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THE MEANING OF “ARRANGEMENT” IN THE COMPANIES ACT 71 OF 2008

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1. INTRODUCTION

Business acquisitions, schemes of arrangement and takeover offers constitute three methods of obtaining control of a company. Schemes of arrangement are suggested to be the most popular of the three methods as they are regarded to be a considerably more flexible means of effecting a takeover than either a business acquisition or a takeover offer.\(^1\)

Essentially, a scheme of arrangement permits an offeror company to use the target company to negotiate an arrangement with its shareholders in a collective manner. Once agreement of a 75% majority is obtained, all shareholders, including dissenting shareholders, are bound to the arrangement. Prior to the introduction of schemes of arrangement, the rights of shareholders of a target company could only be altered with the consent of each individual shareholder.\(^2\)

Due to the growth of the corporate market, the advent of large group companies and the resultant increase in company membership, the process of acquiring individual shareholder consent became increasingly problematic and ineffective.\(^3\) Frequently, the individuals with whom companies wanted to negotiate were either not party to the specific contract or the rights under consideration were encumbered by a contract that rendered their amendment impermissible which presented further challenges.\(^4\) Schemes of arrangement were thus introduced to offer a commercially practical solution.

Under the Companies Act 61 of 1973 (the 1973 Act), schemes of arrangement were regulated by sections 311 to 313. Following the sanctioning of a scheme by the English Courts in \textit{In re National Bank Ltd}\(^5\) (which resulted in one person acquiring control of all the issued shares of a company) section 311 began to be utilised as a means of eliminating minority shareholders in order to achieve a takeover of a company, although not originally intended for that purpose.\(^6\) Various issues arose in this context with the main underlying concern being shareholder protection.

Consequently, it became increasingly important to determine what exactly constituted an “arrangement”. This resulted in a line of judicial decisions concerning the interpretation of section 311. The comparable provision regulating a scheme of arrangement between a regulated company and its shareholders is now captured in section 114 of the Companies Act 71 of 2008 (the 2008 Act). Despite listing various methods that may be included in a scheme

\(^1\) Luiz “Protection of holders of securities in the offeree regulated company during affected transactions: General offers and schemes of arrangement” 2014 SAMLJ 561.
\(^3\) Ibid.
\(^5\) \textit{In re National Bank Ltd} 1966 1 (WLR) 81; 1966 1 (All ER) 1006 ChD.
\(^6\) Luiz “Using a scheme of arrangement to eliminate minority shareholders” 2010 SAMLJ 443.
of arrangement, the legislature failed to provide adequate clarity by leaving the term “arrangement” undefined.

In interpreting the meaning of “arrangement” under section 311, two particularly contentious topics came under judicial scrutiny namely; whether instances of expropriation constituted an arrangement and whether a re-acquisition by a company of its securities was permissible under this mechanism. Given that an arrangement remains undefined under the 2008 Act, it is necessary to determine whether the judicial view taken on these topics continues to apply to arrangements that fall under section 114. In order to do so, section 311 of the 1973 Act and the applicable body of case law together with section 114 and related provisions of the 2008 Act must be analysed. Specific consideration will be given to notable differences between the two regimes and further observations will be made on schemes of arrangement in the United Kingdom.

2. THE AMBIT OF “ARRANGEMENT” UNDER THE 1973 ACT

2.1 SECTION 311

Section 311(1) and (8) provided as follows:

“311. Compromise and arrangement between company, its members and creditors.

(1) Where any compromise or arrangement is proposed between a company and its creditors or any class of them or between a company and its members or any class of them, the Court may, on the application of the company or any creditor or member of the company or, in the case of a company being wound up, of the liquidator, or if the company is subject to a judicial management order, of the judicial manager, order a meeting of the creditors or class of creditors, or of the members of the company or class of members (as the case may be), to be summoned in such manner as the Court may direct...

(8) In this section…the expression ‘arrangement’ includes a reorganization of the share capital of the company by the consolidation of shares of different classes or by the division of shares into shares of different classes or by both these methods.”

In the mid-1980s a series of contradictory decisions were handed down on how wide a construction should be given to the term “arrangement” which demonstrated how divided judicial opinion on the issue was. An overview of selected case law follows below.

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2.2 A JUDICIAL PERSPECTIVE

In *Ex parte Federale Nywerhede Bpk*\(^8\) the court accepted that section 311 could be used to effect a reduction of capital but did not deal with the matter extensively. It was held that for section 311 to apply, the scheme must be a scheme and that it must be between the company and its shareholders. It was further held that, if this is not the case there are no mutually enforceable rights and thus no arrangement. The court referred in this context to the decision in *Re NFU Development Trust Ltd*\(^9\) where it was stated that a member whose rights are expropriated without any compensating advantage is not having his rights rearranged. What was referred to here was expropriation without compensation. Expropriation with compensation was therefore not excluded from the ambit of an arrangement.\(^10\)

A reduction of capital was again dealt with in *Ex parte JR Starck & Co (Pty) Ltd*\(^11\) where it was considered whether it could be used to extinguish shares as opposed to acquiring them. It was held that a scheme may be effected in conjunction with a reduction of capital provided that the relevant requirements are met in doing so.

The courts in *Ex parte Satbel (Edms) Bpk: In re Meyer & Andere v Satbel (Edms) Bpk*\(^12\) and *Ex parte Natal Coal Exploration Co Ltd*\(^13\) considered whether instances of expropriation or compulsory purchase by a company (or a third person) of member’s shares constituted an arrangement.\(^14\) In *Ex parte Satbel* the application made to sanction the scheme was refused, among others, because there was an expropriation and not a “reorganisation or rearrangement of the rights of the shareholders…”. In the *Ex Parte Natal Coal* case the court held, according to the *dictum* in *Ex parte Federale Nywerhede Bpk*, that an expropriation by other means of at least some of the scheme shares is not impossible, but that it cannot be done by means of section 311.\(^15\) Thus, in both cases the schemes were regarded as falling outside the scope of section 311. The courts ruled that, in order to qualify as an arrangement, a scheme must give the members whose shares are to be cancelled a compensating advantage in the form of other rights as opposed to a mere cash payment.\(^16\) The *dicta* in *Ex parte Satbel (Edms) Bpk: In re Meyer v Satbel (Edms) Bpk* and *Ex parte Natal Coal Exploration Co Ltd* were based on an erroneous interpretation of the decision in *Re NFU Development Trust Ltd*.

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\(^8\) *Ex parte Federale Nywerhede Bpk* 1975 1 SA 826 (W). The discussion that follows is informed by the overview in, among others, Delport P “Section 311 of the Companies Act and the ‘Share Cases’” 1994 De Jure and Lehloenya PM “The debate on the meaning and application of ‘arrangement’: Before and after Senwes v Van Heerden & Sons” 2007 19 SAMLJ.

\(^9\) *Re NFU Development Trust Ltd* 1973 1 (All ER) 135.


\(^12\) *Ex parte Satbel (Edms) Bpk: In re Meyer v Satbel (Edms) Bpk* 1984 4 SA 347 (W).

\(^13\) *Ex parte Natal Coal Exploration Co Ltd* 1985 4 SA 279 (W).

\(^14\) Lehloenya PM “The debate on the meaning and application of ‘arrangement’: Before and after Senwes v Van Heerden & Sons” 2007 19 SAMLJ 528.

\(^15\) Delport (n 10) 171.

\(^16\) Lehloenya (n 14) 528.
The court in *Ex parte Suiderland Development Corporation*\(^\text{17}\) challenged and disposed of the above inaccurate reasoning by authorizing the application of the section 311 procedure in circumstances involving the expropriation of minority shares, finding that there was no reason why the compensating advantage referred to in the two earlier decisions could not be constituted by the payment of money alone.\(^\text{18}\)

The decision in *Ex parte NBSA Centre Ltd*\(^\text{19}\) concerned a further aspect of the debate. The court held that it was unlawful to effect a reduction of capital by way of an arrangement providing for a company’s compulsory purchase of its own shares under section 311. In such circumstances, the prescribed procedure for reduction of capital in sections 83 to 89 had to be employed.\(^\text{20}\) The importance of the decision was that there was a reappraisal of the section 311 procedure and its application. The requirements prescribed by the court for when section 311 will apply were articulated by Coetzee DJP as follows:

> 1. Only a scheme or part of it which *necessitates* the invocation of s 311 is an arrangement, provided further that it is not illegal or *ultra vires* the company.

> 2. *A fortiori*, any scheme or part of it in respect of which an exclusive procedure for its attainment is prescribed is not an arrangement. It can only be achieved by employing the prescribed machinery. Such a scheme is one which involves a reduction of capital when the applicable procedure under ss 83 - 89 of the Act must be followed.

> 3. If one part of a scheme involves a reduction of capital and the other part is an arrangement as it necessitates the invocation of s 311, the first part does not thereby become an arrangement or part of the arrangement. To accomplish that, legally, the reduction procedure must be resorted to and followed. Even if it is embodied in the scheme document which the Court sanctions as an arrangement, it does not thereby become an arrangement which has statutory or any force of law...

> 4. The Court has no jurisdiction to allow what is not an arrangement to be dealt with as an arrangement under s 311. It does not have the discretion to sanction such a scheme or to order scheme meetings...

> 5. Only an arrangement *between* the company and its members or creditors or a class thereof can be an arrangement. When members’ shares are to be transferred to or are to be obtained by a third person or other members of the company, this question arises. In every case it will have to be determined on a consideration of all the relevant aspects of the scheme and the surrounding facts whether it is such an arrangement *between* the company and its members or creditors.

> 6. The application in *Natal Coal* was correctly refused although the *ratio decidendi* was defective. It should have been refused for the reason that the cancellation of the shares against payment by the company was a reduction of capital which could be achieved solely by application of the reduction procedure. The purported arrangement was for that reason not an arrangement within s 311.\(^\text{21}\)

The above summary was referred to as the use of “arrangement” as strictly an arrangement within section 311 and not any so-called arrangement or “scheme” in a wide sense to denote

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\(^{17}\) *Ex parte Suiderland Development Corporation* 1986 2 SA 442 (C).

\(^{18}\) Lehloenya (n 14) 528.

\(^{19}\) *Ex parte NBSA Centre Ltd* 1987 2 SA 783 (T).

\(^{20}\) Lehloenya (n 14) 530.

\(^{21}\) See n 19 above.
a general plan of reconstruction of rights attaching to shares.\textsuperscript{22} In support of the decision in the NBSA case, \textit{Senwes v Van Heerden and Sons}\textsuperscript{23} emphasised the impropriety of utilising section 311 where the same result could be achieved by agreement and referred to the history and purpose of the section. It should be observed, however, that exceptions were allowed in instances where it was deemed that the protection afforded to the minority shareholders under section 311 was greater than they would receive if another method was relied upon. Nevertheless, the SCA sanctioned the narrow interpretation given to what constitutes an arrangement in the \textit{Senwes} case, shortly before the enactment of the new Companies Act.

3. THE POSITION UNDER THE 2008 ACT

3.1 SECTION 114(1): A BRIEF OVERVIEW

Schemes of arrangement are regulated by Part A of Chapter 5 of the 2008 Act and specifically section 114(1). The section refers to any arrangement between the company and holders of any class of its securities “by way of, among other things …”. It then proceeds to list six different methods namely; the consolidation, division, expropriation, exchange, and re-acquisition by a company of its securities, and a combination of these methods. It provides that a company’s board may propose and, subject to obtaining the requisite approvals, implement any arrangement between the company and holders of any class of its securities provided that the company is neither in liquidation nor in the course of business rescue proceedings. The concept of “arrangement” therefore appears to have a wide scope of application in terms of section 114(1).

It is noted that the term “arrangement”, albeit expanded, unfortunately remains undefined. According to Henochsberg,\textsuperscript{24} the consequence of the lack of definition of the term is that the case law relevant to concept under the 1973 Act will still apply. However, academic opinion on this matter appears to be divided. By way of example, Seligson submits that the use of broad categories in delineating the targeted type of transactions is in itself a strong indication that any arrangement between the company and the holders of its securities is likely to fall within the ambit of the provision.\textsuperscript{25}

Whilst section 114(1) is indeed broader than its predecessor, especially considering the inclusions of both expropriation (section 114(1)(c)) and a re-acquisition by a company of its securities (section 114(1)(e)), it is my respectful submission that the reference to “any arrangement” in the aforementioned statement may be founded on far too superficial a reading of section 114(1).

\textsuperscript{22}Ibid.
\textsuperscript{23}Senwes Ltd v Jan van Heerden & Sons CC 2007 3 All SA 24 (SCA) and Leholonya (n 14) 528.
\textsuperscript{24}Delport, Kunst & Vorster, Henochsberg on the Companies Act 71 of 2008 (2011) 410.
Even before the relevant provisions of the 2008 Act were enacted, the possible expansion of schemes that may be achieved through other mechanisms under an “arrangement” received criticism. The obvious concern was that such additions were likely to result in the resurfacing of past uncertainties. The courts repeatedly held that section 311 could only be resorted to if the normal mechanisms for reaching independent agreement between the company and its members was not available, and if it was necessary to resort to the section in order to obtain the consent of all the shareholders. Interestingly, if the line of cases relating to the interpretation of the term arrangement (under section 311 of the 1973) still find application, then not only would it not be mandatory to utilise the provisions of section 114 but it could be impermissible to do so if an alternative procedure is available for obtaining agreement.

It is common cause that schemes of arrangement remain a regular occurrence and a commercial reality especially in the listed environment. It is thus of importance to clear the uncertainty by determining what actually constitutes an arrangement. In an attempt to do so, an expansion and analysis of selected individual methods listed in section 114 will follow.

3.2 EXPROPRIATION OF SECURITIES FROM THE HOLDERS

The requirements in section 114 are clear. Firstly, there must be an arrangement and, secondly, the arrangement must be between the company and the holders of any class of its securities. Section 114(1)(c) provides for expropriation of securities. According to Henochsberg, an expropriation for cash of the shares of one holder of securities by another, or the substitution of securities in one company for securities in another company cannot qualify as an arrangement as envisaged by the section since it does not meet the second requirement, namely that the arrangement must be one between the company and its holders of securities.

If the securities are cancelled by the company and payment, whether in the form of cash or shares, is made by the company, or by a third party for the benefit of the company, both requirements are met. It is therefore not the nature of the consideration that is important, but whether the consideration is as a result of enforceable rights and obligations as between the company and the shareholders. This view is in keeping with the decision in *Ex parte Suiderland Development Corporation* wherein the court authorized the application of the section 311 procedure in circumstances involving the expropriation of minority shares, finding

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26 Lehloenya (n 14) 533.
27 Seligson (n 25) 5.
29 Delport et al (n 24) 412. See also *Ex parte Federale Nywerhede Bpk* 1975 1 SA 826 (W).
30 Ibid. See also *Ex parte NBSA Centre Ltd* 1987 2 SA 783 (T) at 787 and *Jan van Heerden & Seuns BK v Senwes Bpk* 2006 1 All SA 44 (NC) at 58.
31 Delport et al (n 24) 412.
32 See n 17 above.
that there was no reason why compensation could not be rendered by the payment of only money.

In the minority judgment of the NBSA\textsuperscript{33} case, Goldstone J questioned why, if some shareholders agree to their shares being expropriated by another shareholder, that should not be an arrangement within the ambit of section 311.\textsuperscript{34} He said that he had “difficulty in accepting the necessity for introducing a requirement of ‘give and take’ as was done by Brightman J in \textit{Re NFU Development Trust Ltd}”. As per the commentary in Henochsberg, such an expropriation is permissible, but it must occur as a result of an arrangement between the “company and its shareholders” as required by subsection 1 of section 114 and further that it must not be “contrary to general law or \textit{ultra vires} the company”.

It follows therefore that, if expropriation of securities from the holders is effected in terms of section 114, there is no reason why the compensating advantage is to be restricted to anything other than cash. However, if the expropriation for cash is by anybody else but the company and it is not for and on behalf of the company, it is not an arrangement between the company and the holders of the securities.\textsuperscript{35}

Expropriation of securities from the holder may therefore be effected within certain bounds and it appears incorrect to submit that “any arrangement” is catered for within section 114. It remains unclear whether expropriation \textit{without a compensating advantage, ie}, a form of confiscation, may be included within the scope of section 114(1)(c). Even if the existing case law is to provide guidance as proposed above, it is my opinion that the position remains ambiguous since a confiscation was agreed to be excluded from the meaning of an arrangement, but the concept of give and take to which it originally referred was not endorsed.\textsuperscript{36}

3.3 A RE-ACQUISITION BY THE COMPANY OF ITS SECURITIES

Section 114(1)(e) makes provision for re-acquisition by the company of its securities under proposals for schemes of arrangement, whilst section 48 caters for a company acquiring its shares as follows:

“48. Company or subsidiary acquiring company’s shares

(2) Subject to subsections (3) and (8), and if the decision to do so satisfies the requirements of section 46 (a) the board of a company may determine that the company will acquire a number of its own shares...

(8) A decision by the board of a company contemplated in subsection (2)(a) –

\textsuperscript{33} See n 19 above.
\textsuperscript{34} \textit{Ibid}.
\textsuperscript{35} Delport et al (n 24) 412.
\textsuperscript{36} See n 19 above.
(a) 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 prescribed officer of the company; and (b) 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.\(^{37}\)

Whether or not any proposal by a company to re-acquire some of its shares in terms of section 48 would constitute a scheme of arrangement as per section 114(1)(e) is unclear but a proposed arrangement as contemplated in section 114, which may result in the re-acquisition by a company of any of its securities, clearly triggers the application of section 48.\(^{38}\)

In terms of section 48(8)(b) a share buyback is subject to the requirements set out in sections 114 and 115 if it involves the acquisition by the company of more than 5% of any class of issued shares of the company. In addition, the company intending to acquire its own shares will have to comply with the solvency and liquidity test. Although it might not be important to label such a re-acquisition a scheme of arrangement, it might be important to know whether or not, if it involves a regulated company, it would be considered to be a scheme of arrangement as contemplated in section 114.\(^{39}\) If so, it would then fall within the definition of an affected transaction under section 117(1)(c)(iii) and compliance with the applicable legislation and the Takeover Regulations would be required. Moreover, it may mean that the definition of an affected transaction includes a re-acquisition by a regulated company of more than five per cent of the issued shares of any class.\(^{40}\)

Another noteworthy point is that any proposed scheme of arrangement triggers the obligation to appoint an independent expert to report on the transaction. However, a proposed re-acquisition in terms of section 48 which falls outside the context of a scheme of arrangement or which involves a re-acquisition that does not exceed the five per cent threshold triggers no such obligation.\(^{41}\) Although when considering the independent expert’s report the state of the solvency and liquidity of the company may become apparent to the board, neither the statutory provisions regulating the independent expert’s report in section 114 nor the Takeover Regulations specifically refer to the matter of solvency and liquidity. Further, the independent expert is not specifically obliged to consider or express an opinion on this.\(^{42}\)

However, a scheme of arrangement involving the re-acquisition by a company of any of its own securities, regardless of whether or not it is a regulated company, triggers the application

\(^{37}\) The Companies Act 71 of 2008.

\(^{38}\) Luiz “Some comments on the scheme of arrangement as an ‘affected transaction’ as defined in the Companies Act 71 of 2008” 2012 PELJ 104.

\(^{39}\) Ibid.

\(^{40}\) Ibid.

\(^{41}\) Ibid 127.

\(^{42}\) Ibid 128.
of section 48. That in turn potentially triggers the application of section 46 which prohibits distributions by a company unless, among others, the solvency and liquidity requirements in section 4 are complied with. The definition of a distribution includes the transfer of money or property of the company to or for the benefit of shareholders as a consideration for the acquisition of any of its shares under section 48, the solvency and liquidity requirements become relevant.43

Under the 2008 Act, all schemes of arrangement as listed in section 114(1)(a)-(f) require the approval of a special resolution before they can be implemented. However, section 48 does not specifically require shareholders to approve all re-acquisitions by the company of its previously issued shares. It is only if the re-acquisition falls within the provisions of section 48(8) that approval by special resolution is required.44

Thus, there remains much uncertainty as to what the correct interpretation and application of section 114(1)(e) is. The legislature has clearly attempted to resolve previous uncertainties by the inclusion of a re-acquisition by the company of its securities as a type of arrangement under section 114 but has failed in clarifying its operation with related sections and further in defining its exact scope.

3.4 MINORITY SHAREHOLDER PROTECTION

Besides ensuring the integrity of the market, one of the main objectives of regulating takeovers is essentially to protect the interests of existing holders of securities in the offeree company by ensuring that they are fairly treated.45 This fair treatment requires the regulation of affected transactions and conduct of the parties involved to ensure that holders of the same class of voting securities are given equivalent treatment and that other holders of voting securities in the offeree company are afforded equitable treatment.46

The main concern underlying most of the issues relating to schemes of arrangement under section 311 of the 1973 Act was whether shareholders (especially minority shareholders) were being adequately protected.47 In Verimark Holdings Limited and Brait Specialised Trustees (Pty) Limited NO48 a scheme of arrangement was used in an attempt to eliminate the minority shareholders from the company. One of the grounds for objecting to the sanctioning of the scheme of arrangement was that the proposer (who was the majority shareholder of Verimark) and the excluded members were in a class of shareholders different from the shareholders who would be expropriated in terms of the scheme and thus should not have voted at the meeting where the scheme was considered.49

43 Ibid.
44 Ibid.
45 Luiz (n 1) 563.
46 s119(2) of the Companies Act 71 of 2008.
47 Luiz (n 6) 444.
48 Verimark Holdings Limited and Brait Specialised Trustees (Pty) Limited NO case number 2009/22928 (South Gauteng High Court) (unreported).
49 Luiz (n 6) 448.
Malan J dismissed the application for the sanctioning of the scheme not on the grounds that the proposer and the excluded members were in a different class of shareholders from the minority shareholders but on the basis that the offer in the scheme of arrangement was not made to them and thus they should not have voted at all. Malan J thus interpreted the offer as being made only to a part of the class of the ordinary shareholders of Verimark. The offer was made to the scheme participants only. It was only the minority shareholders whose shares would be acquired in terms of the scheme and the decision held by the Court was therefore in accordance with fairness.\(^{50}\)

The provisions in the 2008 Act regulating a scheme of arrangement contain several mechanisms that operate in favour of shareholder protection. The 1973 Act not only required the court to order calling of the meeting(s) at which a scheme of arrangement would be voted on but also required the court to specifically sanction the scheme after it was approved by the requisite majority to make it binding on all the shareholders or class of shareholders. In contrast, the 2008 Act makes the scheme of arrangement dependent on a special resolution passed by the shareholders alone. Where the company is a regulated company, the Takeover Regulation Panel would be required to issue a compliance notice or grant an exemption before the scheme can be implemented.\(^{51}\) There is therefore no further requirement that the court specifically approve a scheme that has already been approved by the shareholders.\(^{52}\)

In accordance with section 114(3), the company must retain a qualified, impartial, independent expert to prepare a report to the board, which must be distributed to all holders of the company's securities, about the proposed arrangement. The report must, among other things, identify the categories of shareholders affected by the proposed arrangement and describe the material effects and evaluate any material adverse effects.\(^{53}\)

Additionally, section 115 introduces several innovative requirements for the greater protection of minority shareholders and creates a uniform, compulsory procedure that must be followed before implementing any of the three fundamental transactions.\(^{54}\) Before a company can give effect to the implementation of a scheme of arrangement a number of prerequisites must therefore be met.

For example, and as stated above, in terms of section 115(2)(a), approval of the transaction must be by special resolution at a meeting at which persons entitled to exercise a total of at least 25% of the voting rights are present. Section 115(2)(c), read with section 115(3)(a), caters for the event where the special resolution approving the proposed transaction is

\(^{50}\) Ibid.
\(^{51}\) Ibid 450.
\(^{52}\) Ibid 451.
\(^{53}\) Ibid 314.
\(^{54}\) s115 of the Companies Act 71 of 2008.
opposed by at least 15% of the voting rights that were exercised. Court approval will be required in such an event if one of the persons opposing the proposed transaction requires the company to seek such approval within five business days. In terms of section 115(5), the company must either within ten business days after the vote apply to court for the requested approval and bear the costs of that application, or alternatively treat the resolution as a nullity.

Further, a person who opposed the resolution may, regardless of what proportion of shareholders in total opposed the resolution, apply to the court for leave to apply to have the transaction set aside. Leave may only be granted if the court is satisfied that the applicant is acting in good faith, appears prepared and able to sustain the proceedings and has a *prima facie* case. If the resolution is not set aside in this way, the scheme of arrangement will be binding on all of the shareholders (of that class) of the company.\(^{55}\)

In terms of section 115(8), the holder of any voting rights in a company is entitled to exercise the appraisal rights granted to dissenting shareholders under section 164, if that person notified the company in advance of the intention to oppose the special resolution, and was present at the meeting and voted against that resolution. Provided that the dissenting shareholder has met the requirements and followed the steps as set out in the act, the shareholder may then demand that the company pay him a fair value for all the shares of the company which he holds.\(^{56}\) It has been questioned whether the appraisal remedy can be seen as an effective remedy for dissatisfied shareholders. Whilst it has the benefit of being an exit mechanism and a means of challenging the fairness of consideration offered for shares,\(^{57}\) it is hardly convincing as an appropriate remedy given that a shareholder who voted against a scheme in the first place because he does not wish to be bought out is provided a form of recourse that results in the surrender of those same shares for fair value.

In addition, the process is complicated, costly and time-consuming. Once a fair value has been demanded for the shares of the company, the shareholder has no further rights in respect of its shares other than to receive payment. These considerations may discourage shareholders against exercising their appraisal rights, especially small shareholders with limited funds. The court does have a discretion to award interest on the amount ultimately paid to the shareholder, but this may not necessarily always provide adequate compensation, particularly if the shareholder is ordered by the court to pay its own costs.\(^{58}\)

It can be said that the 2008 Act has taken significant steps to address the need to adequately protect shareholders, especially minority shareholders whose shares might be eliminated in terms of the scheme. 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. Notwithstanding the criticisms expressed above, the appraisal remedy will no doubt be a factor in inhibiting a company from seeking to impose an inequitable scheme of arrangement on its minority shareholders given the potential financial exposure the company will face in having to pay the minority shareholders the fair value of their shares. Thus, the mere existence of the appraisal rights as well as the potential involvement of the Takeover Regulation Panel will surely strengthen minority shareholder protections even further.59

4. COMPARISON WITH THE POSITION IN THE UNITED KINGDOM

4.1 HISTORY AND RELEVANT CASE LAW

Schemes of arrangement were first introduced in the Joint Stock Companies Arrangement Act 1870.60 The scheme of arrangement procedures that followed in sections 206 to 208 of the 1948 English Companies Act as well as sections 425 to 427A of the 1985 English Companies Act formed the basis of sections 311 to 312 and section 389 of the 1973 Act.61

Against this background, it follows that the court made reference to the English case of In Re NFU Development Trust Ltd62 in Ex parte Federale Nywerhede Bpk63 in interpreting section 311. In Re NFU Development Trust Ltd Brightman J quoted Bowen LJ in Re Alabama, New Orleans, Texas & Pacific Junction Railway Co64 where the latter observed that: “[N]o arrangement or compromise can be said to be reasonable in which you can get nothing and give up everything… The object of this section is not confiscation.” He continued by stating that “arrangement” implies some element of give and take and affirmed that confiscation was not his idea of an arrangement.

The terms of the scheme in In Re NFU Development Trust Ltd did not qualify as a compromise or arrangement between the company and its members within section 206 of the 1948 Act. It was held that the words “compromise” and “arrangement” implied some element of accommodation on each side and were not suitable to describe a total surrender of the rights of one side. The rights of members were being expropriated without any compensating advantage and, therefore, it could not be said that they were entering into either a compromise or arrangement with the company. Whilst the court in Ex parte Federale Nywerhede Bpk correctly adopted this view, our courts misinterpreted the judgement by

59 Luiz (n 6) 452.
60 Although their use at that point was limited to arrangements between companies and their creditors where the company was in the course of being wound up.
61 Blackman et al (n 2) 12.2.
62 See n 9 above.
63 See n 8 above.
64 Re Alabama, New Orleans, Texas & Pacific Junction Railway Co 1891 1 Ch 213 (CA) 243.
focusing on the nature of the consideration and not whether the consideration is as a result of enforceable rights and obligations as between the company and the shareholders. The position was later corrected in *Ex parte Suiderland Development Corporation* as described above.65

In *Re Savoy Hotel Ltd*66 it was stated that the word “arrangement” in section 206 of the 1948 Act was to be interpreted widely since the rights and obligations between the company and its members were sufficiently affected for the proposed scheme to be an “arrangement … between” them within section 206(1). However, since section 206(1) of the 1948 Act referred to an arrangement “proposed between” a company and its members, that assumed consent by the company, as a legal personality separate from its members, to the arrangement. Accordingly, the court had no jurisdiction under section 206 to sanction an arrangement regarding the members of a company which did not have the company’s approval, either through its board or by a majority of the members in general meeting.

Another area that has proved difficult to apply in UK practice is determining whether members should meet as a whole or as separate classes.67 A “class” has been defined as constituting “those persons whose rights are not so dissimilar as to make it impossible for them to consult together with a view to their common interest.”68 The definition is used as a general test, although there has been a shift of emphasis in applying it in recent years. In general, a broad view has been taken of the definition of “class”. In particular, the courts have focused on the different rights of shareholders and not just their different interests.69 This has the consequence that fewer class meetings are held and there is less chance of a veto by the minority at that stage. This approach is in accordance with the judgment in the *Verimark*70 case as discussed above and may be contrasted with the *obiter* remarks on the meaning of “class” in *Ex Parte Satbel*.71

4.2 CURRENT LEGISLATION, RULES AND OBSERVATIONS

Schemes of arrangement in the UK are regulated by Part 26 of the Companies Act 2006 (the UK Act) on “arrangements and reconstructions”, and more specifically sections 895 to 901. Section 895(2) reads as follows:

“In this Part— “arrangement” includes a reorganisation of the company’s share capital by the consolidation of shares of different classes or by the division of shares into shares of different classes, or by both of those methods...”

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65 See n 17 above.
66 *Re Savoy Hotel Ltd* 1981 3 All ER 646.
67 Payne “Minority shareholder protection in takeovers: A UK perspective” 2011 ECFR 156
68 Ibid and Sovereign Life Assurance Company v Dodd 1892 2 QB 573.
69 Payne (n 68).
70 See n 49 above.
71 See n 12 above.
Additionally, takeovers of UK incorporated and listed companies are regulated by the rules of the City Code. The City Code was formulated and is administered by the Panel on takeovers and mergers which is the supervisory authority appointed to perform certain regulatory functions pursuant to the Directive on Takeover Bids (2004/25/EC). The rules of the City Code have statutory force in the UK and the Panel has statutory powers in respect of all offers and other transactions to which the City Code applies.

The conduct to be observed in takeover and merger transactions and dual holding company transactions are set out in the City Code. The City Code comprises 38 rules and six general principles that speak to, among others, equivalent treatment, sufficient disclosure of information, fair procedures and maintaining market integrity.

In terms of section 899 of the UK Act, a scheme of arrangement must be approved both by the shareholders of the target company and by the court. A majority in number of each class of shareholders whose shares are the subject of a scheme (and who are voting at the meeting) constitutes shareholder approval. The majority must represent at least 75 percent in number of those shares which are voted. The arrangement is binding on the target company and on all the shareholders involved. The court’s role at this stage does not appear to be a rubber-stamping exercise but instead a real discretion to refuse to sanction the scheme. The court is not bound by the decision of the meeting and has an un fettered discretion as to whether to approve it or not. The scheme of arrangement procedure in the UK is evidently largely court driven. This is considered the main substantive difference between the 2008 Act and the UK Act, as they relate to schemes of arrangement.

It is noteworthy that one of the most common uses of a scheme is as an alternative to a takeover offer. If a scheme is to be used in this way then, typically, the shareholders of the target company agree to the cancellation of their shares in the target company. "The reserve created in the target company as a result of this arrangement is then used by the target to pay for new shares that are issued to the bidder. The shareholders of the target then receive, in exchange for their cancelled shares, cash or shares in the bidder. This is sometimes known as a “reduction scheme” as it combines a scheme with a reduction of capital." It can thus be concluded that the introduction of a reduction in section 114 as an addition to the reduction mechanisms available in section 48 of the 2008 Act has not only affirmed that a reduction may be effected by way of an arrangement but has further aligned our position with that under the UK Act.

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73 Ibid.
74 s 899 of the Companies Act 2006.
75 For a full understanding of UK law as it relates to a redemption or purchase by a company of its own securities, see Part 18 of the UK Act and Rule 37 of the City Code.
In recent years schemes of arrangement have become the preferred mechanism in the UK for effecting recommended bids. Minority protection available in a scheme is, however, substantially less than that available in a traditional takeover bid. The justifications for this may be found in the purpose of minority protection in relation to the differing mechanisms of a traditional takeover bid as compared to a scheme.

For example, in a traditional takeover bid it is necessary to present the bidder in order to ensure that the choice made by the shareholders is as undistorted as possible and further, to provide for the right to exit and to exit at the bid price. In contrast, a scheme involves a decision of the company, taken by the shareholders and consequently there is no opportunity for the bidder to “divide and conquer”. The concerns regarding distorted choice do not arise and there is no need to provide minority shareholders with a right of exit since all shareholders are bound by a successful scheme to transfer their shares to the bidder. As a result, the lower level of minority protection available in a scheme is not considered to be a cause for concern. Although the South African regime no longer requires court approval, there are several alternative protections, as discussed above, in place.

The influence of English company law on the 2008 Act as well as its predecessor in the context of schemes of arrangement is undeniable. The legislature has done well in absorbing many elements from the current as well as prior UK legislation whilst simultaneously also refining and tailoring these elements for the particular competing demands of market liquidity and shareholder protection that operate in a unique political environment in South Africa.

5. CONCLUSION

As observed above, the term arrangement in section 311 of the 1973 Act received significant judicial attention that resulted in a series of contrasting decisions. The continued use of the term in the 2008 Act arguably gives rise to a presumption that the legislature intended the language repeated in the Act to have the same meaning as in the repealed 1973 Act. Thus, given the restrictive interpretation of section 311 by the courts, it might well be contended that section 114 has a similarly restricted application. I concur with the view expressed in Henochsberg that with the term “arrangement” left undefined we are still compelled to seek guidance from existing judicial opinion where the 2008 Act has not dispelled doubt.

However, some legal scholars aver that the courts adopted a restrictive interpretation of the term arrangement to ensure minority shareholder protection and given the substantial protection which is now afforded to the minority by the material changes in the prerequisites

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76 Payne (n 68) 146.
77 Ibid 158.
78 Ibid 159.
79 Seligson (n 25) 8.
to the implementation of an arrangement between the company and the holders of its securities under the 2008 Act this particular consideration will no longer be applicable. Thus, the differences in sections 114 and 115 from their corresponding provisions in the 1973 Act are advanced. For example, the procedures for approval, the role of the courts and the mechanisms designed to protect the minority in support of this contention.  

It is respectfully submitted that this is far too broad a view. Whilst it is accepted that the 2008 Act has made strides in improving the mechanisms available as regards minority shareholder protection, it cannot reasonably be inferred that the term “arrangement” is rendered all-inclusive nor can this be concluded from the additions of “expropriation” or “re-acquisition by the company of its securities”. In fact, as demonstrated above, these inclusions alone present new challenges in defining the exact scope of an arrangement.

It is my recommendation that whilst the term arrangement itself may remain undefined, what does not fall within the ambit of the term should be carved out by the legislature so as to avoid retreating to a restrictive interpretation or the creation of a closed list of mechanisms. Additionally, where an arrangement may be effected in conjunction with other mechanisms it’s operation must be carefully and clearly set out within the Act. Alternatively, as the Panel on Takeovers and Mergers in the UK has formed the City Code, it may be useful that the Takeover Regulation Panel offer much needed guidance in a similar all-encompassing form.

However, more important than the form and/or approach adopted in addressing the residual uncertainty, is the timeliness in which it is done, for if anything can be concluded with absolute certainty, it is that the legal fraternity has dealt with the meaning of arrangement ad nauseam and an analysis of a multitude of section 114 cases is best avoided where possible. Even more petrifying is the possibility that the fog is never cleared by any means and the famous statement by Gower proves to hold true, that “arrangements…are of the widest character and…the only limitations are that the scheme cannot authorise something contrary to the general law or wholly ultra vires the company.”

80 Ibid 12.
81 Du Preez v Garber: In re Die Boerebank Bpk 1963 1 SA 806 (W) 813 per Trollip J (as he then was) quoting Gower Modern Company Law 2 554–555.
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**LEGISLATION**

Companies Act 61 of 1973

Companies Act 2006

Companies Act 71 of 2008

The Takeover Code
7. ANNEXURE A: AFFIDAVIT

AFFIDAVIT: MASTER'S AND DOCTORAL STUDENTS

TO WHOM IT MAY CONCERN

This serves to confirm that I, __EVANIA MOODLEY__________________________,

ID Number _8907050045085______________________________________________________

Student number _201708954_______________________________________ enrolled for the

Qualification _MAGISTER LEGUM IN COMMERCIAL LAW________________________________

Faculty _LAW________________________________________________________________

Herewith declare that my academic work is in line with the Plagiarism Policy of the University of

Johannesburg which I am familiar with.

I further declare that the work presented in the minor dissertation is authentic and original unless

clearly indicated otherwise and in such instances full reference to the source is acknowledged and I
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infringement in my work. I declare that no unethical research practices were used or material gained
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Signed at _______SANDTON_________ on this _______31st______ day of _______JANUARY________

2018.

Signature______________________________ Print name __EVANIA MOODLEY_____________________

STAMP COMMISSIONER OF OATHS

Affidavit certified by a Commissioner of Oaths
This affidavit conforms with the requirements of the JUSTICES OF THE PEACE AND COMMISSIONERS OF OATHS ACT 16 OF 1963 and the applicable Regulations published in the GG GNR 1258 of 21 July 1972; GN 903 of 10 July 1998; GN 109 of 2 February 2001 as amended.