company only, however the Companies Act indirectly requires directors to conduct business in a manner that does not adversely or prejudice the interests of its shareholders.⁶⁹

⁶⁵ s 15(2) of the Companies Act.

⁶⁶ s 65(12) of the Companies Act with subsection (11) containing a list of transactions that require a special resolution.

⁶⁷ Section 1 of the Companies Act defines an alterable provision as a provision which is expressly contemplated in terms of the Companies Act that its effect on a company may be negated, restricted, limited, qualified, extended or otherwise altered in substance or effect by the company's memorandum of incorporation.

⁶⁸ s 76(3) of the Companies Act.

⁶⁹ Van der Linde (*Share repurchases*, n 11) 304.

Section 76(2) of the Companies Act provides that a director of a company must not use his position of a director to gain advantage for the director or for a person other than the company. This provision stands to protect directors from determining a repurchase whereby corporate interests are in conflict with director's personal interests. In *Unocal* the American court indicated that "it has long been recognised that the court must bear in mind the inherent danger in the purchase of shares with corporate funds to remove a threat to corporate policy when a threat to control is involved in such cases. The directors are of necessity confronted with a conflict of interests, and an objective decision is difficult."⁷⁰ Thus directors who are shareholders should not use corporate funds to repurchase shares if such repurchase will confer on them more control over the company, as that would definitely amount to a conflict of interest and abuse of corporate funds.

Directors have a duty to ensure that repurchases are conducted in full compliance with the provisions of the Companies Act and the memorandum of incorporation of a company, failing which their conduct will render them liable to the company.⁷¹ Section 48(7) read with section 77(2)(b) of the Companies Act provides that a director of a company is liable for any loss, damages, or costs sustained by the company as a consequences of the director having been present at a meeting, or participated in a meeting where a decision to acquire shares of the company, and failed to vote against the acquisition by the company of any of its shares of its holding company, despite knowing that the acquisition was contrary to section 46 or 48 of the Companies Act.

Section 218(2) of the Companies Act also provides that a person who contravenes the provisions of the Companies Act will be liable to any person for any loss or damage suffered by that person as a result of that contravention. A director may also be liable to a shareholder in terms of section 20(6) of the Companies Act for any damages suffered by a shareholder as a result of director intentionally, fraudulently or due to gross negligence contravening any provision of the Companies Act or any provision of the company's memorandum of incorporation.

⁷⁰ *Unocal Corp v Messa Petroleum Co* 493 A 2d 985 (1985) 954 – 955.

⁷¹ Van der Linde (*Share repurchases*, n 11) 303.

5. Selective repurchases in terms of the JSE Listings Requirements

In terms of the JSE Listings Requirements⁷² repurchases must be conducted by means of specific (selective) or general offers.⁷³ A selective repurchase must comply with the memorandum of incorporation of a company, be approved by a special resolution of shareholders and be accompanied by a statement of the directors confirming that the repurchase is in accordance with the provisions of sections 4 and 48 of the Companies Act.⁷⁴ The Listings Requirements also require directors to issue a circular and a statement confirming that the selective offer is fair insofar as the shareholders of the company are concerned and that the board of directors has been so advised by an independent expert acceptable to the JSE that selective repurchases is fair to shareholders of the company.⁷⁵ The rules also provide that in any specific offer, a vote of any shareholder and his or her associates that are participating in a repurchase must be excluded from the required special resolution.⁷⁶ An associate of an individual or a director includes a person's immediate family member, a trustee of company in which a director has beneficial interests, a company or close corporation which a director has beneficial interests subject to holding a prescribe percentage of voting rights.⁷⁷

The Listings Requirements also restrict the price to be paid for repurchased shares to be agreed between the company and a shareholder at a weighted average traded price of such equity securities measured over the 30 business days prior to the date of a repurchase.⁷⁸ This measure ensures that the repurchase price is fair to both the company and shareholders. The Listings Requirements also prescribe a limit on a percentage of shares to a maximum of 20% in aggregate that a company is allowed to repurchase in a single financial year.⁷⁹ A company may only conduct general repurchases if authorised in terms of its memorandum of incorporation and without prior

⁷² Johannesburg Stock Exchange Limited Listings Requirements Service Issue 17 (hereinafter referred to as JSE Listings Requirements). The discussion of the JSE Listings Requirements was based on Van der Linde article titled "Share repurchases and the protection of shareholders" 2010 *TSAR* 288.

⁷³ Rule 11.23 of the JSE Listings Requirements, in relation to specific repurchases and Rule 11.26 in relation to general repurchases.

⁷⁴ Rule 5.69(a) and (c) of the JSE Listings Requirements.

⁷⁵ Rule 11.23 and 11.25 of the JSE Listings Requirements. The circular must set out sufficient prescribed particulars to enable shareholders to properly exercise their voting rights on the matter.

⁷⁶ Rule 11.23(d) and 5.69(b) of the JSE Listings Requirements.

⁷⁷ A comprehensive definition of an associate is contained in the definition section of the JSE Listings Requirements.

⁷⁸ Rule 5.69(e)(ii) of the JSE Listings Requirements.

⁷⁹ Rule 5.68 of the JSE Listings Requirements.

arrangement between the company and the other party to a repurchase.⁸⁰ It was submitted that the rule against pre-arranged repurchases is a safeguard against effecting selective repurchases.⁸¹

6. Evaluation of the South African protective measures

In South Africa repurchases are regulated in terms of the Companies Act. In terms of the Companies Act, there is no distinction between proportionate and selective repurchases. Directors are at liberty to conduct repurchases either selectively or proportionately. There is one set of requirements applicable to all repurchases of shares. All repurchases must be approved by the board and satisfy the solvency and liquidity test as well as the requirements of a distribution in relation to repurchase as contemplated in section 46 of the Companies Act. In addition repurchases from directors or prescribed officers and their related persons, or repurchases of shares exceeding 5% of the company's issued shares or repurchases conducted in terms of a scheme of arrangement must be approved by a special resolution of shareholders.

In terms of section 48 a repurchase of shares in excess of 5% of the company's issued shares must meet the requirements of section 114 and 115. However, section 114 is not only applicable to repurchases of more than 5% of the company's issued shares but also to repurchases not exceeding 5% of the company issued shares provided that such repurchases are still undertaken in terms of a scheme of arrangement. This raises a question what would be the company's ground for invoking section 48 or section 114 when a repurchase involves the acquisition of shares of less than 5% of the company's issued shares. The distinction in respect of regarding the choice in respect of repurchases of less than 5% of the company's issued shares should be conducted is unclear. However the distinction was perhaps that section 48 was designed to deal with repurchases that does not refine the company's capital structure and whereas section 114 was meant for repurchases that are meant to change the capital structure of a company.⁸²

The reason for subjecting all repurchases to different requirements is from a shareholder protective point unclear particularly when the effect of repurchases on the interests of a shareholder may be

⁸⁰ Rule 5.72(a) and (b) of the JSE Listings Requirements.

⁸¹ Van der Linde (*Share repurchases*, n 11) 301.

⁸² Cassim (*Contemporary Company Law*, n 1) 304.

similar. The effect on the interests of two targeted shareholders selling 6% (with each selling 3%) of their shares and together the shares constituting 6% of the company's issued shares, is similar to a company repurchasing 3% of one shareholder's shares constituting 3% of the company's issued shares. The selling shareholder interests were diminished by three percent in both scenarios. However as the repurchase in the first scenario is in excess of 5% of the company's issued shares the repurchase must be conducted in terms of a scheme of arrangement with better protective measures compared to the second scenario where the company is not compelled to comply with the requirements for repurchases conducted in terms of a scheme of arrangement.

The solvency and liquidity requirement is a protective measure applicable to all repurchases as it may act as a barrier to repurchases by financially strained companies. The test does to some extent offer protection to remaining shareholders though it was aimed at protecting the interests of creditors not necessarily shareholders. In addition to the solvency and liquidity requirements, the shareholders' approval requirement may also protect shareholders in particular by guaranteeing them a right to participate in key decisions in a company. In terms of the Companies Act only repurchases from directors or repurchases conducted in terms of a scheme of arrangement requires approval from shareholders and the shareholders are thus excluded from participating in any other repurchases unless the memorandum of incorporation of a company provides otherwise. Cassim *et al* indicate that "it is questionable whether shareholders should be excluded from the making of such a significant decision. Their interests and not only those of creditors are also at stake."⁸³ Shareholders' approval requirement may be considered as a watchdog and may prevent the directors from abusing their positions to benefit themselves.⁸⁴

Delpont and Vorster indicates that the requirements of section 48(8) of the Companies Act in relation to shareholders' approval requirements, may go some way to protect shareholders from abuse of power by the directors, as other reacquisitions are not subject to a special resolution.⁸⁵ Blackman *et al* indicate that the fundamental protection afforded to shareholders is the requirement that repurchases be approved by a special resolution of shareholders.⁸⁶ A shareholders' approval

⁸³ Cassim (*Contemporary Company Law*, n 1) 303.

⁸⁴ Ibid.

⁸⁵ Delpont and Vorster (n 25) 207.

⁸⁶ Blackmann *et al* (n 3) (2012) 5 64.

requirement may prevent any ulterior motive and any collusion between directors and some shareholders for conducting repurchases to the detriment of other shareholders.

It must be noted that shareholders' approval may in some instances be subject to abuse. It was submitted that although shareholders' approval protects shareholders, majority shareholders will always influence the outcome of a special resolution and outvote the minority, as the shareholders without significant voting power will always have to abide by the decision of the majority.⁸⁷ However, as Van der Linde indicates, a shareholder resolution may afford even better protection if the required resolution is enhanced by voting restrictions imposed on shareholders whose shares are being acquired.⁸⁸ Voting restrictions imposed on directors of the company and shareholders will effectively manage potential conflict of interest and will ensure that directors or shareholders do not initiate and participate in a repurchase that is aimed at benefiting themselves.⁸⁹

An approval of shareholders may not be necessary when a company repurchases shares on a pro-rata basis and in particular where a repurchase does not result in any significant changes to the percentage of the shareholders' stake in a company. An approval by shareholders may constitute a hurdle when repurchasing shares from retiring employees, and deceased and insolvent estates.⁹⁰ These are non-contentious selective repurchases in terms of which directors should be empowered to conduct without the approval of shareholders. These repurchases should obviously not result in any significant changes in the company's structure and remaining shareholders' stake in a company.⁹¹ If these repurchases result in any significant change it must be approved by a special resolution of shareholders or alternatively approved by the court.

Further, the court may be approached to set aside a decision to implement a selective repurchase. Firstly in terms of section 48(6) of the Companies Act any decision to repurchase shares, stands to be set aside by the court if such decision contravenes the Companies Act. Secondly a shareholder

⁸⁷ Van der Linde (*The regulation*, n 15) 42.

⁸⁸ Van der Linde (*Share repurchases*, n 11) 288.

⁸⁹ Sections 75(2)(a)(i)(aa) and 75(5)(5)(a) of the Companies Act. Section 115(4) of the Companies Act.

⁹⁰ Cassim (*Contemporary Company Law*, n 1) 304. Van der Linde "Share repurchases and the protection of shareholders" (2010) *TSAR* 288 289. See also Cassim *The Practitioner's Guide to the Companies Act of 2008* (2011) 117.

⁹¹ Cassim (*Contemporary Company Law*, n 1) 304.

is at liberty to apply for a review of a company's decision to implement a repurchase of shares conducted in terms of a scheme of arrangement if the shareholder objected and voted against a resolution to implement such repurchases.⁹² Any shareholder whose interests stand to be prejudiced by a repurchase decision may apply to court for an order preventing a company from implementing any action prejudicial to his or her interests.

The protective measures specific to repurchases from directors and repurchases conducted in terms of a schemes of arrangement is to some extent satisfactory. These measures include the requirement that directors should not participate in a board decision if they have financial interests unless the matter concerns all directors, that repurchases must be approved by special resolution of shareholders, and a disclosure requirements. The disclosure requirements ensure that shareholders are informed about the nature and effect of the proposed resolution.

Moreover a shareholder may also approach a court, in respect of repurchases conducted in terms of a scheme of arrangement, to enforce an appraisal remedy by demanding that the company pays a fair value in respect of the repurchased shares. It must be noted that a remedy may be enforced without necessity of the court enforcement processes, a shareholder will have to approach the company first before approaching the courts. The reasons for excluding this remedy to other repurchases other than repurchases conducted in terms of a scheme of arrangement is unclear. It was submitted that the reasons for such exclusion is based on a submission that such repurchases were meant for uncontroversial and pre-agreed repurchases, which may never trigger any appraisal remedy.⁹³ The right to demand that a fair value be paid for repurchased shares must be extended to all shareholders and in all repurchases.

Minority shareholders of regulated companies are further protected through enforcing a right to be paid out of a company after any repurchase of shares with voting rights which resulted in a rights holder acquiring shares in excess of more than 35% of the voting rights. In addition to the Companies Act the JSE Listings Requirements also regulates repurchases for companies listed on

⁹² s 115(3)(a) and (b) of the Companies Act. See also (n48) and in particular section 115(3) for specific grounds to review a decision to implement a repurchase.

⁹³ Cassim (*Contemporary Company Law*, n 1) 302.

the JSE. Shareholders who subscribed for shares in the JSE listed companies will benefit from the protection measures as contained in the JSE Listings Requirements including the shareholder approval requirement, disclosure requirement regarding the fairness of a repurchase on the interests of the company and shareholders, elimination of potential conflicts of interests and assurance to be paid a fair value of shares should a repurchase succeed.

7. Selective repurchases in New Zealand

7.1. Requirements for selective repurchases

In New Zealand repurchases of shares are regulated under the New Zealand Companies Act 1993. The New Zealand Companies Act provides for repurchases to be conducted through proportionate offer to all shareholders or by means of a selective offer to one or more of the shareholders.⁹⁴ The scope of this paper is however limited to a discussion of protective measures in selective repurchases. The New Zealand Companies Act allows directors to make a selective offer to one or more of the shareholders to selectively repurchase shares.⁹⁵ Selective offers must be approved by a written consent of all shareholders, and if not approved by a written consent of all shareholders it must at least be in accordance with the constitution (memorandum of incorporation) of a company and meet the requirements of section 61.⁹⁶

In terms of section 60(3)(a) the New Zealand Companies Act a selective repurchase may be conducted if the board has previously resolved that the acquisition is in the best interests of the company. In addition a selective repurchase which does not require unanimous resolution of shareholders must in terms of section 61 be accompanied by the directors' resolution that the terms of the offer and consideration to be paid are fair and reasonable to the remaining shareholders and that the acquisition is of benefit to remaining shareholders.⁹⁷

It is also permissible in New Zealand that a selective repurchase may be conducted in any other manner other than in terms of sections 60 and 61 provided all shareholders give consent to a

⁹⁴ s 60(1) of the New Zealand Companies Act.

⁹⁵ s 60(1)(b) of the New Zealand Companies Act.

⁹⁶ s 60(1)(b) of the New Zealand Companies Act.

⁹⁷ s 60(1)(b)(ii) read with section 61(1) of the New Zealand Companies Act.

repurchase.⁹⁸ In terms of section 107(1)(c) of the New Zealand Companies Act any repurchase of shares conducted outside the requirements of the Companies Act must be approved by an unanimous consent of all shareholders.

The New Zealand Companies Act requires the board to pass certain determinations before implementing any repurchase proposal. Firstly the board must resolve that a repurchase is in the best interests of the company.⁹⁹ Secondly the board must resolve that the terms of the offer and the consideration offered for the shares are fair and reasonable to the company.¹⁰⁰ Thirdly directors must resolve that they are not aware of any information that will not be disclosed to shareholders which is material regarding the assessment of the value of shares, and as a result of which the terms of the offer and consideration offered for the shares will be unfair to shareholders accepting the offer.¹⁰¹

The board is prohibited from implementing repurchases of shares should at any time after the resolution, it transpire that a repurchase is no longer in the best interests of the company, or terms and consideration offered are no longer fair and reasonable to the company, or that material information on the value of the shares was never disclosed or that the repurchase is no longer in the best interests of the company.¹⁰² In addition to the above resolution directors can only conduct a repurchase if it complies with the solvency test immediately after a particular repurchase.¹⁰³

Procedurally section 61(1) read with section 62 of the New Zealand Companies Act requires directors to issue and send to all shareholders a document setting out the nature and terms of the offer, and if made to specified shareholders, to whom it will be made; and the nature and extent of any relevant interests of any director on shares offered; and the nature and extent of the resolution required, together with such further information and explanation as may be necessary to enable a reasonable shareholder to understand the nature and implications of the proposed repurchase for the company and its shareholders.

⁹⁸ s 107(1)(c) of the New Zealand Companies Act.

⁹⁹ s 60(3)(a) of the New Zealand Companies Act.

¹⁰⁰ s 60(3)(b) of the New Zealand Companies Act.

¹⁰¹ s 60(3)(c) of the New Zealand Companies Act.

¹⁰² s 60(6) and 61(4) of the New Zealand Companies Act.

¹⁰³ s 108 of the New Zealand Companies Act.

The New Zealand Companies Act entitles a shareholder or former shareholder of a company who considers that the affairs of a company are being or are likely to be conducted in a manner that is oppressive, unfairly discriminatory, or are unfairly prejudicial to him or her in that capacity or in any other capacity, to apply to the court for relief.¹⁰⁴ Section 61(4) of the New Zealand Companies Act also protects shareholders by requiring that an offer to selectively repurchase shares and the consideration paid for shares be fair and reasonable to the company and remaining shareholders.

Section 169 of the New Zealand Companies Act entitles shareholders to bring an action against a director for breach of any duty that directors owe to shareholders. The New Zealand court in *Coleman v Myers*¹⁰⁵ held that although there is no general fiduciary duty between a shareholder and a company, a fiduciary duty is however created the moment directors decide that the company will repurchase its shares.¹⁰⁶ This suggests that in a repurchase of shares directors are expected to consider the interests of shareholders and disclose any information that can affect the interests of shareholders.

7.2. Evaluation of protective measures in New Zealand

Selective repurchases must be approved by unanimous resolution of all shareholders or if not approved by unanimous resolution of all shareholders must be conducted in accordance with the constitution of a company, sections 60 and 61 of the New Zealand Companies Act. The protective measures applicable to selective repurchases never approved by unanimous resolution of shareholders include the requirement that a selective repurchase must be in the best interests of the company and that of the remaining shareholders.¹⁰⁷ The requirement that repurchase must be in the best interests of a company suggests that in any decisions that the board takes the best interests of the company must be paramount. In *Unocal Corp*¹⁰⁸ the American court held that “when a board addresses a pending takeover bid it has an obligation to determine whether the offer is in the best interests of the corporation and its shareholders.”¹⁰⁹

¹⁰⁴ s 174 of the New Zealand Companies Act.

¹⁰⁵ *Coleman v Myers* [1977] 2 NZLR 91, 96.

¹⁰⁶ *Ibid.*

¹⁰⁷ Section 60(3)(a) of the New Zealand Companies Act.

¹⁰⁸ *Unocal Corp v Messa* (n 70) 985.

¹⁰⁹ *Ibid.*

Acting in the best interests of the company may allow a repurchase with an ulterior motive to succeed provided that directors are able to prove that the primary purpose for furthering a repurchase is to respond to the best interests of the company.¹¹⁰ It was indicated that a selective repurchase of shares which is unfair to a minority shareholder may stand to be allowed on the ground that directors exercise reasonable business judgment or acted in the best interests of the company.¹¹¹ It was held that “unless it is shown by a preponderance of the evidence that the directors' decisions were primarily based on perpetuating themselves in office, or some other breach of fiduciary duty such as fraud, overreaching, lack of good faith, or being uninformed, and a court will not substitute its judgment for that of the board.”¹¹²

Further shareholders are protected by being entitled to approach the court for any decision regarding the fairness of repurchases and for an order restraining a repurchase.¹¹³ It also ensures equitable treatment and prevents discrimination amongst shareholders; and between the company and a selling shareholder.¹¹⁴

It was indicated that a selective repurchase of shares must be consistent with the principle that a minority shareholder must receive the substantial equivalent in value of what he had before.¹¹⁵ The court indicated that a fair value of the shares must be paid for any investment in shares.¹¹⁶ A proper scrutiny of the New Zealand Companies Act highlights that the end objective of an appraisal remedy being to be paid a fair value of the shares is also available to repurchases because specific provisions are contained in the New Zealand Companies Act that ensures or guarantees payment of fair value for shares.¹¹⁷

¹¹⁰ Van der Linde (*Share repurchases*, n 11) 297.

¹¹¹ Hutchins (n 19) 280.

¹¹² *Unocal Corp v Messa* (n 70) 995. Delpont & Voster (n 25) 570.

¹¹³ Sections 61(8) and 174 of the New Zealand Companies Act.

¹¹⁴ Cassim (*The reform of company law*, n 56) 286.

¹¹⁵ *Unocal Corp v Messa* (n 70) 596.

¹¹⁶ *Herzog v Hertli and Others* [2009] NZHC 1571. This case was however concerned with sale of shares and not entirely a repurchase.

¹¹⁷ Section 61(1)(b) of the New Zealand Companies Act.

In New Zealand a company is permitted to regulate repurchases in its memorandum of incorporation.¹¹⁸ Self-regulation was intended to facilitate the exit of shareholders without the need to comply with the lengthy provisions of the New Zealand Companies Act.¹¹⁹ A unanimous resolution was inserted into the New Zealand Companies Act to protect shareholders from unfair selective repurchases regulated through the constitution of the company.¹²⁰ A repurchase conducted in accordance with the memorandum of incorporation must still follow the process enshrined in the New Zealand Companies Act and if not it must be approved by a unanimous resolution of all shareholders.¹²¹

Further section 61(8) of the New Zealand Companies Act entitles a shareholder of a company to apply to court for an order restraining the proposed repurchase. The restraint application must be based on the grounds that the proposed acquisition is not in the best interests of the company and of benefit to remaining shareholders; and that the terms of the offer or the consideration paid is not fair and reasonable to the company and remaining shareholders.¹²² This mechanism is only applicable to repurchases conducted in terms of section 60(1)(b)(ii) of the New Zealand Companies Act and obviously the remedy is inapplicable in repurchases where all shareholders have consented.¹²³

The New Zealand Law Commission indicated that any action for an unfair repurchase may be brought by a shareholder on the ground that the board has failed to comply with the procedural requirements.¹²⁴ Section 174 of the New Zealand Companies Act entitle shareholders or former shareholders of a company to protect themselves through unfair prejudice remedy available through court processes. Similar to the provision of section 163 of the Companies Act, the court in New Zealand are entitled to make any order it deems fit.¹²⁵ Targeted shareholders may use the provisions of this section to seek any relief if they consider a repurchase to be unfair.

¹¹⁸ Section 60(1)(b)(ii) and s 107(1)(c) of the New Zealand Companies Act.

¹¹⁹ The New Zealand Law Commission Report No. 9: Company Law Reform and Restatement (1989).

¹²⁰ Ibid 57.

¹²¹ s 60(1)(b)(c) read with section 107(1)(c) of the New Zealand Companies Act.

¹²² s 61(8) of the New Zealand Companies Act.

¹²³ s 60(1)(b)(ii) read with s 61(8) of the New Zealand Companies Act.

¹²⁴ (n 119) 133.

¹²⁵ Section 174(2) of the New Zealand Companies Act also lists some of the orders that the court may grant including requiring the company or any other person to acquire the shareholder's shares; payment of compensation to a person;

8. Conclusion

Repurchases pose a serious risks to the interests of shareholders particularly minority shareholders. The dangers of directors abusing their power through repurchases must be alleviated. Protective measures must be designed within the legal prescripts regulating repurchases to thwart any potential abuse of corporate powers. The Companies Act does not provide adequate measures aimed at protecting shareholders in selective repurchases. The Companies Act provides for different shareholder protective measures for selective repurchases conducted in terms of sections 48(8) and 114 of the Companies Act and overlooks the effect of all elective repurchases on the interests of all shareholders. Although the solvency and the liquidity test may be of benefit to all shareholders, the test was aimed at protecting the interests of creditors rather than shareholders. This measure appears to be the only protective measure applicable to all repurchases.

Shareholders in selective repurchases conducted through a scheme of arrangement benefit from further protective measures. These measures include shareholders' approval requirements, the appraisal remedy, disclosure requirements and the court review process. The legislature's failure to extend these measures to other repurchases except for repurchases conducted in terms of a scheme of arrangement may be attributed to reasoning that such repurchases were meant for non-contentious situations.¹²⁶ Though the appraisal remedy is available to shareholders who voted against a repurchase, a selling shareholder's right to demand to be paid a fair value of shares, must be extended to all repurchases.

The distinction between section 48 and 114 requirements, in so far as it relates to a repurchase of company's issued shares not exceeding 5% is unclear. It must be made clear as to what will inform the decision of a company to invoke section 48 and not section 114. If sections 48 and 114 were intended for non-controversial repurchases and major repurchases respectively such distinction must be clearly provided in the Companies Act.¹²⁷ While acknowledging that shareholders' approval remain a necessary measure of protection, it may be unnecessary for some kind of repurchases, such as repurchasing shares from retiring shareholders, employees and shares of

altering or adding to the company's constitution; or setting aside action taken by the company or the board in breach of the New Zealand Companies Act or the constitution of the company.

¹²⁶ (n 91).

¹²⁷ Ibid.

deceased shareholders holding shares which may not significantly change voting rights, control or ownership in a company.¹²⁸ In cases where repurchases pose a danger of any significant changes to the company structure or voting rights a unanimous consent of all shareholders must be obtained before a repurchase can be implemented. If consent is withheld by shareholders, directors acting in the best interests of the company or any person with an interests on a matter (for instance a shareholder or an executor of estate) must be afforded an opportunity to approach the court for an order approving a repurchase.

The use of shareholders remedies such as relief from oppressive conduct will depend on how quick these actions are finalised in courts and shareholders bearing the cost of protecting their interests through litigation. There are further internal hurdles in these remedies that shareholders may be required to prove for the action to succeed.

Unlike in South Africa, the New Zealand Companies Act requires selective repurchases to be approved by all shareholders and if not, is subject to ideal protective measures such as the disclosure requirement, observance of the best interests of the company and shareholder, and that the price paid for shares must be fair to the company and the remaining shareholders. In South Africa, and in respect of repurchases conducted in terms of a scheme of arrangement shareholders benefit from the appraisal remedy and also from the requirements that the expert's report must contain information relating to the value of shares.

Further companies in New Zealand are free to regulate repurchases in their memorandum of incorporation in terms of their own requirements. The measure in place to guard against abuse is that a selective repurchase that differs to the procedure and requirements of the New Zealand Companies Act, must be approved by a unanimous resolution of all shareholders.¹²⁹ In South Africa repurchases can be regulated in the memorandum of incorporation by restricting the powers of directors to conduct a repurchase, requiring special resolution of shareholders or providing for

¹²⁸ Cassim (*Contemporary Company Law*, n 1) 304. Van der Linde "Share repurchases and the protection of shareholders" (2010) *TSAR* 288 289. See also Cassim *The Practitioner's Guide to the Companies Act of 2008* (2011) 117.

¹²⁹ s 107(1)(c) of the New Zealand Companies Act.

highest standards for repurchases than provided for in the Companies Act.¹³⁰ This may significantly protect shareholders as companies can limit powers of directors to repurchase shares in the memorandum of incorporations.

It is proposed that the provisions relating to share repurchases with the purport of protecting the interests of shareholders can be framed in the following:

- While considering that it may be a challenge to classify repurchases, classifications of selective repurchases with those that requires a zero (for instance a repurchase from retiring employees excluding directors), and/or certain percentages (repurchases from directors) and/or an unanimous approval by shareholders (repurchase resulting in significant changes to the company structure) may be ideal;
- Self-regulation, as already done by most companies, assists companies to classify how repurchases should be conducted in a company but the requirements relating to shareholders' approval should remain an unalterable provision;
- A right of all dissenting shareholders to approach the court for recourse must be made available to all shareholders in selective repurchases;
- The price to be paid for acquiring shares must be at a fair value; and
- Repurchases must be disclosed to shareholders prior to implementation, whether or not shareholders are required to vote on a matter, this will ensure that directors whose interest are affected a repurchase transaction are able to timely protect themselves.

In its current form the Companies Act does not adequately regulate repurchases with the objective of protecting the interests of shareholders in selective repurchases. Thorough measures are required to lessen the hardship that shareholders may face and to minimise any possible abuses of powers by the directors.

¹³⁰ (n 81).

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