The decision in Sekhoto is clearly a step in the right direction because of its qualification of the unacceptable view in Tsose. But it is submitted that, in the light of the almost unanimous support of the approach in Louw by the high courts, as well as the Constitutional Court’s apparent approval of the principle that an arrest should be regarded as a last resort, the legal reform in Sekhoto of arrest without a warrant did not go far enough. It is quite understandable why Sekhoto found that section 40(1)(b) of the Act is not unconstitutional, and because legislation overrides the common law, the court could not change the meaning of a statute by developing the common law. However this does not mean that the legislature should not step in and bring about the necessary reform.

The Bill of Rights (s 36 (1)) provides that fundamental rights, including of course the right to freedom of the person, may be limited by a law of general application, of which section 40(1)(b) of the Act is a clear example. But the extent of the limitation must be both reasonable and justifiable in an open and democratic society based on human dignity, equality and freedom. In judging the lawfulness of a limitation, all relevant factors must be taken into account, including the nature of the fundamental right, the importance of the purpose of the limitation, the nature and extent of the limitation, the relation between the limitation and its purpose, and, most importantly for the purposes of this discussion, whether there are less restrictive means of achieving the purpose of the limitation. Since the purpose of an arrest, which limits the arrestee’s right to personal freedom, is to bring him or her before a court to face due prosecution, section 40(1)(b) will probably not be a reasonable and justifiable limitation of this right if provision is not made for the implementation of available less restrictive means than arrest of achieving that purpose. It is submitted that consideration should be given by the legislature to amend section 40(1)(b) accordingly so as to bring it in line with the Bill of Rights.

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ABOUT OFFERS OF SECURITIES TO THE PUBLIC

About “public” contracts
I previously discussed some aspects of the regulation of the market for securities (see Delport “Offers and the Companies Act 71 of 2008” 2011 THRHR 280). The last pieces of this puzzle are the concept of “public” and the disclosure required by the Companies Act 71 of 2008 (“the Act” or “2008 Act”) in the primary as well as in the secondary markets and the all-important concept of the interrelationship between the markets in respect of regulation. The importance of the regulation cannot be overemphasized as is clearly illustrated by recent spectacular collapses in securities investment schemes where people lost millions.

The basic principles, some also discussed in 2011 THRHR 280 and which will not be repeated, are that if there is an offer, if the offer is in respect of securities, and the offer is made to the public, the offer in the primary market must be accompanied by a prospectus and in the secondary market it must be accompanied
by a written statement (ss 99 and 101 of the Act). The three determinants, namely, offer, securities and public therefore trigger the disclosure by prospectus or written statement (see also Yeats “Public offerings of company securities: A closer look at certain aspects of chapter 4 of the Companies Act 71 of 2008: Corporate formation and corporate finance: Part I” 2010 Acta Juridica 117).

An offer (as the first determinant) is defined in section 95(1)(g) as an offer to acquire securities in the company for a consideration, which inexplicably refers to the action by the addressee and not to the action by the company. (The interpretational difficulties with this definition, where the company is the offeree but the offeror must ensure that the offer is accompanied by a prospectus, were addressed in 2011 THRHR 280.) Capitalisation issues and the like are clearly excluded, but for the rest, any acquisition method, whether by means of an acquisition for cash (subscription) or barter (exchange for assets) is included, provided that there is “consideration” as defined in section 1. This definition also therefore confirms the dictum in Gold Fields Ltd v Harmony Gold Mining Co Ltd 2005 2 SA 506 (SCA) that, at least for the purpose of determining whether the offer should be accompanied by a prospectus, there is no distinction between subscription and barter. An offer must obviously be aimed at bringing a particular contract into existence, and in that respect the Act provides for two types of contracts.

The first type of contract is the primary offering (“PO”) as defined in section 95(1)(i) as

“an offer to the public made by or on behalf of a company of securities to be issued by that company or by another company within a group of companies of which the first company is a member or with which the first company proposes to be amalgamated or to merge.”

(The complexities and uncertainty in respect of this definition were discussed in 2011 THRHR 280.)

The second contract is the initial public offering (“IPO”) as defined in section 95(1)(e) as “an offer to the public of any securities of a company if no securities have previously been the subject of an offer to the public, or if there was such an offer, those securities have subsequently been re-acquired by the company”. A difference between the PO and the IPO which may possibly be significant in respect of determining regulation in the secondary market, is that in the case of the IPO it is an “offer of securities” and not an “offer . . . of securities to be issued” as in the case of the PO. Therefore an IPO can be in respect of any “acquisition, for consideration, of any securities” as defined in “offer” in section 95(1)(g), but the PO applies only in respect of (newly) issued securities. The exact ambit of the PO and the IPO is uncertain, but as a general rule of thumb (with obvious exceptions as are wont with any rule of thumb) one may opine that all IPOs will be POs, but not all POs will be IPOs.

About “securities”

The offer to conclude one of the contracts discussed above, must be in respect of securities, as the second determinant. “Securities” is defined in section 1 (after amendment by Act 3 of 2011) and “means any shares, debentures or other instruments, irrespective of their form or title, issued or authorised to be issued by a profit company”. This definition is exhaustive and not inclusive, with the result that anything that does not fall within this definition cannot be offered. The definition of securities other than shares creates interpretational problems in
this context. Section 43(2) provides that the board of the company may authorise the company to issue debt instruments. A debt instrument is defined in section 43(1) to include, inter alia, securities other than shares, but to exclude loans. It is uncertain what the intention with the exclusion of loans is, as debt instruments (presumably also debentures), are by nature loans to the company. Therefore a company can issue debentures (or debt), but they must not be loans. The causa for the debt other than a loan limits section 43 to the level of impossibility as far as company finance is concerned. The definition of debentures has always been problematic, and the new definition does not bring any certainty. To apply the distinction in New South Wales Corporate Affairs Commission v David Jones [1975] 2 NSWLR 710 714 that the word “debenture” should be interpreted as the written acknowledgement of debt rather than the underlying transaction, does not solve anything (see also English and Scottish Mercantile Investment Company v Brunton (1892) 2 QB 700, Coetzee v Rand Sporting Club 1918 WLD 74). Problems with the definition of debentures may have an effect beyond pure company law as may be illustrated by N2173 in Government Gazette 16167 of 1994-12-14 which defines “commercial paper”. In terms of the Banks Act 94 of 1990 (“Banks Act”), if a person does “the business of a bank” as defined in section 1 of that Act, it must register as a bank in terms of section 11. [“T]he business of a bank” is defined in section 1 to include, amongst others, the acceptance of deposits from the general public (including persons in the employ of the person so accepting deposits) as a regular feature of the business in question and also the soliciting of or advertising for deposits. [“D]eposit is also defined in section 1 to mean an amount of money paid by one person to another subject to an agreement that that money will be repaid conditionally or unconditionally, with or without a premium, on demand or on specified or unspecified dates and interest may or may not be payable. A payment by a person to a company which must, at some stage, be repaid by the company will therefore be a deposit. If the company, for example, solicits that deposit, whether through an offer accompanied by a prospectus or not, it is actually doing the business of a bank. If that debt by the company complies with the requirements of “commercial paper”, it will be excluded from the definition of “the business as a bank” by virtue of the notice in terms of subparagraph (cc) of the definition. Regulation 1(b) of the “commercial paper” notice defines commercial paper to also mean “debentures or any interest-bearing written acknowledgement of debt issued for a fixed term in accordance with the provisions of the Companies Act, 1973.” If a company issues a debt instrument under section 43, it must comply with the commercial paper requirement. Any loan by a company, although it may fall within the definition of “commercial paper”, would not be possible as it is expressly excluded by section 43(1)(a) of the Act. Add to this the different concepts of “public” in the Banks Act and the Companies Act and the uncertainty increases exponentially.

Also, securities are by necessary implication in respect of an “issuer”, which is now defined in an attempt to cover the lacunae in the 1973 Act in respect of offers into South Africa by foreign companies. Section 99(1) provides that a person must not offer to the public any securities of any person unless that second person (a) is a company; and (b) in the case of a foreign company, certain documents such as the equivalent of its Memorandum of Incorporation and information about its directors (not officers) have been filed within 90 business days before the offer to the public is made.
AANTEKENINGE

The conjunctive “and” implies that a foreign company is a category in the genus of “company”, otherwise the disjunctive “or” would be used. However, the definition of “company” does not include a foreign company. A “foreign company” is defined in section 1 as an entity incorporated outside the Republic irrespective whether it is profit or non-profit or whether it carries on such business within the Republic. If it does carry on such business inside South Africa, it becomes an external company and section 23 applies. Ironically section 23 has a presumption in respect of “conducting business”, but not “carrying on [of] business”. Distilled to the basics the effect is that all external companies are foreign companies, but not all foreign companies are, due to section 23, external companies. For example, a company incorporated in Delaware will therefore have to comply with the Act if it offers securities in South Africa, irrespective of whether it is an external company or not. This in itself causes certain difficulties, because if the company does not comply with the Act it commits an offence and is liable for losses sustained by a person as a result of the contravention (offence) (s 214(4)). This appears to be in order, but the extraterritorial criminal enforcement will be difficult and the enforcement of a damages claim well-nigh impossible. The biggest problem, however, is that if the offer is of “securities” other than those defined in section 1 of the Act, of which there are many obvious examples under foreign laws, the Act is not applicable as the second determinant is absent.

About “public”

The third determinant, being the concept of “public” may be the most problematic due to the inherent uncertainty as to its exact meaning in the context of company law (Davies Gower and Davies’ Principles of modern company law (2008) 873). A rudimentary determination of the meaning of “public” may be necessary as it may be possible under the Act, in contrast to the 1973 Act, that there may be common law exclusions as to when addressees are “not public”. In an attempt to determine the exact (as far as it may possible) meaning of “public” it may be necessary to examine the historic development of the concept, and to refer to some foreign jurisdictions. The choice of the starting point of the development and the jurisdiction in respect of which it will be done is made on the basis of the significance for this discussion and will, as a result, be eclectic rather than representative and exhaustive.

The concept was first used in section 30 the British Companies Act of 1900 which merely stated that a prospectus means an offer to the public of shares and debentures (see Delport Die verkryging van kapitaal in die Suid-Afrikaanse maatskappyeereg met spesifieke verwysing na die aanbod van aandele aan die publiek (LLD thesis UP 1987) 428ff for the history and development). The significance of this is that the prospectus was not the document that accompanied the offer but that it was the offer. There was no definition of “public” and the next problem was whether an offer to a selection or section of the public fell within the definition. In Nash v Lynde [1929] AC 158 the House of Lords was required to determine whether an offer marked “strictly private and confidential” fell within the definition of “prospectus” in section 81 of the Companies (Consolidation) Act 1908 (which was the exact equivalent of section 30 of the Companies Act of 1900). Viscount Sumner (at 169) held:

“No particular numbers are prescribed. Anything from two to infinity may serve: perhaps even one . . . The point is that the offer is such as to be open to anyone who
brings his money and applies in due form, whether the prospectus was addressed to him . . . or not” (169).

The effect of this judgment was that (arbitrary) selections were made and that the offers were only addressed to the constituent members who could not renounce the offer in favour of outsiders. This was then a “non-public” offer. This practice was soon stopped and the amendments to the British Companies Act of 1929 on the recommendations of the Cohen Commission (1945 Cmd 6659) (which found their way in some form or another into the British Companies Act 1948 and beyond) was that the concept “public” would include any selection, “whether as clients of stockbrokers or otherwise”. This provision was also incorporated in section 84bis of the South African Companies Act 46 of 1926 (“1926 Act”) and eventually in section 142(1) of the 1973 Act. On the ambit of these sections Gower Principles of modern company law (1954) 351 said: “Indeed, the definition is so wide that, unless some limitations were imposed, it would be impossible to issue shares or debentures without making a public issue.”

Certain exceptions were incorporated in section 84bis(4) of the 1926 Act, which were also initially incorporated in section 144 of the 1973 Act with the aim to solve the over breadth. With the exception of the original section 144(a), “not being calculated to result, directly or indirectly, in the shares becoming available to persons other than those to whom the offer was made” (the Nash v Lynde exclusion) most of the provisions (including some reserved for the secondary market) found their way into section 96 of the 2008 Act. The possibility of a “generic” non-public category, which can be determined on the basis of the particular offer, disappeared together with the relevant case law, with the deletion of section 144(a) by section 8 of the Companies Amendment Act 35 of 1998.

The exclusions are obviously based on basic principles as to why the offers are not to the public (that is, non-public or private offers). These principles are important not only to determine whether the exclusions presently contained in section 96 of the Act are principally sound, but also to determine what the requirements would be for any “common law” non-public categories. As to the development of the principles there is, up to a stage, a confluence in the development of the British and US systems (Loss Fundamentals of securities regulation (1988) 321), and the discussion will therefore refer to both these systems. The concept “public” was not defined initially and the question was when an offer was a non-public (or a private) offer. As was seen, the British legislature extended the concept of “public”. In the US, section 4(2) of the Securities Act 1933, on the other hand, merely stated the opposite, in that “transactions by an issuer not involving any public offering” are excluded from the prospectus requirements. The judicial interpretation of public offerings started with SEC v Ralston Purina Co 346 US 119 (1953) where the court said:

“Decisions under comparable exemptions under the English securities Acts and state “blue sky” laws, the statutory antecedents of federal securities regulation, have made one thing clear – to be public an offer need not be open to the whole world.”

In SEC v Sunbeam Gold Mines Co 95 F 2d 699 (CA 9th Cir 1938) 701 the concept was further defined as follows:

“In its broadest meaning the term ‘public’ distinguishes the populace at large from groups of individual members of the public segregated because of some common
interest or characteristic. Yet, such a distinction is inadequate for practical purposes; manifestly, an offering of securities . . . to all existing stockholders of the General Motors Corporation . . . is no less 'public', in every realistic sense of the word, than an unrestricted offering to the world at large . . . for the means used to select the particular individuals to whom the offering is to be made bear no sensible relation to the purposes for which the selection is made . . . To determine the distinction between 'public' and 'private' in any particular context, it is essential to examine the circumstances under which the distinction is sought to be established and to consider the purposes sought to be achieved by such distinction . . . the applicability [of the protection of the disclosure of information] should turn on whether the particular class of persons affected needs the protection of the [Securities] Act. An offering to those who are shown to be able to fend for themselves is a transaction 'not involving any public offering' . . . [B]ut the statute would seem to apply to a 'public offering' whether to few or many. It may well be that offerings to a substantial number of persons would rarely be exempt . . . But there is no warrant for superimposing a quantity limit of private offerings as a matter of statutory interpretation.”

In *Doran v Petroleum Management Corporation* 545 F 2d 893 (5th Cir 1977) 903 the picture became clearer and the test was laid down that the offeree must be able to acquire the information as would have otherwise been provided by the prospectus because of “a relationship based on factors such as employment, family, or economic bargaining power that enables the offeree effectively to obtain such information”.

The above *dicta* in respect of the common law non-public offers have, to a large extent, been incorporated in statutory provisions. In the US, the essence of the common law “transactions by an issuer not involving any public offering” was enacted in 1982, substituting previous provisions, as Rule 506 of Regulation D under the Securities Act 1933 (Loss 324). Based on Rule 506, it may be possible to establish objective criteria to determine the non-public (or private) category of offerees (or where the offerees are able to “fend for themselves”). These are basically the offeree profile and the availability of information (Loss 334). In respect of the offeree profile the requirements are either sophistication or wealth or the relationship with the offeror. Sophistication will entail that the addressee will be able to understand the complexities of the investment and the risk involved. Wealth requires that the person is able to assume the risk of the investment, while the relationship is such that there is no practical need for disclosure (because the offeree is a senior employee or business associate with knowledge of the offeror and the risks involved). The criteria above to determine the “rich and smart” class of non-public offerees should also be instructive to determine the common law “non-public” category, as it is based on common law principles.

In respect of the availability of information, the requirement will be that the offeree must have access to the information to enable her to make a decision about the investment. This can be that as a result of an existing relationship (as distinct from that in the offeree profile above) the offeree already has the information or, because of the financial bargaining power of the offeree (like offers to a bank in respect of loan capitalisation), he can readily obtain the information (Loss 339). The “existing relationship” requirement can also be illustrated with reference to *Corporate Affairs Commission v Australian Central Credit Union*, *Corporate Affairs Commission (South Australia) v Australian Central Credit Union* (1985) 157 CLR 201 (HC) where the offer for shares was made by the
Australian Central Credit Union to its own members to effect a demutualisation of the entity. There was a clear, existing relationship between the offeror and the offerees which was of such a nature that they had the information which would have been provided by the prospectus or they could readily obtain it. It was stated thus:

“The question whether a particular group of persons constitutes a section of the public for the purposes of sec. 5(4) of the Code cannot be answered in the abstract. . . If, however, there is some subsisting special relationship between offeror and members of a group or some rational connection between the common characteristic of members of a group and the offer made to them, the question whether the group constitutes a section of the public for the purposes of the offer will fall to be determined by reference to a variety of factors of which the most important will ordinarily be: the number of persons comprising the group, the subsisting relationship between the offeror and the members of the group, the nature and content of the offer, the significance of any particular characteristic which identifies the members of the group and any connection between that characteristic and the offer” (795).

An important, and obvious, qualification in Rule 506 is that there must be no “redistribution” by the offerees for at least a year. It is also important to note that the test is qualitative (characteristics of the offer or offerees) rather than quantitative (number of offerees) (Loss 321).

In Britain (the eventual) sections 85 and 86 of the Financial Services and Markets Act 2000 (c 8) as amended by the Prospectus regulations 2005 (SI 1433 of 2005 as amended by SI 1668 of 2011)) provide that a prospectus must be made available to the public (undefined) before an offer of transferable securities is made to the public (s 85(1)) unless the offer is exempt under section 86. Section 86 follows, to a large extent, the philosophy as set out above, in providing exemptions.

The South African legislation followed, for obvious historical reasons, the British legislative precedent even more closely than did the United States. Section 84bis of the 1926 Act was substituted by section 142 of the 1973 Act and provided as follows:

“[‘O’]ffer to the public’ and any reference to offering shares to the public mean any offer to the public and include an offer of shares to any section of the public, whether selected as members or debenture-holders of the company concerned or as clients of the person issuing the prospectus concerned or in any other manner.”

It may be important that the word “public”, which was omitted in the definition is section 84bis was expressly included in the definition in section 142 as this may affect the ambit of “public” and also the possibility of a common law non-public category (Delport “Offer to the ‘public’: Even more disharmony” 2005 S4 Merc LJ 388). Be that as it may, the position seems to have reversed itself into the 1926 Act with section 95(1)(h) of the Act which provides that an “offer to the public”:

“(i) includes an offer of securities to be issued by a company to any section of the public, whether selected—
(aa) as holders of that company’s securities;
(bb) as clients of the person issuing the prospectus;
(cc) as the holders of any particular class of property; or
(dd) in any other manner; but
(ii) does not include—
(aa) an offer made in any of the circumstances contemplated in section 96; or
(bb) a secondary offer effected through an exchange;”
There is also a somewhat lost reference in section 95(2) which states that for the purposes of chapter 4 of the Act, a person is to be regarded, by or in respect of a company, as being a member of the public, despite that person being a shareholder of the company or a purchaser of goods from the company. This is clearly an unnecessary complicating relic of section 141 of the 1973 Act and its predecessors where reference to a “member” of the public was inserted to extend the prohibition on the “hawking” of shares (see Lansdown Commission UG 45 of 1936 16, Millin Commission UG 69 of 1948 107 and S v Rossouw 1968 4 SA 380 (T), 1971 3 SA 222 (T)). The continued extension of the meaning of “offer to the public” by the addition of subcategories of “section of the public” is unnecessary, as a single subcategory such as that in section 95(1)(h)(i)(dd) would include all those above it (and would make the definition easier to understand). The Act therefore defines “offer to the public” and “member of the public” but does not define “public”. The Act therefore uses “offer to the public” and “member of the public” but does not define “public”. The Act defines certain offers to a section of the public, such as that listed in section 96, but the language of section 95(1)(h) does not indicate that this exclusion is exhaustive, but rather that it is a “safe harbour” (see Loss 324 for the “safe harbour” concept).

Common law “non-public”?
In Gold Fields Ltd v Harmony Gold Mining Co Ltd supra 510F the court found that the ordinary meaning of “public” in terms of an offer would mean that it is capable of acceptance “by the public at large”. It basically followed the Nash v Lynde (supra) principle in that it is not necessary for the offer to be made to the “the public at large” but also if it is made with “indifference to any random section of the public”. If the offer is aimed at acquiring specific private property, it is only capable of acceptance by the owner of the property (the offer is addressed to the owner in this “peculiar capacity”), and has the effect that the offer is not extended to the public at large or to a random section of the public. There is now a “rational connection” between the offer and the characteristics that sets the group apart from the “public” and based on that principle the court found that it was not an offer to the public under section 145 of the 1973 Act. While aspects of Gold Fields are susceptible to (possibly justified) criticism (see eg Cassim “Gold Fields v Harmony: A lost opportunity to clarify section 145 of the Companies Act” 2005 SALJ 269; Delport 2005 SA Merc LJ 3008), it (re)opened the door, together with the new definition in section 95(1)(h), for the common law non-public category. The principles as discussed above, especially in respect of Rule 506 under the United States Securities Act 1933 should, it is submitted, be used as a basis for the determination of this category of “non-public”.

About the secondary market
It should be borne in mind that the above principles (offer, securities and public) now also apply in respect of secondary offers (the previous s 141), which can lead to interesting permutations and (perhaps) unintended consequences. (S 141 was in a separate chapter in the 1973 Companies Act to avoid confusion with the primary market regulation (see Van Wyk de Vries Commission Supplementary Report RP 31 of 1972 102.) A secondary offer is defined in section 95(1)(m) as “an offer for sale to the public of any securities of a company or its subsidiary, made by or on behalf of a person other than that company or its subsidiary”. Section 101 basically requires a written statement to be filed in the case of a
public company (securities of private companies can be sold in the secondary market, but it cannot be issued to the public (s 8(2)). The whole of section 101 is not applicable if the offer is in respect of listed shares (s 101(1)), although the written statement for some reason must name the exchange if the shares are listed (s 101(6)). The requirements as to the accompanying documentation (s 101(4)–(6)) do not apply if the securities are offered by public tender or by certain “functionaries”, such as executors, administrators or trustees of various estates (s 101(3)). The significance of this differentiation in respect of application is not clear. The written statement (or the original prospectus which accompanied the PO or IPO) must accompany the secondary offer. If a prospectus was issued on the first distribution of the shares, that prospectus must accompany the secondary offer. In general terms a prospectus ceases to have effect after the conclusion of the primary offer, or otherwise four months after registration (filing) no offers may be accepted on it for the issue of shares (s 107). However, it is not clear when a prospectus will become stale in respect of a secondary offer. In any case will it be preferable for the seller to issue the written statement instead, as the differences in civil liability and also the possible defendant in case of such liability, will favour her. In addition the amount of information required for a written statement is much less and less detailed than that for a prospectus (see s 101(6)(d) for requirements for the written statement and regulations 54 and 55 of the Companies Act regulations (R351 in Government Gazette 34239 of 2011-04-26) for the prospectus requirements). If a prospectus was not required in the primary issue, it may be that a written statement is nonetheless required in the on-selling of the securities. This is the situation due to the fact that although the same principles (ss 95(1)(h) and 96) are used to determine who the “public” is, the secondary offer could be in respect of a different category and therefore public.

The above principles are logical and correct in respect of the “bona fide” primary and secondary markets where all the transactions and dealings are at arm’s length. However, regulatory arbitrage may be possible and thereby the protection of the prospectus is not available to investors if the secondary market is used as an extension of the primary market. This can happen where the primary market transaction is structured to ensure that it is not an offer to the public by using one of the safe harbour provisions in section 96. The subscriber for the securities can then offer the securities for sale immediately and this “redistribution” in the language of Rule 506 discussed above (and regulated in the 1973 Act in s 146), will only be subject, at best, to the limited disclosure in the written statement in terms of section 101. The possible prejudice of investors is clear because the principle that “people who are forced to undress in public will presumable pay some attention to their figures” (Loss 33) will not apply, at least not in full.

PIET DELPORT

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