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SHAREHOLDER PROTECTION RULES UNDER FUNDAMENTAL TRANSACTIONS

By

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ABSTRACT

Empirical research in previous years has shown the history and evolution of takeovers and mergers in South Africa. Many theories have emerged to show the advancement in the Companies Act 71 of 2008 (2008 Act) from the Companies Act 61 of 1973, especially in issues relating to takeovers and reorganisations. This includes measures in the 2008 Act that are designed to protect shareholders involved in fundamental transactions.

Several academic writers have provided insight into the changes brought about by the 2008 Act with regard to the protection of shareholders, especially in fundamental transactions. It is noted that shareholder protection rules and fundamental transaction rules are the result of some of the purposes of the 2008 Act. Both these rules are a result of the purpose to encourage investment in the economy of the country and to promote the development of South African markets, respectively.

However, this research, through critical and comparative analysis of shareholder protection rules in South Africa, the United States of America, India and the United Kingdom, sets out to highlight the conflict between shareholder protection rules and fundamental transactions rules in the 2008 Act. It also shows that with the realisation of one rule comes the transgression of the other and raises the question of whether the 2008 Act has actually struck the right balance.

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CHAPTER 1

General Introduction

1.1 Background

1.1.1 The need to reform

There is a need to reform company law in South Africa from time to time owing to the changing environment within which companies operate.[1] Company law review is a process that should be continuous to ensure that the laws that regulate businesses are a reflection of societal needs and cater for market practices.[2] The first time that South African company law underwent a comprehensive review was in 1963 through the Van Wyk De Vries Commission.[3] This commission was tasked with reviewing the Companies Act 46 of 1926, which was mostly based on English company law. The comprehensive review by this commission led to a report that gave us the Companies Act 61 of 1973 ("**the 1973 Act**").[4]

1.1.2 The 1973 Act

The 1973 Act also had not been subjected to a comprehensive review for a long period. It was thus not reflective of the developments that had taken place in South Africa and internationally. This conclusion is drawn from the fact that international corporate structures had undergone significant developments and many ways of doing business had been abandoned or modified and incorporated into new concepts.[5]

[1] The Department of Trade and Industry "The South African Company Law for the 21st Century: A Guideline for Corporate Law Reform" at 13. Hereafter the DTI policy guideline.
[2] *Ibid.*
[3] Van Der Linde "*Aspects of the Regulation of Share Capital and Distribution to Shareholders*" (LLD thesis, University of South Africa, 2008) at 260.
[4] Hereafter the 1973 Act.
[5] DTI n1 at 13.

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Furthermore, the number of corporate failures, owing to serious defects in the administration of company law, resulted in investors suffering extensive losses.[6]

The 1973 Act was clearly not aligned with modern business practices and was found to be deficient in a critical area such as shareholder protection. What causes this area to be critical is that it is vital in attracting international capital. This called for more investor-friendly and competitive domestic laws, in line with international trends. Furthermore, the rise in foreign investment near the end of the period of validity of the 1973 Act created a need for provisions that cater for the operation of foreign companies in South Africa.[7]

1.1.3 The Constitution

The Constitution of the Republic of South Africa, 1996 ("**the Constitution**") is important in respect of the fact that no South African law can be inconsistent with the Constitution, as it is the supreme law of the country.[8] Given that it regulates the economic relationships between citizens, it has fundamental implications for company law.[9] This means that reformed company law needs to be consistent with the Constitution and of course with other laws that have been enacted, such as the Competition Act 89 of 1998 and the Broad-Based Black Economic Empowerment Act 46 of 2013.[10] In this study the environment in which business is conducted in the South African jurisdiction was also considered, taking into account other laws that regulate specific features within the corporate sector. These were labour legislation laws, in particular the Labour relations Act,[11] the Skills Development Act[12] and the Employment Equity Act.[13]

1.1.4 The Companies Act of 2008[14]

[6] *Ibid*.
[7] *Ibid*.
[8] S2 of the Constitution.
[9] See S8 (4) of the Constitution, which states that a juristic person is entitled to the rights that are in the Bill of Rights and to the extent required by the nature of those rights and the nature of that juristic person. Also S8 (2) of the Constitution, which states that the Bill of Rights binds any juristic person and if applicable to any extent of the nature of the right and the nature of the duty imposed by that right.
[10] DTI n1 at 14.
[11] The Labour Relations Act of 1995.
[12] The Skills Development Act 97 of 1998.
[13] The Employment Equity Act 55 of 1998.
[14] Hereafter the 2008 Act.

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The 1973 Act was finally abolished by the Companies Act 71 of 2008 ("**the 2008 Act**") in an attempt to align South African company law with international best practices.[15] In pursuit of such best practices, the Department of Trade and Industry ("**DTI**") came up with a corporate law reform process and all the recommendations emanating from that process were documented in "The South African Company Law for the 21st Century: A guideline for Corporate Law Reform".[16] This policy led to a reformed merger[17] and takeover regime and determined what were to be the purposes of the Act.[18]

1.2 Introduction

The DTI policy guideline, in considering the vision of the economy and the challenges that South Africa is facing, conceived that the purpose of company law should be to promote: (i) the development of the South African economy and (ii) the economy's competitiveness by promoting investment and innovation in South African markets by making sure that there is harmonisation and compatibility with the best practice jurisdictions internationally, among others.[19] Therefore, two of the purposes of the 2008 Act form the subject of this study.

1.2.1 Promoting the development of the South African economy

One of the purposes of the 2008 Act is promoting the development of the South African economy.[20] This makes mergers and takeovers important, as takeover offers are increasingly seen as beneficial to the economy and to wealth creation.[21] Activity in cross-border mergers and acquisitions is a way in which multinational companies are able to engage in direct foreign investment.[22] Therefore, mergers and acquisitions are

[15] DTI n1 at 3-4.
[16] Hereafter the DTI policy guideline.
[17] S 1 of the 2008 Act describes a "merger" or "amalgamation" as "a transaction, or series of transactions, pursuant to an agreement between two or more companies, resulting in "the formation of one or more new companies, which together hold all the assets and liabilities that were held by any of the amalgamating or merging companies immediately before the implementation of the agreement, and the dissolution of each of the amalgamating or merging companies, or the survival of at least one of the amalgamating or merging companies, with or without the formation of one or more new companies, and the vesting in the surviving company or companies, together with such new companies, of all of the assets and liabilities that were held by any of the amalgamating or merging companies."
[18] DTI n1 at 5.
[19] DTI n1 at 9.
[20] S7 of the 2008 Act.
[21] Austin and Ramsay *Ford's Principles of Corporations Law* 13ed (2007) in para 23.080.
[22] Cassim "The Introduction of the Statutory Merger in South African Corporate Law: Majority Rule Offset by the Appraisal Right (Part 2)" (2008) *South African Mercantile Law Journal* at 174.

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a general global trend and have an impact on the global economy; this highlights their importance as an element of any healthy economy. This has led to the inclusion of rules that make it possible to restructure business to adapt to changing business conditions in the 2008 Act.[23]

1.2.2 Promoting investment in the South African markets

Another purpose of the 2008 Act was to promote investment in the South African markets[24] and this makes it important that company law caters for the protection of investors in companies. These investors can be broadly described as equity investors and creditors. Even though creditors are at risk, equity investors who are shareholders are the ones that are at greater risk.[25] They invest their capital in companies with the intention of getting back a return on that capital. This makes it important for effective remedies to be in place for these shareholders to be protected. Hence, the primary purpose of company law is to ensure that shareholders as equity investors are provided rights and whenever these rights are transgressed, they can have effective recourse.[26] This led to the inclusion of shareholder protection rules in the Act in respect of takeovers and mergers.[27]

1.3 Problem statement and research questions

The rules that bolster the two values of promoting the development of the South African economy and promoting investment in the South African markets are in conflict with one another and as a result of this conflict they can frustrate the realisation of what they are intended for.

Take for example a company wanting to enter into a business restructuring proposal such as a merger or takeover offer, which promotes the development of the South African economy, since it is seen as beneficial to the economy. However, one of the shareholders exercises a shareholder protection measure such as the appraisal

[23] Mergers and amalgamations in terms of s113 of the Act, scheme of arrangement in terms of s114 of the Act and disposal of all or a greater part of company's assets in terms of s112 of the Act.
[24] S7 of the Act.
[25] A further discussion with respect to creditors falls outside the scope of this study.
[26] DTI n1 at 35-37.
[27] The appraisal remedy in terms of s 163 of the 2008 Act, the mandatory offer in terms of s 123 of the Act, shareholders' approval in terms of s 115 of the 2008 Act, court approval in terms of s 115 of the 2008 Act and compulsory offers in terms of s 124 of the 2008 Act.

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right[28], which promotes investment in South African markets since it attracts investment by ensuring protection of investors' interests. The shareholder in exercising this right asks for a fair market value for his shares in the company, as he does not want to be part of the proposed merger or takeover offer.[29] Considering the fact that a company is obliged to buy the dissenting shareholder's shares in the appraisal remedy, this may result in a drastic cash drain from the company.[30] This cash drain, in satisfying the dissenting shareholder's demands, may result in the abandonment of a takeover[31] or fundamental transaction.[32] In other words, the shareholder protection measure concerned, which advances the value of promoting investment in South African markets, frustrates the realisation of the business restructuring proposal fostering the development of the South African economy.[33] This raises the question of whether the 2008 Act struck the right balance between facilitating business restructuring through fundamental transactions and shareholder protection.

1.4 Purpose of the research and methodology

South African company law has absorbed business restructuring measures and shareholder protection rules from several jurisdictions, because these promote the development of the South African economy and investment in South African markets, respectively. These values are promoted by rules absorbed from different jurisdictions, which are influenced by different experiences.[34] It is believed that they are in conflict with one another and frustrate the realisation of what these values stand for; this contradiction has not been addressed. This theory will act as a guiding principle for

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[28] Wertheimer "The Shareholders Appraisal Remedy and how Courts Determine Fair Value" (1998) *Duke Law Journal* at 613-614 provides that under the appraisal remedy —

> "minority shareholders are granted limited statutory rights as a check against rampant majority rule. One such right is the ability of shareholders to dissent from certain corporate actions, primarily mergers and other fundamental corporate changes, and to receive the appraised fair value of their shares."

[29] Cassim *et al Contemporary Company Law* (2012) at 807-810. Delport *et al Henochsberg on the Companies Act 71 of 2008* (2018) at 577-578. Paine "Achieving the Proper Remedy for a Dissenting Shareholder in Today's Economy: Yuspeh v Koch" *Louisiana Law Review* at 918.

[30] Manning "The Shareholder's Approval Remedy: An Essay for Frank Coker" (1962) *Yale Law Review* at 236.

[31] *Ibid*.

[32] Fundamental transactions are the disposal of all or a greater part of the assets of the company or undertaking in terms of s 112 of the 2008 Act, mergers and amalgamations in terms of s 113 of the 2008 Act and schemes of arrangement in terms of s 114 of the 2008 Act.

[33] The argument here is discussed in more detail in CHAPTER 3.

[34] This is discussed in detail in
CHAPTER **2**.

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this research or a philosophical point of view, which will perhaps lead to providing solutions to the identified problems.

Hence, the objective of this research is to reveal the conflict between the two rules, namely the shareholder protection provisions on the one hand and business restructuring provisions on the other hand. These provisions promote the two purposes of the 2008 Act as indicated above, which are the promotion of the development of the South African economy and promotion of investment in South African markets.[35] In pursuit of this objective, provisions in the 2008 Act that provide protection to shareholders in the context of takeovers will be analysed.

The research will also shed light on how the conflict between the two rules indicated above tends to frustrate the realisation of what these very rules are intended for. This is due to the fact that with the realisation of one of the rules comes the transgression of what the other rule stands for. However, after these findings, the researcher will make recommendations on how corporate law in respect of takeover provisions could be improved from its current stance to realise the objectives of these rules fully. Furthermore, the research will analyse whether the 2008 Act, in respect of its takeover rules, is aligned with international trends, since one of the purposes of the DTI policy guideline was to ensure compatibility and harmonisation with the best practice jurisdictions internationally.[36]

As mentioned above, the corporate law reform process that was undertaken led to the enactment of the 2008 Act,[37] which included takeover provisions as a topical issue that received a massive amount of response from professionals and academic legal scholars alike.[38] There was a great amount of literature that attempted to address a number of issues in the 2008 Act.[39] Included in these publications was literature that

[35] This is discussed in detail in the introduction to this chapter.
[36] DTI n1 at 3-4.
[37] See discussion on 2008 Act under the background heading.
[38] Mongalo "An Overview of Company Law Reform in South Africa: From the Guidelines to the Companies Act 2008" (2010) *Acta Juridica* at xiii-xviii provides a broad overview of the company law reform process and indicates that on takeovers, priority arears that were identified for reform was the role of the Securities Regulation Panel and the reconsideration of fundamental and affected transactions. Boardman "A Critical Analysis of the New South African Takeover Laws as Proposed under the Companies Act 71 of 2008" (2010) *Acta Juridica* at 306 provides an analysis of provisions in the Act in so far as they relate to takeovers and takeover offers. The publication also compares these provisions with the first pre-existing South African company law and with the provisions of company law in the UK, Australia and the USA.
[39] Davids *et al* "A Microscopic Analysis of the New Merger and Amalgamation Provision in the Companies Act 71 of 2008" (2010) *Acta Juridica* at 356-357 query whether it is necessary in all

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addressed the takeover law regime.[40] The proposed research intends to contribute to the existing body of knowledge, particularly in respect of the takeover law regime in South Africa, but from a conflict of rules perspective, as hypothesised above.

In association with the existing literature in respect of the takeover laws in the 2008 Act, there is consensus that it is important to regulate the South African takeover market with a set of well-designed takeover rules.[41] Based on the understanding that a number of jurisdictions internationally have adopted different methods to regulate takeovers, South Africa also needs to adopt a takeover legal system with South African characteristics that cater for its market practices. The proposed research intends to do that by gathering knowledge of the different ideas from the experience of different jurisdictions and prepare these for future legal reform, with the aim of developing mercantile law.

The study will rely on primary sources such as case law and legislation, as well as secondary sources, namely textbooks and published articles. The comparative analysis method will be used in investigating the issues raised, on the grounds that acquiring knowledge of different foreign legal systems by comparison provides deeper understanding of certain components of the subject matter being studied and provides

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circumstances to have shareholders' approval in all mergers as the Act suggests under S115 of the 2008 Act, in light of the fact that in a number of jurisdictions the approval of shareholders by the acquiring company is not required when the acquiring company is significantly larger than the target company. This is because such transactions constitute a small purchase for pocket change in respect of tax reasons and are highly unlikely to make a significant change or have an impact of the acquiring company's shareholders. The authors further query the need for approval of shareholders from each of the merging companies in the context of internal group reorganisations, whether these be mergers between holding companies or their subsidiaries or between two subsidiaries, where there are no minority shareholders and no creditors who are prejudiced and where a simple board approval may justify the merger. In view of the fact that under S112 of the 2008 Act, which deals with the disposal of all or a greater part of the company's asset or its undertakings, the requirement of having shareholders' approval will not apply in the context of disposals between a wholly owned group company and its parent company and/or sister companies, the author sees no reason why the same method cannot apply in the context of a merger. This forms part of the subject of study and it is discussed in detail under CHAPTER 3.

[40] Latsky "The Fundamental Transactions under the Companies Act: A Report back from Practice after a Few Years" (2014) *Stellenbosch Law Review* at 377 provides that S115 (4) of the 2008 Act makes it difficult to comply with it, since it states that voting rights that are controlled by an acquiring company *must* not be included in the quorum of meetings that voted in support of the resolution of an intra-group merger where a wholly owned subsidiary is absorbed into its holding company and the holding company survives the merger. This is in light of the fact that an acquiring party under S1 of the 2008 Act is defined as a person who will directly or indirectly as a result of the transaction acquire direct or indirect control of a greater part of the company or all the assets of a company or its undertaking. This forms the subject of study and is discussed further under CHAPTER 3.

[41] This is discussed in detail in

CHAPTER **5**.

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better knowledge of the different rules being compared.[42] Furthermore, as highlighted in the introduction to this chapter, comparison with foreign jurisdictions is important because, when the 1973 Act was abolished by the 2008 Act, this was an attempt to align South African company law with international best practices[43].

The comparison in this study includes the United States of America (USA), the United Kingdom (UK) and India. This is because provisions in the 2008 Act that regulate takeovers in South Africa are an absorption of elements of laws of various jurisdictions, which include the USA and to a lesser extent the UK.[44] Another reason is that India is part of an emerging national economies association called BRICS, along with South Africa.[45] In respect of the USA, the comparison is based on the Model Business Corporation Act[46], as it is used in most of the states in America, and the Delaware General Corporation Law ("**DGCL**")[47], as it is the leading law in most of the states in America. The Securities Act,[48] Securities Exchange Act[49] and the Williams Act[50] are federal law and deemed superior to state authority.[51] In respect of the UK the comparison is based on the City Code[52] and the Companies Act.[53] In respect of India the comparison will be based on the Companies Act,[54] the Competition Act,[55] the Foreign Exchange Management Act[56] and the Securities and Exchange Board of India (Substantial Acquisitions Shares and Takeovers) Regulations.[57]

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[42] Sacco "Legal Formants: A Dynamic Approach to Comparative Law (Installment I of II)" (1991) *American Journal of Comparative Law* at 4-6.
[43] See discussion on 2008 Act under the background heading.
[44] Boardman "A Critical Analysis of the New South African Takeover Laws as Proposed under the Companies Act 71 of 2008" (2010) *Acta Juridica* at 306.
[45] Shoba "South Africa's Foreign Policy Position in BRICS" (2018) *Journal of African Unions Studies* at 173-188.
[46] The Model Business Corporation Act of 2002.
[47] The General Delaware Corporation Law of 2001.
[48] The Securities Act of 1933.
[49] The Securities Exchange Act of 1934.
[50] The Williams Act of 1968.
[51] Hammack "A Comparative Analysis of U. and UK Regulations Pertaining to Domestic Corporate Takeovers, and the Resulting Differences in Hostile Takeover Activities between the Two Markets" (2017) *Willamette Journal of International Law and Dispute Resolution* at 125.
[52] The City Code.
[53] The Companies Act of 2006.
[54] The Companies Act of 2013.
[55] The Competition Act of 2002.
[56] The Foreign Exchange Management Act of 1999.
[57] The Securities and Exchange Board of India (Substantial Acquisitions Shares and Takeovers) Regulations of 2011.

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Most significantly, an international reference team of specialists recommended most of the principles in the South African Act and actually drafted the 2008 Act.[58] Their mandate was to draft the 2008 Act in plain and simple language that would be readable and understandable to commercial participants.[59] This makes foreign law relevant to the interpretation of parallel provisions in the 2008 Act.[60] It is also important to understand the company laws of those countries from which South Africa borrowed the laws and the reasons for adopting the rules of that particular jurisdiction.[61]

Furthermore, most of the above-mentioned jurisdictions have advanced judicial systems that deal with merger and acquisitions transactions.[62] These countries have well-developed takeover regimes irrespective of the fact that they have adopted different approaches to takeover regulation.[63] Therefore, it would be sensible to compare the current South African takeover regime with these advanced takeover regimes and propose recommendations for legislative reform if necessary. However, it must be noted that the purpose of this comparison is to learn, not to copy from these jurisdictions. This is in light of the fact that this study aims to assist in constructing a modern legal system with South African characteristics, which caters for companies operating in South Africa. In addition, the purpose of this comparative analysis with these jurisdictions is not to discover which is best[64], but to find solutions to the problems identified in this study.

1.5 Research structure

The balance of this thesis is structured as follows:

1.5.1 Chapter 2: The influence of shareholder protection rules enactment

This chapter looks at the influence of rules in South African takeover regulation and refers to foreign law, as South African takeover law is influenced by other jurisdictions' takeover laws. In a way it compares the developmental history of takeover laws and different reasons why takeover laws were adopted in different jurisdictions. This could

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[58] Yeats "Putting Appraisal Rights into Perspective" (2014) *Stellenbosch Law Review* at 329.
[59] *Ibid*.
[60] *Ibid*.
[61] Sutherland "The State of Company Law in South Africa" (2012) *Stellenbosch Law Review* at 159.
[62] Klaus, Hopt and Wymeersch *European Takeovers: Law and Practice* (1992) at 10.
[63] *Ibid*.
[64] Ventoruzzo "Europe's Thirteenth Directive and US Takeover Regulation: Regulatory Means and Political and Economic Ends" (2006) *Texas International Law Journal* at 176 provides that there is never a best single model to deal with takeovers in the world.

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help in providing multiple solutions to a problem at different times, as no two jurisdictions experience the same event in exactly the same way. Case law will form part of this analysis, as some takeover laws, such as those of the UK, were influenced by judicial decisions and South African law is based on common law. A synopsis of this segment will be given at the end of the chapter.

1.5.2 Chapter 3: Fundamental transaction approval

This section comprises a comparison between South Africa, the UK, USA and India in respect of shareholder and court approval takeover provisions. Each provision's origin and evolution, its nature and effects are discussed. However, the main objective in the discussion is to demonstrate how each of these provisions conflicts with the value of restructuring business, as one of the purposes of this research is to highlight the conflict between the two values. The differences and similarities between takeover law regimes of the selected jurisdictions are discussed with explanatory notes on distinct features and indistinguishable features. Case law forms part of the analysis and a conclusion on the findings in the chapter is reached in relation to the analysis conducted in it.

1.5.3 Chapter 4: Dissenting shareholders

This chapter is a continuation of an analysis and comparison of takeover shareholder protection provisions of all jurisdictions chosen for the research. However, the body of the chapter highlights shareholder protection rules in respect of takeover laws that have the potential of frustrating the realisation of business restructuring. In support of this view, case law forms part of the analysis and a conclusion is drawn at the end of the chapter.

1.5.4 Chapter 5: Conclusions and recommendations

This segment of the research provides the main conclusion, which is drawn from the analysis and provides findings and recommendations in relation to the problem question and on how the 2008 Act could be improved or interpreted, so that the provisions in relation to takeovers can be fully realised or the conflicting rules can be balanced.

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CHAPTER 2

Influence of shareholder protection rules enactment

2.1 Introduction[65]

The central focus of the thesis was identified above in paragraph 1.4 *Purpose of the research and methodology*, namely to highlight how takeover rules conflict with one another and end up frustrating one another's initial purpose. However, this chapter looks at the influences of takeover regulation in South Africa.[66] The purpose is to: (i) understand the applicable rules better in order to highlight how they conflict;[67] (ii) identify if South Africa had a similar stance to the jurisdictions discussed and enacted rules that are similar to those jurisdictions. This is done in pursuance of one of the purposes of this research, as identified in paragraph 1.4 *Purpose of the research and methodology*, that South Africa needs to adopt a takeover legal system with South African characteristics, which caters for its market practices.

Furthermore, as hypothesised in the central focus of the thesis, South Africa has incorporated rules that are in conflict with one another into its law by way of adopting the latest developments in international leading countries. This approach was adopted as opposed to inventing provisions that solve the problems that are unique to the South African context.[68] South Africa and the countries that influenced most of the South African company law provisions are very different in terms of their political and

[65] This chapter assists in showing how South Africa adopted a shareholder-centric approach, which led to shareholders deciding in fundamental transactions, which is discussed in detail in para 3.2.1 Origins. This chapter furthermore assists in terms of jurisdictions that have more experience in dealing with takeovers, which will bolster the arguments raised in this research on the threshold aspect. This is discussed in detail in para 3.2.3 Observations and submissions.
[66] This is done taking cognisance of foreign law, as South African takeover law has been influenced by foreign law to a certain extent, as indicated in para 1.4 Purpose of the research and methodology.
[67] See CHAPTER 3 and CHAPTER 4 below.
[68] Varottil "The Evolution of Corporate Law in Post-Colonial India: From Transplant to Autochthony" (2016) *American University International Law Review* 253-326 at 268 states that the impact of replicating English law, which favoured British businesses in India, had adverse consequences for the country, as such laws frequently ran counter to Indian local business interests.

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historical background. In this regard, South Africa recently became a democratic country; it adopted a new constitution 26 years ago, which restructured the legal framework.[69] In contrast, the UK and the USA gained their democratic independence long ago, indicating that these jurisdictions are not on the same political and historical footing.[70]

2.2 Historical background

2.2.1 South Africa

The most essential influence in South African company law has been English law subsequent to the establishment of the British settlement at the Cape in 1806.[71] The opening up of the gold and diamond fields in the late 19th century marked the first explosion in commercial activity in South Africa.[72] That was when English law began to have a profound influence on South African law, which was noticeable in 1827 when the First Charter of Justice started a Supreme Court at the Cape and appointed English judges familiar with English mercantile law, such as Sir William Burton, George Kekewich and Sir John Wylde CJ.[73] South African company law is an example of the assimilation of English company law. For example, on 14 August 1861 legislation was passed to limit the liability of members of companies of certain joint stock. This legislation was based on the English Limited Liability Act of 1855.[74] Even though this legislation was repealed by the Cape Companies Act[75], that legislation was also based on the English Companies Act of 1862. After a while the Cape legislation followed the same pattern of resorting to the most recent English legislation, namely the Companies Act of 1892.[76] This legislation was later repealed by the Union Companies Act of 1926, which was also based on provisions that were in force in England.[77] South African company law has been subject to continual change cultured by socio-

[69] This is highlighted in paragraph 1.1.3 The Constitution.
[70] Flinders *et al Book of History. A History of all Nations from the Earliest Times to the Present* (The Grolier Society, New York) (1951) at 5163. Also Kach "Democracy in America" (1933) *Commercial Law Journal* 324-328 at 325.
[71] Girvin "The Antecedents of South African Company Law" (1992) *The Journal of Legal History* 63-77 at 63.
[72] *Ibid.*
[73] *Idem* at 69-70.
[74] *Idem* at 70.
[75] Act 25 of 1892.
[76] Girvin *supra* n71 at 70.
[77] *Ibid.*

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economic advances and development in the UK.[78] From the above, one can conclude that South African takeover regulation was influenced by the most recent English law at the time. This English law that influenced South African company law, as discussed above, came from its own history. This was the basis for takeover regulations in English law, which later found their place in South African takeover regulation.

2.2.2 India

India is part of the common law family, like South Africa, as it has British colonial origins as part of the larger British Empire.[79] The emergence of modern business corporations in India can be attributed to the establishment of the English East India Company in 1600, which created a monopoly to trade in India after it was granted a royal charter.[80] After that, companies were established and carried on business without any law that regulated companies in India.[81] Proper legislation that regulated companies was promulgated in the year 1850 when India passed the Act of Registration of Joint Stock Companies. This legislation was in correlation with England's Companies Act of 1844 and marked the beginning of India's corporate law legislative development, keeping up with developments made in England.[82] In other words, corporate law in India operated as a continuous replication of English law and this continued for a period of over a century.[83] This legislation was later found to be ineffective as far as the lack of protection afforded to shareholders through limited liability was concerned.[84] The pattern of mimicking English legislation continued when India enacted legislation that conferred limited liability protection, following English legislation enacted in 1858. Even after the decolonisation of India in 1947 the influence of colonial laws continued and affected India's most significant piece of legislation, which was the Companies Act of 1956, as it modelled the English Companies Act of 1948.[85] The 1956 legislation provided for a scheme of arrangement or an arrangement

[78] The advances and developments in the UK are discussed in detail below in para 3.
[79] Jain *Outlines of Indian Legal and Constitutional History* (Wadhwa and Co. Nagpu, New Delhi) (2007) at 364-367.
[80] Harris *The English East India Company and the History of Company Law* (GA Deventer: Kluwer Legal Publishers) (2005) at 219-229.
[81] Rosen "The Myth of Self-Regulation or The Dangers of Securities Regulation without Administration: The Indian Experience" (1979) *Journal of Comparative Corporate Law and Securities Journal* 261-302 at 261-262.
[82] Varottil *supra* n68 at 263.
[83] *Ibid.*
[84] *Idem* at 264.
[85] Rosen *supra* n81 at 261-262.

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such as amalgamation, which was permitted as long as it was not prejudicial to the public interest.[86] Furthermore, it provided protection to shareholders in terms of the oppression remedy when the affairs of the company were conducted in a manner that prejudiced the public interest.[87]

2.2.3 United Kingdom

In light of the fact that South African company law and Indian company law were influenced substantially by English law, as indicated above, it makes sense to discuss English law and determine the initial purpose behind the enactment of shareholder protection rules. There is extensive history on what led to English shareholder protection rules being enacted as law.[88] Prior to the First World War, companies in the UK were generally owned and managed by families. This allowed these companies to evade the problems that are commonly associated with separation of control and ownership. However, this limited all expansion possibilities and inhibited the professionalism of management.[89] Of course, there were instances where families employed and remunerated external managers.[90] The family business dispensation changed when the first great wave of mergers began in the UK around the 1920s. During this time family-owned and -managed businesses began to sell their interests in the companies in the market. This was a result of a number of pressures such as state regulation of competition.[91] Owner-managers favoured mergers rather than cartels, which were found to be unstable, as they were the only way to restrict competition.[92]

The second great wave of mergers hit the UK during the 1960s, resulting in further significant changes to family-controlled and -managed companies. Control and ownership continued to separate and this led to the advent of professional managers who were not necessarily owners or shareholders in the companies.[93] The families who were the owners and managers of business continued to sell their shares that

[86] Varottil *supra* n68 at 278-279.
[87] *Ibid*.
[88] Pennington "Takeover Bids in the UK" (1969) *American Journal of Comparative Law* 159-193 at 159.
[89] Johnston "Takeover Regulation: Historical and Theoretical Perspectives on the City Code" (2007) *The Cambridge Law Journal* 422-460 at 423.
[90] Hannah "Takeover Bids in Britain before 1950: An Exercise in Business 'Pre-History'" (1974) *Business History* 65-77 at 66-67.
[91] *Ibid*.
[92] Johnston n89.
[93] Hannah *The Rise of the Corporate Economy* (1983) Ch 1 and 2.

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were held in merged companies and the purchasers of these shares were institutional investors. This kind of investor had gained an appetite to have shares in companies and by the end of the 1950s was beginning to dominate in the largest companies in terms of shareholder registers.[94] The change in ownership of companies from family ownership to institutional investor ownership had implications. In the main, companies were freed from financial constraints of family ownership and key decisions were placed in the hands of professional managers.[95] In all companies that did not have a major shareholder it meant that the minority shareholders did not have much choice but to give management a free hand in this regard.[96]

In the UK hostile takeovers did not occur until 1953, when a shoe retailer, J. Sears & Co ("Sears"), for the first time received a tender offer that was made directly to its shareholders by Charles Clore ("Charles").[97] Charles approached one of Sears's directors, informed him that he was interested in purchasing the Sears company and asked that the board recommend the sale to its shareholders so they would accept his offer. However, the board of directors turned down his proposal. This takeover attempt by Charles was viewed as an enormous shock for the board and, in responding to his attempts, it was desperate to frustrate unwanted bids in order to protect itself against the loss of positions in the company. The board promised to increase dividends and to revalue the company's property so that it would reflect higher value, but it was too late, as the majority of shareholders had accepted Charles's offer.[98]

Furthermore, around this period institutional investors such as insurers, banks and pension funds started to sell their shares at market price.[99] This was due to a number of factors, such as the fact that the Companies Act of 1948 for the first time required companies to disclose their current earnings publicly, inadvertently enabling predators

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[94] Johnston *supra* n89 at 426.
[95] *Ibid*.
[96] *Idem* at 427.
[97] Roberts "Regulatory Responses to the Rise of the Market for Corporate Control in Britain in the 1950s" (1992) *Business History* 183-200 at 186-187. For further reasons and an analysis of the reasons for the emergence of hostile takeovers in the UK see Johnston "Takeover Regulation: Historical and Theoretical Perspectives on the City Code" (2007) *Cambridge law Journal* 422-460 at 426-427.
[98] Armour *Enforcement Strategies in UK Corporate Governance: A Roadmap and Empirical Assessment in John Armour and Jennifer Payne Rationality in Company Law: Essays in Honour of DD Prentice* (UK, Hart Publishing) (2009) at 112.
[99] Roberts *supra* n97. Institutional investors played a pivotal role in the analysis of shareholder approval provisions in this research and they are discussed further in para 2.5 of this chapter and para 3.2.3 of Chapter 3.

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to investigate targets that could be acquired easily.[100] In addition, the fact that there was a rise in tax burdens meant that a larger portion of the profits of the company went to tax.[101] Consequently, directors reduced the amount that was distributed to shareholders, as they also had to put aside funds to grow the company.[102] Over time, this led to shares in companies being undervalued, compared to the assets, and provided an opportunity to the bidders that was too good to pass up.[103] As a result, once in control of a company, a bidder could simply sell the company assets for far more than what he had paid for the shares or liquidate the surplus value for him to realise large profits.[104] Bidders also replaced conservative management with management that would maximise returns generated by company assets.[105] Returns were maximised by, for example, selling the company's freehold properties to institutional investors such as insurance companies, leasing them back and distributing the surplus cash that was held within the company.[106]

2.2.4 United States of America

Meanwhile, in the USA hostile takeovers became increasingly common around the 1960s.[107] Before that, business was conducted in adherence to federal law such as the Securities Exchange Act of 1934 ("SEC Act") and Securities Exchange Proxy Rules.[108] One of the ways used through the SEC Act to force change in the control of a company was making a proxy contest with the intention of replacing the target company board.[109] However, this soon changed around the late 1950s and early 1960s when corporate raiders devised a more powerful strategy, which was a tender offer.[110] This was in light of the fact that proxy contests were an ineffective mechanism

[100] Bull *et al Bid for Power* (1961) (ELEK BOOKS, UK) at 30. Hopt *et al European Takeovers: Law and Practice* (1992) (Butterworths Tolley, UK) at 79.
[101] *Ibid.*
[102] Bull *supra* n100 at 30.
[103] *Ibid.*
[104] *Idem* at 31-32.
[105] *Ibid.*
[106] *Ibid* at 31-32.
[107] Chandler "Cash Tender Offers" (1969) *Harvard Law Review* 377-403 at 377.
[108] Armour *et al* "The Evolution of Hostile Takeover Regimes in Developed and Emerging Markets: An Analytical Framework" (2011) *Harvard International Law Journal* 219-286 at 239.
[109] *Ibid* at 239.
[110] Samuel and Taussig "Tactics of Cash Takeover Bids" (1967) *Harvard Business Review* 135-148 at 136-137. Alcock "The Regulation of Takeovers" (2001) *Journal of International Financial Markets* 163-166 at 164-165 stated that: "…almost everything was possible. There was little constraint on creeping control or protection of minorities. Potential bidders could privately buy shares or publicly purchase them in street sweeps ..."

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for obtaining control of a company because their success was dependent mostly on the bidder's powers to induce shareholders and the extent of dissatisfaction among the shareholders of the company.[111]

Tender offers were a powerful strategy and were found to be more effective than a proxy contest because the bidder offered hard cash to the shareholders, as opposed to a simple plea for the target shareholders' vote in a directorial election. The greater speed at which an acquisition could be executed provided the hostile acquirer with the ability to bypass the board of the target company and deal directly with the shareholders.[112] If it so happened that the takeover failed, it was possible for the acquirer to regain the expenses of that failed takeover.[113] Acquirers offered short-term but high-price deals on a first-come-first-served basis.[114] This conduct put pressure on shareholders to buy quickly, fearing that not doing so would result in them holding illiquid shares and being exposed to a squeeze-out merger at a lower price.[115] It was found that the tender offers made at the time were abusive towards the target companies' shareholders. In addition, the boards of these target companies were prevented from applying defensive actions against these tender offers.[116]

2.2.5 United Kingdom

In the UK, amidst the emergence of hostile takeovers as discussed above, a boardroom revolution was triggered. Directors in companies started to reverse the policy of retaining earnings of the company for fund growth and increasing dividend pay-outs to shareholders.[117] However, management was still not protected from removal from office, as most shareholders preferred tax-free capital gain to a taxable dividend income. This was due to the fact that they could sell out at the market price. During this period takeover bids became unavoidable, except if some form of capital

[111] Armour *et al* "Who Writes the Rules for Hostile Takeovers, and Why - The Peculiar Divergence of US and UK Takeover Regulation" (2007) *Georgia Law Journal* 1727-1794 at 1753. Samuel and Taussig "Tactics of Cash Takeover Bids" (1967) *Harvard Business Review* 135-148 at 136-137.
[112] Armour *supra* n98 at 242.
[113] *Idem* at 240.
[114] *Ibid*.
[115] Armour *supra* n108 at 1755 provides that until 1968 tender offers were strategically utilised by bidders to persuade the shareholders of the target company. The persuasive offers were called Saturday night specials. Tender offers were made over a weekend with no disclosure of information that could put the shareholders of the target company in a position that would enable them to make an informed decision and in this case the bidder was not an insider and therefore insider trading rules would not apply.
[116] Armour *supra* n98 at 241.
[117] Bull *supra* n100 at 11.

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gains tax had been imposed.[118] Management increasingly became desperate and started complex schemes to fend off unwanted bids.[119] An example of this is the Savoy Hotel affair.[120]

The board of Savoy Hotel Limited feared that a hostile takeover was imminent and its aim was to convert Berkeley Hotel into offices, as it was seen as more profitable than its existence as a hotel. The board drew up a scheme and put Berkeley Hotel beyond the control of the shareholders, which prevented bidders from changing its use as a hotel.[121] This scheme basically involved transferring the property of Berkeley Hotel to the Worcester company at its full market value in return for preference shares in Worcester company.[122] This meant that Savoy Hotel Limited had the full right to capital and the income after payment of certain preferential dividends.[123] The board of directors of Savoy Limited also created a staff benevolent fund, which consisted of ordinary shares in the Worcester company that were subsequently vested in trustees of the fund who could not be removed by the company.[124]

Berkeley Hotel was then leased back to Savoy Hotel Limited on condition that it would not be used for any purpose other than a hotel without the consent of the Worcester company trustees. This removed the possibility of a speculator profiting by taking control of these assets and selling them with a lease back. Although this matter never came before the courts, bidders requested assistance from the Board of Trade and this board appointed an inspector under section 165 of Companies Act of 1948 to investigate the matter.[125] The inspector was to investigate whether the board of Savoy Hotel Limited had committed a breach of fiduciary duties to the company or its members by launching the Worcester scheme.[126] The inspector found that the objective of the board of Savoy Hotel Limited to launch the Worcester scheme was to deny any person who might obtain majority voting control of Savoy Hotel Limited any power that might be used to bring about a sale or change of control in the Berkeley

[118] *Idem* at 37.
[119] *Idem* at 36-40.
[120] *Ibid.*
[121] For a detailed synopsis of this example, see Gower "Corporate Control: The Battle for the Berkeley" (1955) *Harvard Law Review* 1176-1193 at 1176.
[122] *Ibid.*
[123] *Ibid.*
[124] *Ibid.*
[125] *Ibid.*
[126] *Ibid.*

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Hotel, thereby discouraging those who were seeking control from pursuing their objective further.[127] There are several court cases in common law that dealt with such instances, which are part of a chain that led to the enactment of shareholder protection rules and are discussed below.[128]

2.3 Position at Common law

South African courts still refer to English cases for guidance when interpreting provisions of company legislation.[129] In the USA development of rules has always been dependent upon the accumulation of common law precedents.[130] Meanwhile, in India during 1936, Indian courts started to refuse to accept English court judgements as they were without adjusting and adapting them to the legal principles that suited the conditions of Indian society.[131] In English law, under common law, shareholders did not decide on an offer, as the board of the target company relied on the business judgment rule and bids were increasingly being contested.

Amidst the Notes on Amalgamations ("Notes") and takeover regulation still under consideration, the litigation that transpired as a result of defensive actions taken by the boards was coming before the courts with increasing frequency.[132] The general

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[127] *Ibid.*

[128] *Hogg v Cramphorn Ltd* [1974] A.C. 821, P.C., [1974] 1 All E.R. 1126 and *Howard Smith Ltd v Ampol Petroleum Ltd* [1974] A.C. 821, P.C., [1974] 1 All E.R. 1126.

[129] Girvin *supra* n71 at 72. There has been cause for concern regarding reliance on English cases for guidance when interpreting provisions of company legislation in South Africa. In the case of *Van Zyl v. Euodia Trust (Edms) Bpk* 1983 (3) SA 394 (T), the court had to decide whether the interpretation of South African company law provisions that had been imported from English law should be viewed as imported from English law, taking into account the interpretations by the English courts, or whether they should be interpreted as drafted. It was held that the intention of the legislature must be followed as opposed to the background of the existing common law position. In the case of *Wolhuter Steel (Welkom) (Pty) Ltd v. Jatu Construction (Pty) Ltd* 1983 (3) SA 815 (0) 816-826, it was held that although the English and South African legal principles differed, they were in fact substantially the same on closer examination. However, South African legal principles should be given precedence while English decisions will have persuasive force on similar provisions.

[130] Armour *supra* n98 at 239.

[131] Varottil *supra* n68 at 265. This was after India started to introduce amendment processes to its company legislation in 1936 as opposed to re-enacting legislation that was similar to the 1929 English legislation regulating companies. This trend started becoming evident in the judicial system; see *Ramanandi Kuer v Kalawati Kuer,* (1928) 30 Born. L.R. 227 § 9 (1927) where the Bombay High Court stated that: "where there is a positive enactment of the Indian legislature, the proper course is to examine the language of that statute and to ascertain its proper meaning uninfluenced by any considerations derived from the previous state of law – or of English law upon which it may have been founded."
Also in *Laguna Holdings v Eden Park Hotels (2013) 176 Comp. Cas. 118 (Del.),* the court selected principles that were handed out by English courts and decided that some provisions had to be read together to make sure that an order that was just and equitable was given.

[132] Johnston *supra* n89 at 436.

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approach under common law was that management was given wide discretion in terms of corporate decision-making and the business judgement rule was used. However, this business judgment rule was limited by the decision that was taken in the sense that it had to be motivated by a proper purpose.[133] Courts then used the proper purpose method to scrutinise if management decisions were camouflaged as anything but defensive measures in response to takeovers. Courts conducted a detailed examination of the factual context in which management's decision was made. This was done to ascertain the purpose behind management's decision. It was believed that this process could distinguish a legitimate business decision from illegitimate ones. This method was less satisfactory from the investors' perspective because it caused delay and uncertainty and made takeovers unlikely to succeed. Thus litigation was seen as an influential defensive measure to the implementation of takeovers.[134] Two leading cases serve as examples of the common law approach to giving effect to defensive measures:

2.3.1 *Hogg v Cramphorn Ltd*[135]

In this case the board of Cramphorn Ltd, a public company, received a takeover bid from Baxter.[136] The directors of Cramphorn reacted by creating a trust, which they alleged was for the benefit of the company's employees.[137] In this trust they allotted a number of shares and each share carried the right to exercise 10 votes on a poll vote.[138] The trustees of this trust were all nominated by the board of directors and the indirect control by these directors over the additional votes attached to these shares ensured that they remained in control of the company.[139] The board averred that the decision satisfied the business judgement rule in consideration of the basis that they as the board acted in good faith and in the company's best interest when they treated the employees in an enlightened manner.[140] However, Judge Buckley held that the board acted with an improper purpose, which was to maintain control of the company.[141] After referring to a long list of cases, it was established that the board

[133] *Ibid.*
[134] *Ibid.*
[135] [1967] Ch. 254, [1966] 3 All E.R. 420.
[136] *Idem* at 422-423.
[137] *Idem* at 420-421.
[138] *Idem* at 430.
[139] *Idem* at 423-424.
[140] *Idem* at 427.
[141] *Idem* at 426-427.

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had breached their fiduciary duties when they issued shares purely for the purpose of maintaining control of the company or the affairs of the company or for the purpose of defeating the wishes of the other shareholders in the company.[142] The ratio of the case was that the board was aware of a bid and they used their fiduciary powers purely for the purpose of manipulating the voting position and frustrating the bid.[143]

2.3.2 *Howard Smith Ltd v Ampol Petroleum Ltd* [144]

In this case the board of directors had two competing bidders and issued shares to their preferred bidder.[145] This reduced the control of the previous controlling shareholder to a minority shareholder and allowed an effective takeover offer to be made to their preferred bidder.[146] It was held that this was an improper use of fiduciary powers by the board.[147] The board argued that this conduct was merely for the primary purpose of raising capital for the company and to keep it going.[148] However, this was rejected on the basis that their intention was to make sure that the initial controlling shareholder did not effect a takeover of the company.[149]

2.4 Takeover regulation forums

2.4.1 The Jenkins Committee

In the UK during the late 1950s, uncertainty arose among the boards of target companies about whether they had the right to take action against hostile bidders. At that time, hostile bidders were free to do whatever they could to make their bids successful. However, the shareholders of the target companies were disadvantaged, as they were not given an opportunity to voice their own opinions about the takeover bids.[150] Courts applied the doctrine of proper purpose to scrutinise takeover defences during this period.[151] However, the delay in the litigation process and the uncertainty

[142] This was also found in the cases of *Piercy v Mills* [1920] 1 Ch. 77 at 85 and *Fraser v Whalley* 2 H & M 10.
[143] *Hogg v Cramphorn* [1967] Ch 254 at 428-429.
[144] [1974] A.C. 821, P.C., [1974] 1 All E.R. 1126.
[145] *Idem* at 1127.
[146] *Idem* at 1127-1128.
[147] *Ibid.*
[148] *Idem* at 1128.
[149] *Hogg v Cramphorn* [1967] Ch 254.
[150] Mukwiri "The Myth of Tactical Litigation in UK Takeovers" (2008) *Journal of Corporate Law Studies* 373-388 at 373-374.
[151] *Hogg v Cramphorn* [1967] Ch 254. This court case has already been discussed further under the position at common law.

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of the court's decisions meant that the courts were not acceptable as the only solution.[152] Management in companies increasingly started to use their power to hinder the progress of bids of which they did not approve and for the first time, regulation of takeovers was openly discussed.[153] Institutional investors started to lobby for takeover-related legislation in the UK and called for a code of conduct that could be enforced to regulate hostile takeovers.[154]

Two significant events related to the regulation of takeovers occurred in 1959. First, the Bank of England Governor convened a conference to consider the production of a code of conduct that could be applied to regulate takeovers.[155] The view was that if takeovers were correctly regulated they could be beneficial to the economy of a country.[156] A City Working Party was set up, consisting of representatives from merchant and commercial banks, institutional investment entities and major organisations in the UK. It produced the first set of regulations to deal with takeovers.[157] Notes were published on 31 October 1959 by the Issuing Houses Association in conjunction with a number of institutions in the city.[158] This was the very first attempt at takeover self-regulation, which in many ways played a part in the shape of the City Code.

Secondly, in November 1959 the Jenkins Committee was appointed, following Labour Party demands for a statutory body to regulate takeovers.[159] Even though many of the recommendations on takeover regulation that were made by the Jenkins Committee were not implemented in legislation, they somehow had a significant influence on the manner in which takeovers are currently regulated. The Notes commended the virtues of amalgamations and stated that shareholders should decide whether to sell their shares or not and that to allow the shareholders to make such a decision, it should be based on adequate information. Provision of this information and advice to the shareholders is the duty of the target board.[160] The board's obligation to provide

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[152] Johnston *supra* n89 at 422.
[153] Johnston *supra* n89 at 432-433.
[154] Mukwiri *supra* n150 at 373, 374.
[155] Roberts *supra* n97 at 194-195.
[156] *Ibid*.
[157] Johnston *The City Takeover Code* (Oxford University Press) (1980) at 29.
[158] Johnston *supra* n89 in Chapter 3.
[159] Roberts *supra* n97 at 194 and Johnston *supra* n157 at 22.
[160] See Report of the Company Law Committee, Cmnd. 1749 June 1962, paragraph 267. Johnston *supra* n89 at 29.

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information to shareholders was a reasonable and impactful change from the common law position, which did not require the board to make sure that shareholders were provided with information in order to make informed decisions.[161]

The case of *Re Everlite Locknuts*[162] discussed the fact that shareholders should be provided with sufficient information to make informed decisions. In this case, the court had to analyse the information that was provided to the shareholders by the board as part of its assessment of whether an offer under section 155 of the Companies Act 1929 was fair. The applicant in this case averred that the offer made to the shareholders of a company was unfair because the information that the board provided to the shareholders of the company was insufficient. The court stated that the offer was not unfair, but agreed that the shareholders had been provided with insufficient information to make an informed decision on whether the offer was fair in terms of the Notes. The Notes provide that shareholders must be provided with adequate information to make a decision in an offer. From this legal precedence one can conclude that the Notes were an important innovation in facilitating informed decision-making by shareholders of a company.[163]

Although the Jenkins Committee viewed takeovers and mergers as an important feature of economic growth and development, the committee felt that it should address a number of continuing abuses in the conduct of takeovers. The first was the issue of abuse of power by management (e.g. diverting company assets in ways to which shareholders would object, similar to the *Savoy Hotel* case discussed above).[164] The committee proposed a mandatory statutory provision requiring the approval of shareholders to be obtained where the board proposes the disposal of the whole or substantially the whole of the business or company assets.[165] This was not law at the time, as it was believed that this imposed a heavy burden on management and could easily be circumvented, as it identified one particular defensive measure.

The increase in the adoption of takeover defences, as indicated above, and the absence of mechanisms for enforcement and adjudication meant that the influence of

[161] This is a contentious issue and is discussed further in para.3.2.2 Nature and effect of the provision. It is a UK perspective and will be compared with the South African perspective in respect of shareholder approval provisions.
[162] In *Re Evertite Locknuts* [1945] Chapter 220.
[163] Johnston *supra* n89 at 432.
[164] Report of the Company Law Committee, Cmnd. 1749 June 1962, para 267.
[165] See generally Jenkins Report, above n160, paras 119-122.

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the Notes in the UK takeover market was insufficient in terms of protecting shareholders.[166] This called for a statute to regulate takeovers and the Notes, in this regard, were revised and extended.[167] The drafting committee drew up a draft of the City Code, which, after amendments, was approved by the association and published on 27 March 1968.[168] The City Code consisted of 35 rules and 10 general principles and, compared to the Notes, was far more comprehensive. The City Code required the same fair treatment among all the shareholders of the same class.[169] It prescribed equality of the same information to all the shareholders and compelled the board of the offeree company to provide their shareholders with their opinion on a bid.[170] The principle that was deemed most important in the City Code was the one that prohibited the board of a target company from frustrating an offer once it became aware of a bid without the approval of the shareholders.[171] Again, the choice of permitted defences against takeovers demonstrates that the City Code was mainly aimed at improving the position of shareholders.[172] The prohibition on the conduct of the board of a target company still applies today in the City Code under Rule 21.1(a), which reads:

> "During the course of an offer, or even before the date of the offer if the board of the offeree company has reason to believe that a bona fide offer might be imminent, the board must not, without the approval of the shareholders in general meeting:
>
> (a) take any action which may result in any offer or bona fide possible offer being frustrated or in shareholders being denied the opportunity to decide on its merits."[173]

The shareholders' approval provision is discussed further in Chapter 3.

2.4.2 Commission of Enquiry

Meanwhile in South Africa, as far as protection afforded to investors is concerned, the President of the Republic of South Africa appointed a Commission of Enquiry ("**the**

[166] Armour *supra* n108 at 1727-1759.
[167] *Ibid.*
[168] Johnston *supra* n89 at 38.
[169] Para 2 of the introduction of the Code.
[170] Rule 3 of the Code.
[171] Principle 4 and Rule 38 of the Code.
[172] Moon *Business Mergers and Takeover Bids* (Gee Publishing Ltd, UK) (1971) at 137.
[173] Rule 21.1(a) of the Code.

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Commission") on 14 October 1963 into the 1926 Companies Act. One of the terms of reference of the Commission was to consider what major amendments are required in company law, having regard to *inter alia* the protection afforded to investors.[174] This was in light of the fact that the Act hardly differed from the English Companies Act of 1908, and while English companies' legislation had been consolidated three times in a period of 50 years, in South Africa there was no consolidation.

The Commission recommended that there be disclosure of information on the current affairs of the company at frequent intervals.[175] This was raised as the Commission had noted that regarding approval, there was a world-wide trend towards the full disclosure of affairs of companies.[176] It also recommended that evolved investigative derivative action be brought by the shareholders of a company where directors of a company had committed wrong against the company.[177] This was because directors were in control of the affairs of the company and would most likely not bring an action against themselves.[178] The Commission concluded that the evolved remedy should not suffer from conceptual problems and procedural hazards afflicting the existing derivative action.[179] At that time derivative action did not play a significant role in the context of shareholder protection in South Africa as it did in the USA.[180]

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[174] Benade "The Commission of Enquiry into the Companies Act" (1970) *Comparative and International Law Journal of Southern Africa* 277-309 at 309.
[175] *Idem* at 293.
[176] *Ibid* at 293.
[177] *Idem* at 294-295.
[178] *Ibid*.
[179] *Ibid*.
[180] The commission in its report stated that the evolved derivative action should be utilised where any of the past or present directors of a company by any reason of any wrongful act or omission has caused damage to the company while the person is a director or is still a director for which he/she is liable to the company. Any shareholder may apply to Court for an order appointing a provisional curator *ad-litem* for the purpose set out hereunder. The applicant must satisfy the court that there is a *prima facie* case against the directors or director of the company and that a provisional curator-ad-litem must be appointed for the purpose of investigating whether there are present grounds for an action and whether the action would be the suitable option in all circumstances. The curator *ad-litem* has the same powers given in the Act to inspectors and those sections that describe such powers should apply *mutatis mutandis*. The curator *ad-litem's* first task should be to investigate whether there are grounds for an action and whether it is desirable for the shareholders or shareholder to bring an action on behalf of the company in the given circumstances and to report back to the court on the return day of the order. Furthermore, that court should have the power to order that the applicant provide security for the costs of the application for the appointment of the curator *ad-litem*. Lastly, on the return day, should the court be satisfied that there are grounds for such an action and that it is possible for such an action to be instituted, the court will confirm the appointment of the curator *ad-litem* and give its directions as it may deem necessary in regard to the institution and conduct of the case.

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The Commission also recommended that there be an extended oppression remedy that would be readily available to shareholders, as the remedy at that time was limited and not readily available to the oppressed shareholders against persons who were in control.[181] This was because the remedy needed the shareholders to show that they were being "oppressed", which was a high burden to prove and applied only when a company was being wound up.[182] The Commission recommended that all that needed be shown was that the conduct complained of was "unfairly prejudicial, inequitable or unjust", and that the requirement that it only applied when a company was being wound up be removed.[183] The fact that the Commission's reasons for the amendments in South Africa were that England had consolidated legislation three times in the previous 50 years whereas South Africa had not confirms what has been highlighted above, that South Africa was influenced by and resorted to whatever was the most recent English law at the time.

2.4.3 The Van Wyk De Vries Commission

In South Africa the Van Wyk De Vries Commission ("**De Vries Commission**") was appointed around 1963 to investigate the comprehensive reform of company law.[184] This De Vries Commission of enquiry on the Companies Act was a follow-up on the Jenkins Committee report in England, which was a response to the need for a major re-appraisal of existing companies' legislation.[185] The De Vries Commission report's main focal point was the departure of pure English company law practice from that of South Africa. It stated that it had observed that in the past decades differences had emerged between company activities and their underlying concepts in respective countries, along with the fact that the time had long passed for South Africa to write its own legislation other than what it found in the corresponding English legislation.[186] The De Vries Commission gave a report that led to the 1973 Act, but this too was found to be deficient in critical areas such as shareholder protection rules, as indicated in paragraph 1.1.2 The *1973 Act*.[187]

[181] Benade *supra* n174 at 295-296.
[182] *Ibid*.
[183] *Ibid*.
[184] DTI n1 at 7.
[185] Girvin *supra* n71 at 71.
[186] *Ibid*.
[187] Van Der Linde *supra* n3 at 260.

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2.4.4 Department of Trade and Industry policy guidelines[188]

It was felt that the framework of South African company law at the time was still based on foundations of English law that had been put in place since the middle of the 19th century by the British.[189] It was held that even though the 1973 Act was hailed as cutting the umbilical cord between English and South African company law, as shown above in the historical background, South African law was a reflection of English law and still adopted most of the provisions and principles of English law.[190] It was concluded that there was a need for South African company law to be shareholder-friendly, given that this boosts the economy in terms of investment and because there had been a rise in foreign investment and international trade in South Africa since 1994.[191] The 1973 Act was out of line with modern practices and found to be deficient in critical areas such as shareholder protection,[192] whereas the primary goal of company law should be to ensure that the shareholders of a company have explicit rights and have effective recourse whenever these rights are violated.[193] This led to the inclusion of shareholder protection rules in the 2008 Act. These are discussed further below.

The enactment of some of the shareholder protective measures occurred after the DTI policy guideline stated that the primary objectives of the takeover provisions in the 2008 Act should be to ensure that the interests of the parties involved in a takeover, including shareholders, are adequately protected.[194] The DTI policy guideline also stated that takeover bids were an important mechanism by which a person could replace inefficient management.[195] However, in the same manner it was important for

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188 DTI *supra* n1. It is briefly discussed in para 1.1.4 of Chapter 1, as it forms an integral part of this research, and serves as a point of reference, since it is relevant in the context of where we are and where we are heading. It is also referred to in Chapter 5 of this research.
189 DTI *supra* n1 at 7.
190 *Ibid*.
191 DTI *supra* n1 at 13.
192 This was pointed out in para 1.1.2 The 1973 Act.
193 *Ibid* at 35.
194 DTI *supra* n1 at 40. Professor Mongalo, in his article titled "An Overview of Company Law Reform in South Africa: From the Guidelines to the Companies Act 2008" (2010) *Acta Juridica* xiii-2 at xiii-xxv, names some of the participants that were heading the 2004 reform. Some of them are from the USA, which gives reason to believe that some of the laws enacted that were a result of this reform may have been influenced by the USA. That leads one to analyse their reasons for enactment as well. In addition, Allen and Kraakman, in the textbook titled *Commentaries and Cases on the Law of Business Organizations* (Aspen Publishers, New York) (2003) at 452 stated that the appraisal remedy, which is a shareholder protective measure under fundamental transactions on the Act, is taken from the USA.
195 *Ibid*.

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the interests of shareholders to be protected in the process, which should be the main objective of the takeover bid provisions in the 2008 Act.[196] Therefore, with the introduction of a statutory merger in the already existing fundamental transactions,[197] it was important that the 2008 Act should also protect shareholders when a company engages in an affected transaction.[198] The few shareholder protection rules that were linked to the provisions that catered for these fundamental transactions for the purpose of this study included the approval of shareholders, which is discussed in detail in CHAPTER 3 of this research. This protective measure requires the shareholders of a company to vote in favour of or against the proposed transaction and sets specific percentages for votes for the approval of certain transactions.[199] Furthermore, the court review of protective measure requires those shareholders who had voted in favour of a proposed transaction to obtain court approval if a certain percentage of shareholders voted against the proposed transaction.[200] This protective measure is discussed in detail in paragraph 3.3 *Court approval provisions*.

2.4.5 The Bhabha, and Parliamentary Standing Committee

In India, the Indian government appointed a committee under the chairmanship of C.J. Bhabha. The Bhabha Committee undertook an extensive exercise in interviewing experts and finally presenting a report to the government in March 1952, which led to the government enacting the Companies Act of 1956.[201] The inspiration for this legislation was drawn from the appointment of the Cohen Committee in England, which led to the enactment of the English Companies Act of 1948 after

[196] *Ibid.*
[197] The disposal of all or a greater part of the assets of a company, schemes of arrangement and offers.
[198] An affected transaction in the Companies Act of 2008 under s 117 is defined as:
'(i) a transaction or series of transactions amounting to the disposal of all or the greater part of the assets or undertaking of a regulated company, as contemplated in section 112, subject to section 118(3);
(ii) an amalgamation or merger, as contemplated in section 113, if it involves at least one regulated company, subject to section 118(3);
(iii) a scheme of arrangement between a regulated company and its shareholders, as contemplated in section 114, subject to section 118(3);
(iv) the acquisition of, or announced intention to acquire, a beneficial interest in any voting securities of a regulated company to the extent and in the circumstances contemplated in section 122(1);
(v) the announced intention to acquire a beneficial interest in the remaining voting securities of a regulated company not already held by a person or persons acting in concert;
(vi) a mandatory offer contemplated in section 123; or
(vii) compulsory acquisition contemplated in section 124'. This is similar to what constitutes a fundamental transaction as explained in n32.
[199] Section 115 of the 2008 Act.
[200] Section 115 of the 2008 Act.
[201] Gupta *Datta on the Company Law* (LexisNexis, New York) (2008) at 29.

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recommendations had been made by the Cohen Committee.[202] The Bhabha Committee report largely referred to English company law developments and considered what would be relevant for India at the time.[203] The Companies Act of 1956 took a different trajectory, even though it too was a result of a classic replication of English law. Constant amendments to the legislation were necessary to deal with problems that were unique to India's corporate setting and local conditions.[204] Furthermore, as indicated in the common law discussion, the Indian courts started to refuse to accept English court judgements, as these were made without adjusting and adapting the legal principles that suited the conditions of Indian society.[205] This substantiates what was hypothesised under the purpose of this research, that South Africa needs to adopt a takeover legal system with South African characteristics that caters for its market practices.

South Africa could also learn from India's transition from the replication of English law to being original when it enacted its current Companies Act of 2013 and its enforcement in part to replace the Companies Act of 1956. The Companies Act of 2013 was not merely a result of nearly two decades of debates and discussions, but was also a reaction to the problems that had plagued India in respect of corporate law and governance.[206] The evolution of India's corporate law can teach South Africa valuable lessons. Though India is part of the common law family, its corporate law has evolved to such an extent that it is different from that of its country of origin, which is the UK. This casts doubt on the assumption that all countries that are under common law bear similarities, implying that each country should follow corporate law that is best suited to it and that is built on the needs of that country rather than what the country of origin follows.[207]

With reference to India's 2013 company law, it makes sense to discuss the committee that led to its enactment. The appointment of an expert committee on company law under the chairmanship of Mr J.J. Irani in 2004 led to the Companies Act of 2013.[208]

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[202] Varottil *supra* n68 at 275.
[203] *Ibid*.
[204] Varottil *supra* n68 at 258.
[205] *Ibid*, *Laguna Holdings v Eden Park Hotels* (2013) 176 Comp. Cas. 118 (Del.) in this case the court selected principles that were handed out by English courts and decided that some provisions must be read together in order to make sure that an order that is just and equitable is given.
[206] Varottil *supra* n68 at 259.
[207] *Idem* at 260.
[208] *Idem* at 288-291.

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However, before that, there were challenges, as the Irani Committee had issued a concept paper to the public, inviting suggestions.[209] Thereafter, a report was issued for legislation, but the recommendations that were submitted to Parliament lapsed.[210] The bill was referred to a Parliamentary Standing Committee on finance ("**Standing Committee")** under the chairmanship of Mr Yashwant Sinha. This standing committee reviewed the bill and submitted a report in 2010.[211] This bill that was introduced by the Standing Committee, as opposed to the one that the Irani Committee submitted, was of immense significance, as it redefined the role of the corporation in the Indian context. The Government introduced this bill in Parliament in 2011, but it too was referred back to the Standing Committee for review of certain provisions.[212] The Standing Committee issued another report, which led to the Companies Act of 2013 being passed by both Houses of Parliament and receiving the assent of the President of India on 31 August 2013.[213]

Throughout several law reform processes that lasted for almost two decades before the enactment of the Companies Act of 2013 there was essentially no reference of English company law in the Indian Companies Act.[214] This was a very different Indian Companies Act from that of 1956, which was essentially a replication of the English Companies Act of 1948. This was despite the fact that English company law had made giant strides in its evolution since India's decolonisation with the Companies Act of 1985 and the subsequent Companies Act of 2006. Neither committee, meaning the Irani Committee and the Parliamentary Standing Committee, in its recommendations and reports ever made any significant reference whatsoever to the prevailing English position in company law.[215]

The Indian Companies Act as it currently stands has incorporated shareholder protection rules in the context of mergers and takeovers in view of the fact that section 230 of the Companies Act of 2013 provides that a tribunal needs to grant an order[216] whenever there is a proposal for a merger or an arrangement on application that may

[209] *Ibid*.
[210] Paterson "Corporate Governance in India in the Context of the Companies Bill 2009: Part 1: Evolution" (2010) *International Company and Commercial Law Review* 1-94 at 41-42.
[211] Varottil *supra* n68 at 289.
[212] *Ibid*.
[213] *Ibid* at 291.
[214] Varottil *supra* n68 at 288.
[215] Varottil *supra* n68 at 291.
[216] Section 230(1) of the Companies Act of 2013.

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serve as a takeover offer.[217] Obviously there must have been a meeting and voting must have taken place for the proposed transaction in respect of which an order is being requested.[218] Furthermore, whenever there is a purchase of minority shares in a company where the acquirer will become a holder of 90% or more of the shares in a company upon acquisition, he needs to notify other shareholders of the company of his intentions.[219] This is done to enable the minority shareholders to take steps to prevent potential adverse activities by the new controlling shareholder, because the minority may find themselves in a company where: (i) the danger of exploitation of resources in the company for private interest is rife; and (ii) corporate policy is unilaterally determined by the new controlling shareholder.[220] Therefore, rather than policing the behaviour of the new controlling shareholder, a way out is provided to exit the company in advance.[221] The protection measure is discussed further in Chapter 4 of this research. The Companies Act of 2013 further provides that a party can acquire the shares of a dissenter in any company, but this needs to be approved by shareholders holding no less than nine-tenths in the value of shares.[222] Lastly, an oppression remedy is provided that whenever the affairs of the company are conducted in a prejudicial manner, any shareholder may apply to the tribunal for an order rectifying the oppressive situation.[223]

2.4.6 The Senate and Revision Committee

2.4.6.1 Federal law

Following the trend of hostile tender offers as indicated above under the historical background, in the USA a New Jersey Senator, Harris Williams ("**Senate**"), in 1965 introduced a federal law bill that would set ground rules on how the 1980s takeover bids would be structured from thereon.[224] This was in response to offers that were strategically abusive towards the shareholders, as indicated above under the historical

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[217] Section 230(11) of the Companies Act of 2013.
[218] Sections 230(3) and (4) of the Companies Act of 2013.
[219] Section 236 of the Companies Act of 2013.
[220] Psaroudakis "The Mandatory Bid and Company Law in Europe" (2010) *European Company and Financial Law Review* 550-584 at 550-554.
[221] *Ibid*.
[222] Section 235(1) of the Companies Act of 2013. This is a contentious issue in this jurisdiction and will be discussed in detail in para.3.2.2 Nature and effect of the provision, and will be juxtaposed against shareholder approval provisions in South African law.
[223] Section 241 of the Companies Act of 2013.
[224] Armour *supra* n111 at 1754.

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background.[225] The bill would initially have required that the target company be given 20 days to respond to an offer, so that the target company could get its defences ready.[226] However, the Senate, the Senate committee and the Securities Exchange Commission worked together to refine the bill. As now enacted, the Williams Act of 1968 ("**Williams Act**") requires that any party that intends to tender an offer that would make that party obtain 5% or more of the target company's shares should give the shareholders of the target company the right to withdraw the shares that they had tendered to the bidder for the first seven days of offer.[227] The Williams Act also requires the bidder to purchase shares on a pro rata basis, allowing even shareholders who had tendered their shares at a lower price to be offered a price as high as that offered to the other shareholders who had tendered their shares at a higher price.[228]

2.4.6.2 State law

Lawmakers drafting state law passed essential reforms in the late 1960s. The first of these reforms was the 1967 amendments to DGLC. These amendments to the DGCL were made because of the recommendations of the Revision Committee, which was commissioned in 1967.[229] The changes that were made by this revision commission included a codification of the standard for reviewing self-interested transactions in these takeover offers, for example the board frustrating a takeover offer for job safety and not because of what is in the best interest of the shareholders.[230] This leads to the next point. There was no regulation at federal level that regulated anti-takeover defensive measures used by company boards in responding to and resisting takeover bids, even if it was for the benefit of shareholders. As shown above, federal law regulated strategic abusive takeover offers of acquiring parties in view of the fact that

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[225] *Ibid.*
[226] Notes "The Developing Meaning of 'Tender Offer' Under the Securities Exchange Act of 1934*"* (1973) *Harvard Law Review* 1250-1281 at 1254-1260.
[227] Section 14(d)(5) of the Williams Act.
[228] Section 14(d)(8) of the Williams Act. White "Conflicts in the Regulation of Hostile Business Takeovers in the United States and the European Union" (2003) *Ius Gentium* 161-195 at 161-166 provides that the focus on the Williams Act of 1968 maximises the information and freedom to target shareholders that are faced with a tender offer and this enables these shareholders to make the best decisions with regard to the value of their shares.
[229] William "A Case Study in Legislative Opportunism: How Delaware Used the Federal-State System to Attain Corporate Pre-Eminence" (1984) *The Journal of Corporation Law* 233-260 at 252-253.
[230] Samuel and Stapleton "Delaware's New General Corporation Law: Substantive Changes" (1967) *Journal of Business Law* 75-94 at 77-90. The reduction of appraisal rights during takeovers might be due to the conflict of the two values as hypothesised in this research. However, this is discussed in more detail in Chapter 3 of this research.

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shareholders were not given sufficient time to decide on offers.[231] This meant that regulation of how the board of a company reacted to an offer was left to the states through the passing of state legislation and interpretation by state courts, giving rise to case law.[232]

The case of *Unocal Corporation v Mesa Petroleum Corporation*[233], in respect of the board of directors of a company being authorised to protect the shareholders' interests in the company, serves as a rubber stamp case in line with Delaware law. The board of Unocal launched an offer to Unocal as a company, meaning Unocal made a self-tender to itself.[234] However, this self-tender offer excluded Mesa Petroleum, which held 13% of Unocal's outstanding shares.[235] The Delaware Chancery Court made a preliminary injunction against the self-tender offer that excluded Mesa Petroleum.[236] This injunction was made on the grounds that the board of Unocal had a fiduciary duty to treat all the shareholders of Unocal fairly, but the self-tender offer was discriminatory against Mesa Petroleum as a shareholder of Unocal.[237] However, the Delaware Supreme Court decided that a self-tender offer that is used against a hostile bidder, who happened to be a majority shareholder of Unocal, was valid.[238] In other words, the board had the right to apply defensive actions to frustrate a hostile takeover if it was in the best interest of the shareholders.[239] These defensive actions that are employed have proven to be for the protection of shareholders through the empowerment of the board of a company as opposed to shareholders.[240]

2.4.6.2.1 State anti-takeover laws

Between 1982 and 1989 most states passed anti-takeover laws in response to the appeals of companies that claimed that they were under threat of takeovers and

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[231] Boardman "A critical analysis of the new South African takeover laws as proposed under the Act" (2010) *Acta Juridica* 306-336 at 333.
[232] Armour *supra* n98 at 170-172.
[233] 493 A 2d 946 (Del 1985).
[234] *Idem* at 5-6.
[235] *Idem* at 3 and 12.
[236] *Idem* at 8.
[237] *Idem* at 12.
[238] *Idem* at 2-3.
[239] The measurement of whether the board is acting in the best interest of the company is not the subject of this chapter; the purpose of citing this case is to show how shareholder protection rules evolved over time.
[240] Luiz "An Evaluation of The South African Securities Regulation Code on Takeovers and Mergers" (2003) Thesis UNISA at 461.

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wanted some kind of protective statute.[241] Furthermore, political pressure played a part in the state legislature in the sense that if a party who is not from a certain state launches a takeover in that state, that will mean a significant job loss in the company taken over, as well as loss of community support, such as charitable donations made by the local company.[242] These anti-takeover laws took various forms, but their initial purpose was the same, namely to assist local companies by fending off unwanted hostile takeovers, by making them difficult to be taken over by companies from other states.[243] These state anti-takeover statutes went through three generations of development. These statutes started as protective measures for different stakeholders at large. However, over time these evolved and protected shareholders, as will be shown below.

2.4.6.2.1.1 First-generation statutes

In the first-generation statutes just after the Williams Act was passed as discussed above, state anti-takeover law became prominent and gave the boards of target companies powers beyond those of the Williams Act to resist hostile bids. These statutes enforced substantive and procedural requirements that made takeover bids difficult, as the statutes created substantial obstacles to a takeover.[244] However, these statutes were later found to be unconstitutional, as they interfered with the federal supremacy of the Williams Act.[245] This was in light of the fact that they gave state administrators the power to review offers on several grounds, such as the adequacy of disclosures and substantive fairness.[246] Holding a hearing to review an offer imposed a delay from when the offer was filed to when the offer became effective.[247]

Furthermore, the statutes ventured into governing takeovers involving companies that were incorporated in other states and this was held to be unfair for bidding companies.[248] In the case of *Edgar v MITE Corporation*[249] a statute governing

[241] Kenyon *Mergers and Takeovers in the US and UK* (Oxford University Press, UK) (2004) at 139.
[242] *Ibid*.
[243] Gaughan *Mergers What Can Go Wrong and How to Prevent It* (Wiley, UK) (2005) at 13. White *supra* n228 at 161-166.
[244] Armour *supra* n108 at 254.
[245] Bainbridge *Mergers and Acquisitions* (Foundation Press, UK) (2012) at 252.
[246] *Ibid*.
[247] Magnuson "Takeover Regulation in the United States and Europe: An Institutional Approach" (2009) *Pace International Law Review* 205-240 at 220-235.
[248] Gaughan *Mergers, Acquisitions, and Corporate Restructurings* (Wiley, UK) (2014) at 37.
[249] 457 US 624 (1982).

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takeovers in Illinois was found to be unconstitutional, as it was inconsistent with the dormant clause of the Constitution of the USA.[250] The Illinois Business Takeover Act required bidders to notify the target company and the secretary of the state 20 days before the offer was to become effective and allowed the secretary of the state to block a "nationwide" tender offer for a target company within that state if the bidder failed to comply with the law of disclosure as required in that state.[251] Moreover, it required the secretary of the state to hold a hearing at the request of shareholders who hold 10% of the shares that are subject to the offer made.[252] The Supreme Court decided that this Illinois Business Takeover Act under s.137.51 gave the shareholders of that state speculative protection and that it had no legitimate interest in protecting shareholders who are not resident in that state.[253] Basically, this meant that the state could not regulate companies that were not incorporated within that state regarding the protection of shareholders. This gave way to the second-generation statutes.

2.4.6.2.1.2 Second-generation statutes

The second-generation statutes corrected what was learnt from the first-generation statutes and narrowed their protection range. The protection of these statutes applied only to target companies that were formed within that state or that conducted business activities within that state.[254] However, they further enacted the fair price and control share acquisition provisions. The fair price provision prescribed that bidders must give an equal highest paid price for the shares of the target company during the tender offer process to all shareholders of that target company.[255] The control share acquisition prescribed that bidders would not have voting rights when they had reached a controlling percentage of the target's voting power[256] unless the majority of

[250] *Idem* at 624.
[251] *Idem* at 625.
[252] Rosenzweig "Private Versus Public Regulation: A Comparative Analysis of British and American Takeover Controls" (2007) *Duke Journal of Comparative Law* 213-238 at 213.
[253] Seretakis "Hostile Takeovers and Defensive Mechanisms in the UK and the United States: A Case Against the United States Regime" (2013) *Ohio State Entrepreneurial Business Law Journal* 245-280 at 272. *Great W. United Corp. v. Kidwell* 577 F.2d 1256, 1282-83 (5th Cir. 1978) and *Leroy v. Great W. United Corp* 443 U.S. 173 (1979); the court was of the view that the Texas long-arm statute serves as a protector for state shareholders and the community from a business restructuring proposal that comes with a hostile takeover. *Dart Indus. v. Conrad*, 462 F. Supp. 1, 9-10 (S.D. Ind. 1978); the court held the opinion that the statute serves as a protection for entrenched management.
[254] *Idem* at 272.
[255] DePamphilis *Mergers, Acquisitions and Other Restricting Activities* (2015) (Academic Press, United States) at 1735.
[256] Rosenzweig *supra* n252 at 213.

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the remaining shareholders in the target company granted them this voting power by supermajority vote.[257] This served as protective measure for the minority shareholders in a target company.

However, this statute did not go unchallenged. Its constitutionality was questioned under the case of *CTS Corporation v Dynamics Corporation of Am*.[258] The CTS Corporation ("**CTS**") fought against a takeover attempt by the Dynamics Corporation ("**Dynamics**") based on the Indiana business corporation law, which required that all disinterested shareholders of the target company must determine in a shareholders' meeting whether a bidder owning more than 20% of outstanding shares would have voting rights to his shares.[259] Dynamics challenged this statute by arguing that the statute was pre-empted by the commerce clause under the Williams Act and that it was unconstitutional.[260] However, the court in question held that this statute was constitutional.[261] Within a short time after this statute was regarded as constitutional by the court, most states in America enacted various anti-takeover laws.[262] Moreover, most of the hostile takeovers in the USA are now subject to the regulation of the second-generation anti-takeover statutes, as the provisions of this statute are enacted under the current DGCL.[263]

2.4.6.2.1.3 Third-generation statutes

The third-generation statutes were enacted in most states around 1980 and their purpose was to prohibit certain post-bid transactions. The most common ones in most states are business combination statutes, which prohibit a shareholder who is a prospective bidder and who has obtained a certain percentage of the target company's voting rights from making any post-bid acquisition for a period of five years from the date of the first acquisition unless the board of the target company approves this or a supermajority of the disinterested shareholders approve it or he meets a specific price

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[257] Wang "Takeover Law in the UK, US and China: A Comparative Analysis and Recommendations for Chinese Takeover Law Reform" (2013) (unpublished Ph.D. thesis, Salford Law School) at 98.
[258] 481 U.S. 69 (1987).
[259] *Idem* at 70.
[260] *Idem* at 89-96.
[261] *Idem* at 101.
[262] Herzel and Shepro "The Changing Fortunes of US Takeover Defense" (1988) *Company Law* 116-135 at 122-134.
[263] Armour *supra* n98 at 247.

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or any other conditions.[264] This provision falls under DGCL but requires three years instead of five.[265]

The constitutionality of the third statute was challenged in the case of *Amanda Acquisition Corporation v Universal Foods Corporation*.[266] The Amanda Acquisition Corporation ("Amanda") was a subsidiary of High Voltage Engineering Corporation, which was based in Boston.[267] Amanda initiated a tender offer to own all the outstanding shares of Universal Foods, a corporation based in Wisconsin.[268] However, Amanda was prevented from making this acquisition based on the Wisconsin Business Combination Act, which required that a bidder with 10% or more of the target company's voting shares needs to obtain the approval of the target company's board or wait for a period of three years to make a further acquisition within the same company.[269] In the Seventh Circuit Court of Appeals Amanda argued that the third generation statute was pre-empted by the commerce provision under the Williams Act.[270] However, this argument was denied and the constitutionality of the Wisconsin Business Combination Act was upheld.[271]

In the USA the Williams Act, as indicated above, regulates takeovers on federal level.[272] The position of the Williams Act is that shareholders of a target company should be provided with information and time to make an informed decision about an offer.[273] This position still applies even today in the Williams Act, considering the fact that under section 13 there are substantial disclosure obligations and these provide for an early warning system to inform a target company, including both the board and the shareholders, that there is a possibility of change in the company control.[274] The current DGCL deals with fundamental transactions including takeover offers on state level and provides protection to shareholders in the form of approval by them in light of the fact that whenever there is a proposition in a company for the sale, lease or

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[264] Fay "State Takeover Laws: Shareholder Protection, the Constitution, and the Delaware Approach" (1988) *Gonzaga Law Review* 249-296 at 268.
[265] Section 203 of the DGCL, Title 8. Boardman *supra* n231 at 335.
[266] 877 F 2d 496 (7th Cir 1989).
[267] *Idem* at 988.
[268] *Idem* at 989.
[269] *Idem* at 997-1000.
[270] *Idem* at 999.
[271] *Idem* at 1017.
[272] Section 13d of the Williams Act of 1968.
[273] *Ibid*.
[274] *Ibid*.

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exchange of all the property and assets of the company, there must be authorisation by a resolution that was adopted by the majority of shareholders of the company.[275] This is discussed in detail in Chapter 3. Furthermore, it provides for an exit remedy commonly known as an appraisal remedy and is similar to the one enacted in the South African Act.[276] This remedy serves as an exit mechanism for dissenting shareholders of a company who do not want to be shareholders anymore because of the proposal of a fundamental transaction by other shareholders in the company.[277]

2.5 Conclusion

From the above in can be inferred that South African takeover provisions have been influenced mostly by English law and so were those of India for some time. This influence in South African takeover provisions by English law led the researcher to examine the influences of shareholder protection rules in the UK as they had found their way to South African law through replication, as indicated above. From this analysis it was found that the regulatory framework that was regulating takeovers in the UK was developed to reflect the opinion of those that were professionally involved in the field of takeovers, namely institutional investors. This was because by the time the UK Takeover Code was drafted in 1968, institutional investors were already in co-ownership in family-owned businesses if not in entire ownership of the companies in the UK, which meant that they had emerged as a significant power in the UK business landscape.[278] Therefore with the strong presence of institutional investors in regulation there was better protection for shareholders' interests in the UK, as they looked out for their interests. This eventually included those from outside the UK.

As indicated above, the British government delegated the Bank of England, which set up a working group that was dominated by institutional investors.[279] Again, the

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[275] Section 271(a) of the DGCL, Title 8. This is a contentious issue in this jurisdiction and will be discussed in detail in para.3.2.3 Observations and submissions, and will be juxtaposed against the shareholders' approval provisions in South African law.
[276] Davids *et al* "A Microscopic Analysis of the New Merger and Amalgamations Provision in the Companies Act 71 of 2008" (2010) *Acta Juridica* 337-371 at 352.
[277] Cassim "The Introduction of the Statutory Merger in South African Corporate Law: Majority Rule Offset by the Appraisal Right: Part 2" (2008) *South African Mercantile Law Journal* 147-176 at 157 - 176.
[278] Armour *supra* n108 at 1771.
[279] Bebchuk and Ferrell "Federalism and Corporate Law: The Race to Protect Managers from Takeovers" (1999) *Columbia Law Review* 1168-1199 at 1192-1193 provides that the UK's takeover regulation—

> "'is not imposed from the outside by a detached governmental body but rather by a group that has strong connections to the interested parties' and that group 'gave less

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Takeover Panel, which is a pillar of the UK takeover regulation attending to takeover corporate disputes, was developed largely in accordance with the wishes of institutional shareholders.[280] The parties that designed the takeover rules in the UK were participating in the market practice and understood what would have assisted them and therefore they created a takeover system that was catering for their market practice. This substantiates the hypothesised statement in Chapter 1 that South Africa needs to adopt a takeover legal system with South African characteristics that caters for its market practices.

With respect to the USA, it was highlighted above that the boards of the target companies had more influence in the development of takeover rules in the USA.[281] This was influenced by the fact that states looked to maximise the number of companies that were incorporated within their states and therefore cared a great deal about managerial preferences.[282] As a result of caring for managerial preferences, states passed anti-takeover laws that offered more protection against takeovers with the intention to attract more companies incorporated in those states.[283] Such an influence and stance cannot be compared with any situation in the South African jurisdiction, as there are no states but provinces, which are all regulated under one national regulation. A replication of solutions into the South African takeover regulation of problems that were encountered in other jurisdictions but not necessarily in South Africa could have led to the hypothesised problem statement of conflict of rules as indicated in CHAPTER 1, since these different solutions from different jurisdictions catered for the particular jurisdictions' market practices.

Lastly, this analysis of the influence of shareholder protection rules is important, as it will aid in understanding various factors that were at play in different times of corporate law development relating to shareholders. This will assist in examining some of the

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weight to managerial interests because of the close connection at least some of them had with the interests of shareholders'."

[280] Armour J *et* al *The Anatomy of Corporate Law A Comparative and Functional Approach* (Oxford University Press) (2009) 83.

[281] Bebchuk and Ferrell "A New Approach to Takeover Law and Regulatory Competition" (2001) *Virginia Law Review* 111-164 at 121 provided that the states in competing with each other produced a systematic tendency that made states protect management excessively from takeovers.

[282] Loewenstein "Delaware as Demon: Twenty-Five Years after Professor Cary's Polemic" (2000) *University of Colorado Law Review* 497-540 at 502-508.

[283] Bebchuk and Cohen "Firms' Decisions Where to Incorporate" (2003) *Journal of Law and Economics* 383-426 at 383.

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present South African legislative provisions that will be analysed in Chapters 3 and 4 that follow.

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CHAPTER 3

Fundamental transaction approval

3.1 Introduction

As mentioned above, the purpose of this research is to highlight that shareholder protection provisions in the 2008 Act in relation to fundamental transactions frustrate the realisation of the fundamental transaction proposals.[284] Accordingly, this chapter analyses the approval methods in relation to fundamental transactions, namely the shareholders' approval and court approval.

It should be noted, in supplementing what was stated above, that the arguments that will be offered do not intend to make any claim that shareholder and court approval provisions should be annulled.[285] Instead, it is submitted that the approval requirements in respect of fundamental transactions act as deterrents at times. This can be attributed to the manner in which they are currently administered, resulting in an undesirable overreach that frustrates the realisation of fundamental transaction proposals.

This chapter also addresses the question of (i) whether the benefits of the approvals outweigh the cost of exploring solutions that are different from the current regime, and (ii) whether approval protective measures are so hallowed that amending certain aspects in their provisions that result in the frustration of realisation of takeover rules as hypothesised, would impair shareholders' interests. In summary, this chapter explores other ways of approaching shareholder protection measures without the unjustified effects.[286]

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[284] Para 1.4 Purpose of the research and methodology above.
[285] See para 1.4 Purpose of the research and methodology above.
[286] Similar notes were raised in an article by Gatti *infra* n290 at 842.

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3.2 Shareholder approval provisions

3.2.1 Origins

South Africa has adopted a shareholder-centric approach as opposed to a board-centric approach, meaning that the shareholders of a company are the decision-making authority under takeover regulations.[287] This shareholder-centric approach is similar to that of the UK and this could have resulted from the replication of English law, as indicated in paragraph 2.2.1 South *Africa*, of this research. The first signs of the shareholder approval provisions in respect of some of the fundamental transactions can be seen in the 1973 Act.[288] The approval applied to business acquisition and the scheme of arrangement and later applied to the merger and amalgamation provisions in the 2008 Act.[289]

In the USA shareholder approval in respect of fundamental transaction proposals began around the 1800s.[290] This shareholder approval requirement originally implied unanimous approval to alter the initial terms of an investment made by the shareholders.[291] From a structural and historical perspective, it was derived from old rules of the principle of the inviolability of a contract.[292] However, during the 1800s, unanimity went out of favour simply because it prevented strategic hold-outs at the expense of consolidations that were considered necessary for technological innovations.[293]

There are several traditional theories that justify shareholders having to approve mergers. One is that mergers are a fundamental alteration of what constituted the original investment contract and that it does not make sense for such important decisions to be taken by the directors of a company alone.[294] Another theory is that shareholders should be able to have a say in mergers because transactions such as mergers involve not only a pure business decision, but are essentially an investment decision that should be connected with those who will bear its effects, namely the

[287] Davids n276 at 339.
[288] Section 228 and 311 of the 1973 Act.
[289] Section 113 of the 2008 Act.
[290] Gatti "Reconsidering the Merger Process: Approval Patterns, Timeline, and Shareholders Role" (2018) *Hastings Law Journal* 835-960 at 843-844.
[291] *Ibid.*
[292] *Ibid.*
[293] *Ibid.*
[294] Gatti *supra* n290 at 843-844.

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shareholders.[295] An additional interesting theory is that shareholder voting in such transactions serves as protection against potential abuse by directors. This vote operates as a protection against potential conflicts of interest within management during deal negotiations, i.e. side payments or offers of career opportunities.[296]

3.2.2 Nature and effect of the provision

The shareholder approval provision in the current South African Act in relation to fundamental transactions serves as a shareholder protection measure. This is because for every proposed fundamental transaction in a company the 2008 Act requires that there must be approval by the shareholders of the company. This conclusion is drawn from the fact that section115 (1) and (2) of the current Act states that a company may not give effect to a proposed transaction unless shareholders of the company have approved it by way of a resolution.[297]

There were three methods of obtaining control of a company under the 1973 Act, namely business acquisition,[298] the scheme of arrangement[299] and takeover offers.[300] However, this position has changed under the 2008 Act as the US style merger takeover method was introduced into South African company law.[301] This was an addition to the methods of obtaining control of a company under fundamental transactions.[302]

3.2.2.1 Disposal of all or a greater part of a company's assets or undertakings

Section 112 of the 2008 Act provides that a company may not dispose of all or a greater part of its assets or undertaking unless that company has complied with the requirements of sections 112 and 115. This would normally occur when there is a sale of a major business or asset and such a transaction has an economic effect on

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[295] *Idem* 846.
[296] *Ibid.*
[297] Latsky "The Fundamental Transactions under the Companies Act: A Report Back from Practice after the First Few Years" (2014) *Stellenbosch Law Review* 361-384 at 363 states that the issue of obtaining approval from shareholders is debatable in regard to the approval being procured at a meeting even though this is the predominant view among practitioners in the market: that it cannot be done by way of a written resolution like a round-robin under section 60 of the 2008 Act.
[298] Section 228 of the 1973 Act.
[299] Section 311 of the 1973 Act.
[300] Section 440A to 440N of the 1973 Act.
[301] Boardman n231 at 308.
[302] These fundamental transactions are governed by part A of Chapter 5 of the Act and relate to the disposal of all or a greater part of the assets of a company or undertaking of a company, mergers and amalgamations and schemes of arrangement.

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shareholders. Such transactions may be labelled as one of the many ways for a predator to take over a business.[303] The 2008 Act describes the disposal of all or a greater part of the assets of a company or undertaking of a company as a disposal of 50% or more of the gross assets of a company fairly valued irrespective of its liabilities and 50% or more of the value of the company's entire undertaking fairly valued.[304]

In so far as disposals and acquisitions are concerned, the 2008 Act provides that no company may dispose of all its assets or a greater part of its assets or undertaking unless the disposal itself of all or a greater part of the company's assets has been approved by a special resolution of the company's shareholders.[305] This means that the disposal of the company's assets must be approved by shareholders of that company who hold at least 75% of the voting rights together and these voting rights must be exercised at a meeting where a sufficient number of persons are present.[306] A sufficient number refers to at least 25% of those holding voting rights being present or a higher percentage as may be set out in the company's memorandum of incorporation ("MOI").[307] This requirement is subject to certain exceptions. In this regard, it does not apply to: (i) transactions that are part of a business rescue plan; (ii) intra-group transactions that are between a wholly owned subsidiary and its holding company; (iii) transactions between two or more wholly owned subsidiaries of the same holding company or in a transaction between a wholly owned subsidiary of a holding company and a parent company of that holding company or wholly owned subsidiaries of that parent company.[308]

[303] Latsky *supra* n297.
[304] S 1 of the Act.
[305] S 112 of the Act. Boardman n301 at 307. There have been some arguments regarding when disposal actually takes place. In *Standard Bank of SA Ltd v Hunkydory Investments 188 (Pty) Ltd* 2010 (1) SA 634 (WCC), it was held that the registration of the mortgage bond over all or a greater part of the assets of a company did not initiate a disposal for the purposes of s 228 of the 1973 Act. Owen-Rogers AJ stated that it is inaccurate for one to set apart the mortgage as the first step to a sale in execution over the foreclosure of a mortgage, since it is not the directors of a company but the sheriff that sells the property in execution. This meant that for a mortgage property that was foreclosed, disposal did not take place when directors of a company entered into a mortgage of the same property after the sheriff sold the property in execution but rather when the sheriff sold the property in execution. This judgement substantiates the ordinary meaning of disposal as a way to part with an object by way of sale or bargain.
[306] The 75% threshold of voting rights can be reduced in the memorandum of incorporation of a company but there must be a difference to 10 percentage point between the special resolution and the ordinary resolution as provided under section 65(8) and (10) of the 2008 Act.
[307] S 115 (1) and (2) of the Act.
[308] S112 (1) of the Act.

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Prior to the above position, the 1973 Act only required a simple majority as opposed to the current special resolution that is required for the approval of the disposal of all the company's assets or a greater part of the company's assets. Boardman submits that the 2008 Act provides for the retention of a more stringent requirement to give enhanced protection to minority shareholders.[309] Furthermore, the 1973 Act exempts just two categories of intra-group transactions in contrast to the three grounds that are exempted from the approval requirements under the 2008 Act. The two categories under the previous legislative dispensation were transactions between a wholly owned subsidiary and its holding company, and a transaction between two or more wholly owned subsidiaries of the same holding company.[310] These exceptions in the 1973 Act were regarded as too restrictive and as imposing too high a burden, especially on those companies that were only seeking to transfer assets intra-group. Therefore, the 2008 Act, by exempting a further category of intra-group transactions from the special resolution requirement, but keeping other protection provisions, was seen as increasing efficiency and flexibility and most of all, encouraging investment.[311]

In contradistinction with the position in South Africa, in the UK company asset disposals are not subject to statutory regulations. However, these transactions are held as private treaty sales that are governed by the general law of contract.[312] As a result of this, any *unlisted*[313] company, private or public, in the UK can dispose of any amount of a company's assets or undertaking without the approval of its shareholders at all, whether by a special resolution or simple majority unless of course the company's MOI provides otherwise.[314]

There are measures that protect shareholders' interests despite the lack of the statutory shareholders' approval requirement. This is because the directors of a company that is disposing of its assets must be satisfied that the disposal is most likely to promote the success of the company and for the benefit of the shareholders as a whole, having regard to the long-term consequences of such a disposal and considering what impact the disposal would have on other stakeholders.[315] Should the

[309] Boardman n231 at 310.
[310] S 228(5) of the 1973 Act.
[311] *Ibid.*
[312] *Ibid.*
[313] Writers' emphasis.
[314] *Ibid.*
[315] S 170 to 177 of the Companies Act of 2006.

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disposal have a negative impact on the company, the shareholders have a right to bring an action against the directors of the company seeking relief on behalf of the company if the directors were in breach or negligent in promoting the success of the company for the benefit of the shareholders.[316] The directors of the company as well when effecting the disposal need to note statutory provisions that may render the disposal voidable, for example if the disposal of the company assets was undervalued or the disposal was conducted at a time when the vendor was technically insolvent.[317]

Notwithstanding these stipulations, for *listed*[318] public companies there are additional restrictions for companies that are seeking to make a significant disposal or acquisition.[319] These transactions must be approved by a simple majority of the shareholders of the company that is either disposing or acquiring. In order to measure whether a disposal or acquisition is significant, the listed company that is either disposing or acquiring must evaluate the size of the proposed transaction relative to the company by running four tests, which entail comparing gross assets, profits, market capitalisations and the capital of the company.[320] If under one or more of these class tests the transaction is found to be 25% or more of the size of the company, the transaction is deemed significant and will require the approval of shareholders of the company.[321] Exceptions to this general shareholder approval requirement are the same as the ones in the South African 2008 Act for intra-group transactions.

In the USA the requirement of shareholders' approval for the disposal of all or a greater part of the assets of the company differs from state to state.[322] However, for the purpose of this research the researcher looks at those states that are under Delaware law and the Model Business Corporation Act. Under Delaware law any company, whether private or public, may dispose of, lease or exchange all of its assets or undertaking if it has been authorised to do so by a resolution adopted by the shareholders of a majority of the outstanding shares of the company entitled to vote or by a majority of the shareholders having the right to vote for the election of the

[316] Section 260 to 264 of the Companies Act of 2006.
[317] Example of this is in Part 6 of the UK Insolvency Act of 1986.
[318] Writers' emphasis.
[319] Ch 10 of the UK Listing Rules.
[320] Annex in Ch 10 of the UK Listing Rules.
[321] Rule 10.2.2 of the UK Listing Rules.
[322] Boardman n231 at 313.

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board.[323] It is submitted that South Africa adopted the US model for business acquisitions that provides for greater shareholder protection by implementing the shareholder approval requirement for disposals.

However, the difference is that in South Africa the approval requirement applies to the disposal of all or a greater part of the assets of a company and in terms of the 2008 Act this means 50% or more of the assets of the company. In the USA under Delaware the approval requirement applies when there is a sale of all or substantially all of the company's assets, i.e. 100% of the company's assets.[324] It is submitted that the USA's provisions protect the majority of the shareholders, as an ordinary resolution is required, while the South Africa provisions protect the interests of the minority shareholders, as a special resolution is required. For those states that use the Model Business Corporation Act for the sale of all or a greater part of the assets of a company in a regular or usual course of business, there is no provision that compels a company to obtain the approval of shareholders,[325] unless that disposal will leave the company without significant continuing business activity.[326]

3.2.2.2 On the scheme of arrangement

The Takeover Regulation Panel in its 2013 annual report indicated that of the 45 affected transactions that it regulated and approved, about 19 were schemes of arrangement and only one of those transactions was in the form of a general offer. The scheme of arrangement has been a popular structure for affected transactions.[327] It is another mechanism through which a company can bring about any kind of takeover, whether it be a merger, demerger or internal reorganisation. It can be in any

[323] *Ibid.* Section 216 and 217 of the Delaware General Corporation Law, Title 8.
[324] In the case of *Hollinger Inc v Hollinger International Inc* 2004 CA No. 543-N in an opinion by Leo Strone of the Delaware Chancery Court in 2004 it was held that shareholder approval will be required if there is disposal of everything, as "substantially all" was taken to mean everything.
[325] Section 12.01 of the Model Business Corporation Act of 2002.
[326] Section 12.02 of the Model Business Corporation Act of 2002.
[327] Luiz "Protection of Holders of Securities in the Offeree Regulated Company during Affected Transactions: General Offers and Schemes of Arrangements" (2014) *South African Mercantile Law Journal* 560at 561. Payne J "Minority Shareholder Protection in Takeovers: A UK Perspective" (2011) *European Company and Financial Law Review* 147-173 at 152-153 discusses the use of the scheme of arrangement as another form of a take offer in the context of UK law. In the case of *Re Expro International Group plc* [2010] 2 BCLC 514 it was provided that a commonly used alternative structure is a scheme of arrangement apart from conventional bids. Furthermore, Latsky *supra* n297 at 368 states that the scheme of arrangement that was first introduced under section 311 of the 1973 Act later repealed by section 114 of the Act remains as an effective and popular method to take over and reconstruct a company especially in the listed environment, *despite* the introduction of the new statutory merger provision in terms of section 113 read with section 116 of the Act.

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structure that a company and its shareholders propose and agree on, including a consolidation of securities that are from different classes, a division of these securities into different classes, an expropriation of the company's securities from the holder of those securities, a reacquisition by the company of its securities, an exchange of securities for other securities or a combination of all the listed structures.[328]

Nevertheless, these are not the only methods by which a scheme of arrangement can be effected.[329] This makes it a considerably more flexible means to effect a takeover than either a standard takeover offer or a business acquisition.[330] A company's board may propose and implement any arrangement between the holders of any class of a company's securities and the company itself, provided that the company is not either in business rescue proceedings or in liquidation.[331] Also, importantly for the purpose of this research, as with any fundamental transaction, a scheme of arrangement must be approved by a special resolution of those shareholders who are entitled to exercise voting rights in respect of a scheme of arrangement proposal in terms of section 115 of the 2008 Act.[332] This means that shareholders holding 75% of the voting rights must vote in favour of the scheme of arrangement proposal at a meeting.[333] In this regard, there should be a quorum of at least 25% of all the voting rights that are supposed to be exercised on the proposal, or such quorum as may be prescribed in terms of the company's MOI.[334]

However, the definition of what qualifies as a special resolution under section 1 of the current 2008 Act gives way to the possibility of having a different percentage for approval as opposed to the default 75% of voting rights. This would be the case particularly where the change has been in terms of the company's MOI as contemplated in section 65(10) of the 2008 Act. In this regard, section 65(10) requires that where there is a deviation from the default 75%, there should still be at least 10% between what would constitute an ordinary resolution and a special resolution of the company.[335] In this special resolution the voting rights that would be exercised are

[328] Section 114(1) of the Act. Latsky *supra* n297 at 369.
[329] Cassim *et al Contemporary Company Law* (2012) 726.
[330] Boardman n231 at 314.
[331] Section 114(1) of the Act.
[332] Latsky *supra* n297 at 370. See also Luiz *supra* n327 at 575.
[333] Luiz *supra* n327 at 575.
[334] Section 115(2) of the Act.
[335] However, section 115 (1) of the Act states that in spite of section 65 and any memorandum of incorporation provision a company may not implement a fundamental transaction agreement unless

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those of the holders of that class of securities to whom an offer was made.[336] However, voting rights of the acquiring party (which would be an offeror in the case of a scheme of arrangement) and any related or concerted party are excluded from the quorum count and majority requirement.[337]

In contradistinction, the position under the 1973 Act was that all scheme of arrangement proposals had to be sanctioned by the court, except in limited circumstances.[338] In the UK, schemes of arrangement are regulated by Part 26 of the UK Companies Act as well as provisions of the Takeover Code. These were introduced in 1870 and their use was limited to arrangements between a company and its creditors and where a company was on the verge of being wound up.[339] However, over time, the restrictions were eased and now their schemes of arrangement can be utilised in many ways. For example, they can be utilised to effect an arrangement between a company and its creditors when a company is solvent or insolvent, alongside being wound up, or to effect a merger agreement between one company and another in order to re-organise their share capital into one company.[340] Hence the recent UK Companies Act describes the scheme of arrangement as an arrangement between a company with any class of its creditors and/or any class of its members.[341]

One of the most common uses of a scheme of arrangement in the UK is being an alternative to a takeover offer.[342] Here the bidder deals with the target company and not directly with the shareholders of the target company, since the scheme is proposed by the board of a company and an application is made to court to obtain an order for

that agreement has been approved in terms of section 115 and one of the requirements found under section 115(2) for such an agreement is approval by special resolution. This raises the question whether the introductory phrase of section 115(1) of the Act excludes the possibility of a company requiring a different percentage level for the approval of any fundamental transaction in its memorandum of incorporation. For a further discussion of this see Delport *et al Henochsberg on Companies Act 71 of 2008* (2019) 417-418.

[336] This means that an offer can be made to shareholders of a class as was held under *Kleena Industries (Pty) Ltd v Senator Insurance Co Ltd* 1982 (2) SA 458 (W) at 464 para. 459, *Namex (Edms) Bpk v Kommissaris van Binnelandse Inkomste* 1994 (2) SA 265 (A) at 290 para. 272-273 and *Verimark Holdings Ltd v Brait Specialised Trustee (Pty) Ltd NO* (unreported case) case no. 2009/22928 (28/08/2009). In the *Verimark* case it was held that those to whom a scheme of arrangement offer was made to are the ones that should vote on the matter.

[337] Section 115(3) (a) of the 2008 Act.

[338] Section 311 of the 1973 Act; Boardman n301 at 315.

[339] Joint Stock Companies Arrangement Act 1870.

[340] Payne *supra* n327 at 152.

[341] Section 895(1) of the Companies Act of 2006.

[342] Payne *supra* n327 at 152.

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a meeting of shareholders to approve the proposed scheme of arrangement.[343] The scheme of arrangement must be approved by a majority of a company's shareholders representing at least 75% of the voting rights or each class present and voting in a meeting, similar to the South African Act.[344] It has been noted that a bidder when utilising the scheme of arrangement in a takeover can acquire 100% of the target company when 75% of the voting rights are in favour the proposal, as indicated above. However, in terms of a general offer the bidder needs at least 90% acceptance of the offer by the target shareholders before he can acquire 100% of the target company.[345]

Concerns have been raised that this means that the minority shareholders can be bound by a lower percentage of the shareholders in a scheme than in a takeover offer.[346] It has consequently been suggested that a very high standard of approval be required for approving a scheme of arrangement under such circumstances.[347] However, the *status quo* of the courts is that whether a company proceeds by way of takeover or a scheme of arrangement is a matter of choice.[348] The courts have rejected the argument that where a scheme of arrangement is proposed as an alternative to takeover of a target company, the court should insist on 90% voting rights of shareholders' approval for a scheme and not 75%, given that the court still has to sanction the scheme in the end.[349] Also, on what constitutes a quorum, there is no requirement for 25% of the voting rights of shareholders of a certain class to be present. This means that in the UK a scheme of arrangement can be implemented by a single shareholder with less than 1% in the value of shares.[350] Furthermore, the scheme of arrangement in the UK has to be sanctioned by court. [351] Under the 1973

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[343] Section 896 of the Companies Act of 2006.
[344] Section 899 of the Companies Act of 2006. Payne *supra* n327 at 152. *Re Tea Corporation Ltd* [1904] 1 Ch 12 was stated that all those groups affected under the proposal of a scheme of arrangement must consider and vote on the proposal.
[345] Payne *supra* n327 at 154.
[346] *Ibid*.
[347] *Re Hellenic and General Trust* [1976] 1 WLR 123.
[348] *Re BTR plc* [1999] 2 BCLC 675, affirmed [2000] 1 BCLC 740, *Re TDG plc* [2008] EWHC 2334 (Ch), [2009] 1 BCLC 445.
[349] *Re National Bank* [1966] 1 WLR 819, *Re TDG plc* [2008] EWHC 2334 (Ch), [2009] 1 BCLC 445. Payne *supra* n327 at 155 states that courts are able to protect minority shareholding by ensuring correct class meetings are held and that minority shareholders have all the relevant information they need in order to determine whether they should attend resolution meetings and how to vote at those meetings. The fact that meetings of different classes are held means that shareholders should vote with others that have the same concerns and interests so that they make it more likely that the minority voice will be heard but that the level of protection will largely depend on the determination of how many class meetings are held.
[350] Boardman n231 at 316.
[351] Section 899(1) of the Companies Act of 2006.

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Act in South Africa, the scheme of arrangement was a court-driven process that had to be sanctioned by a court as indicated above, but this position has since changed under the 2008 Act. In the UK, once the scheme of arrangement is sanctioned by a court, it becomes binding on all the shareholders of a certain class of a company. [352] However, the court is never bound by the decisions emanating from a shareholders' meeting and it has unrestricted discretion as to whether or not to approve the scheme of arrangement.[353]

However, the court is most likely to approve the scheme, as it is only concerned with three matters.[354] First, the court needs to be convinced that there is compliance with the statutory requirements. In this sense, the court will want to see the explanatory statement submitted with regard to the scheme of arrangement (i.e. that it was adequate and the resolutions at class meetings were passed by the correct statutory majority of each class). If not, the court will not sanction the scheme. Secondly, the court will check if the majority of shareholders fairly represented the class.

If the court is of the view that the meeting was unrepresentative or that the holders of voting rights at the meeting voted with special interests to promote an aspect that differed from the interests of an ordinary but objective and independent shareholder, the court is unlikely to sanction the scheme. This is because the court will want to ensure that the decision taken on the scheme of arrangement in a meeting was representative of the class as a whole.[355] Although not common, the court, on occasion, has refused to sanction a scheme on this basis. For example, the court can refuse to sanction a scheme of arrangement proposal if the votes that are necessary to secure the approval were cast in order to promote a particular interest of some of the shareholders and the interest is not shared with the other shareholders of the same class as a whole.[356] Thirdly, the court will consider whether the proposed scheme of

[352] Boardman n231 at 316.
[353] Boardman n231 at 316.
[354] *Re Anglo Continental Supply Co Ltd* [1922] 2 Ch 723, 733, *Re National Bank Ltd* [1996] 1 WLR 819.
[355] *Re Alabama*, *New Orleans*, *Texas & Pacific Junction Railway Co* [1891] 1 Ch 213. This test by the court is similar to the requirement that shareholders should vote in good faith and in the best interest of the company when voting to amend the memorandum of incorporation of the company: See *Allen v Gold Reefs of West Africa Ltd* [1900] 1 Ch 656 and *Citco Banking Corp NV v Pusser's Ltd* [2007] UKPC 13, [2007] 2 BCLC 483 (PC).
[356] *Re BTR plc (Leave to appeal)* [2000] 1 BCLC 740. See also *Re British Aviation Insurance Co Ltd* [2005] EWHC 1621, [2006] BCC 14 where it was stated that while a low turnout in itself is not a valid reason for the court to refuse to sanction a scheme of arrangement, the size of the turnout might be a relevant reason in considering whether the result of the vote could have in some way been affected by collateral factors either of the shareholders or creditors with special interests.

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arrangement is one which a reasonable person would approve. Its role is not only to take into account the views of those who properly voted in favour of the scheme of arrangement proposal, but is strongly influenced by whether there is a substantial majority vote in its favour.[357]

Even though this provision has the potential to be valuable, in practice there has never been an instance where the court refused to sanction a scheme of arrangement on this basis.[358] The reason why the 2008 Act does not require that a scheme of arrangement be sanctioned by court, as the 1973 Act requires, is that the 2008 Act utilises the court approval process as a further shareholder protection platform after the shareholders' approval protection measure has been exhausted.[359]

Similar to the position in the UK, in India an arrangement includes reorganisation of the company's share capital by the division of shares into shares of different classes or by consolidation of shares of different classes, or by both of those methods.[360] These arrangements can be between a company and its creditors or any class of creditor, or its shareholders or any class of its shareholders. [361] This may be pursuant to an application that has been made by either of these parties to the Tribunal. The Tribunal may order that a meeting be held in a manner it prescribes between the affected parties on the proposed transaction.[362] A notice of a meeting for such an arrangement needs to be sent to all the affected parties, subject to the possibility of an objection being made by persons holding not less than 10% of the company's shares.[363] The approval of the arrangement is the same as the one in South Africa, as the arrangement must be approved by a majority of a company's shareholders representing at least 75% of the voting rights of each class present and voting in the meeting. However, it differs from the South Africa position where the approval has to be sanctioned by the Tribunal and the decision becomes binding on all affected parties.[364] Furthermore, in light of the fact that the arrangement may be used in a

[357] *Re Equitable Life Assurance Society (no. 1)* [2002] BCC 319.
[358] *Re British Aviation Insurance Co Ltd* [2006] BCC 14 at [75]–[76].
[359] Boardman n231 at 316.
[360] Section 230 of the Companies Act of 2013.
[361] Section 230(1) of the Companies Act of 2013.
[362] Section 230(1) of the Companies Act of 2013.
[363] Section 230 (3) and (4) of the Companies Act of 2013.
[364] Section 230(6) of the Companies Act of 2013

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takeover offer,[365] any parties that may feel aggrieved by the proposed arrangement may make an application to the Tribunal.[366]

3.2.2.3 On the merger and amalgamation provisions

The 2008 Act describes a merger and amalgamation as a transaction or a series of transactions between two or more companies on agreement and as a result forming one or more new companies, which hold all the assets and liabilities that were previously held by each of the merged companies separately or resulting in the dissolution of each of the merging companies to one new company or in the survival of at least one of the merging companies and vesting the surviving company together with new companies if there are, with all the assets and liabilities that were held by the merged companies previously.[367] In terms of the 2008 Act, once the merger agreement has been concluded between the merging companies, the board of directors of each of the merging companies must submit the transaction to the shareholders of their companies for approval.[368]

The merger transaction must be approved in a meeting where a quorum of shareholders entitled to exercise at least 25% of the voting rights exercisable in regard to the relevant matter at hand are present. The transaction must be approved by a special resolution.[369] In an earlier draft of the 2008 Act, there was a proposal that a simple majority of the voting rights would be sufficient for the approval of a merger, but given the nature of the transactions themselves in possibly causing expropriation of minority shareholders, it was decided that it is an appropriate policy decision to retain the established requirement of a special resolution for all fundamental transactions and not just for the merger.[370] Even though it may seem as if a merger needs to be approved by 75% of the voting rights of shareholders present in a meeting, this is not the case entirely, as this threshold can be reduced in a company's MOI, as long as there is a 10% difference between the special resolution and the ordinary resolution.[371]

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[365] Section 230(11) of the Companies Act of 2013.
[366] Section 230(12) of the Companies Act of 2013.
[367] Section 1 of the Act.
[368] Section 115 of the Act.
[369] Section 115(2) (a) of the Act.
[370] Davids *et al supra* n276 at 356.
[371] Section 65(8) and (10) of the Act.

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It is also noted that certain shareholders may not have voting rights in such a resolution, for example the holders of preference shares. Also excluded from the calculation of the quorum and approvals are voting rights that are controlled by an acquiring party, any person related to an acquiring party or any person acting in concert with the acquiring party.[372] This raises questions in a situation where the holding company and its subsidiary or subsidiaries of a holding company are merging or amalgamating companies and have to obtain a special resolution of shareholders in order to comply with section 115 of the 2008 Act.[373] However, section 115(4) of the 2008 Act states that voting rights controlled by the acquiring party (which may be the holding company) must not be included in the quorum of a meeting or exercise its voting rights in respect of the resolution. That being said, the 2008 Act in terms of section 1 describes an acquiring party as a person who, as a result of the transaction, would indirectly or directly acquire, indirectly or directly control or increase control of all or a greater part of a company's assets or its undertaking. This suggests that the acquiring party, which is the holding company, acquires direct control of all or a greater part of its subsidiary's assets or the undertaking of its subsidiary, making the holding company unable to vote in terms of section 115(4) as stipulated above. This makes a resolution impossible, as there are no other shareholders who can vote in favour of the merger or amalgamation.[374]

However, it has been suggested that the maxim *lex non cogit ad impossibila aut inutilia* (which means that the law never exists for an impossible purpose) applies in this case.[375] The effect of this principle is that the related parties would be excused from complying with such a requirement, as it is objectively impossible to comply with the relevant provisions. This is a principle that has been held as applying not only to criminal law, but to civil law as well, as it is not confined to any particular area of law.[376] There also appears to be no reason why it should not be applied to the current circumstances where the 2008 Act in itself excludes the shareholders of a holding company from voting on a special resolution that is required to approve a merger.[377]

[372] Section 115(3) of the Act.
[373] Section 113(4) (b) of the Act.
[374] Latsky *supra* n297 at 377.
[375] *Ibid.*
[376] *Gassner NO v Minister of Law and Order* 1995 1 All SA 223 (C).
[377] Latsky *supra* n297 at 378.

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Apart from the above-mentioned anomaly, in most instances the approval of shareholders of all the merging or amalgamating companies is required, which makes one question whether this is necessary in all circumstances because, as hypothesised, such a protection measure can deter a fundamental transaction proposal that is for the betterment of the company. As in other jurisdictions, like the USA, the approval of shareholders is not required if the acquiring company is significantly larger than the target company, in light of the fact that the transactions are merely seen as modest purchases done with a tax-related intention in mind and are not likely to have a significant impact on the shareholders of the acquiring company.[378] This also applies in a South African instance such as the one discussed above regarding a merger between a holding company and its subsidiary or a merger between two subsidiaries of the same holding company. A similar instance as the one applied in section 112 of the 2008 Act that exempts the shareholder approval requirement in intra-group transactions could be applied to mergers and amalgamations, as there is no good reason why a similar principle should not apply under the provisions of a merger in the 2008 Act.[379]

While the position in South Africa is that a merger needs to be approved by a special resolution, in the USA most states have a default requirement of a majority of the outstanding shares to approve a merger.[380] However, similar to the South African position, this too can be increased in the equivalent of the company's MOI.[381] In South Africa, as indicated above, the quorum requirement is 25% of the voting rights. In some of the states in the USA a higher quorum is required. This may vary considerably in other jurisdictions because of each jurisdiction's legislator's policy.[382]

Under Delaware, the approval requirement mostly covers the shareholders of the target company and not those of the acquiring company.[383] This is because section 251(f) of the DGCL states that a shareholder vote is not entirely necessary if the MOI of the surviving company is not altered and if the number of shares does not increase by more than 20%.[384] This means that cash mergers and medium to small acquisitions

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[378] Allen and Kraakman nat 135.
[379] Davids *et al supra* n287 at 357.
[380] *Idem* at 356.
[381] *Ibid.*
[382] *Ibid.*
[383] *Ibid.*
[384] Gatti *supra* n290 at 844.

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through a merger never trigger a shareholder vote in the acquirer.[385] In addition, under short-form merger statutes, such as the DGCL, a company is permitted to avoid a vote if the acquiring company already holds a higher percentage of the target company and the threshold is 90%.[386]

Furthermore, section 251(h) of the DGCL exempts the shareholders of the acquiring company from the voting requirement in a two-step merger if, among others, following the first step of a tender offer the acquiring company has a great number of shares, which at least equal the percentage of the shares in the target company. There are several theories regarding the rationale justifying the shareholder approval requirement in connection with mergers. The approval of shareholders is seen as necessary, since mergers are a fundamental alteration of the original investment contract and shareholders, as investors, should have a say in their investment; directors should not decide alone.[387]

However, this argument is no longer accepted as a rationale since there are other decisions in the life of a company that are arguably seen as equally critical and fundamental as a merger and yet they do not necessarily require the voting of shareholders.[388] Another rationale is that shareholders need to decide on mergers, as such transactions involve not merely a pure business decision, but an investment decision as well: an investment belonging to those who will bear its effects.[389] A more satisfying rationale is that shareholder voting in mergers offers protection against the potential abuse of directors in a typical final period situation.[390] By this is meant that the shareholders' vote operates as protection against peculiar conflicts such as potential side payments to management and career potentials.[391]

3.2.3 Observations and submissions

The statutory merger in its draft phase was criticised. A similar concern to the one raised under the scheme of arrangement as discussed above is that it is easier to have

[385] Thompson and Edelman "Corporate Voting" (2009) *Vanderbilt Law Review* 127-176 at 129-130.
[386] Section 253 of the Delaware General Corporation Act, Title 8.
[387] Gatti *supra* n290 at 844. Clark *Corporate Law* (1986) 414. Eastbrook and Fishel *The Economic Structure of Corporate Law* (1991) at 79.
[388] Allen and Kraakman *supra* n194 at 466-468.
[389] Eisenberg *The Structure of the Corporation* (1976) 1416.
[390] Gilson and Black *The Law and Finance of Corporate Acquisitions* (1995) 720-721.
[391] Manne "Mergers and the Market for Corporate Control" (1965) *Journal for Political Economics* 110-120 at 110-118.

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a 100% takeover in a company with a 75% approval threshold than in a general offer where 90% of shareholders' acceptance is required for compulsory acquisition. It was furthermore suggested that a very high standard of approval be required for approving a scheme of arrangement compared to the one in a general offer. In terms of the statutory merger it was raised that where shareholders receive cash for their shares in a target company, such a merger could be used to achieve a similar outcome as the one obtained in a compulsory acquisition of the shares of the minority, but with a lower approval threshold. In respect of the compulsory acquisition, the approval requirement is 90% of the shareholders in a company, whereas in a merger 75% of the shareholders must vote in its favour, yet obtain the same goal, which is 100% shareholding. This seems problematic in light of the fact that this could be used as a procedure to evade more stringent requirements of the takeover offer provisions, resulting in harming investor confidence.[392]

It was further argued that the shareholders' approval requirement as it stood in its draft phase meant that even if the quorum at a meeting of the shareholders of a company in respect of a merger is 100%, a small group of shareholders or even a single shareholder who holds more than 50% of voting rights in a company actually has the power to approve or even reject a merger all on his own, regardless of whether the other shareholders in the company are in favour of the merger or not. As a result it was felt that the draft of the 2008 Act was heavily weighted in favour of a dominant majority shareholder and was biased against the numerical majority.[393] Furthermore, the majority shareholder would not even have to hold 51% of the voting rights in a company in order to be able to reject or approve a merger, as a result of shareholder apathy. This would happen when a company has a large number of minority shareholders, each with a very small shareholding, who do not attend meetings, let alone cast their votes.[394]

This makes it possible in some cases that a favourable vote of as little 12.5% of voting rights would suffice for the approval of a merger, in view of the fact that the draft provided that approval must be obtained by a majority of shareholders at a meeting with a minimum quorum of at least holders of 25% of the voting rights being present.

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[392] *Ibid.*
[393] Cassim "The introduction of the Statutory Merger in South African Corporate Law: Majority Rule Offset by the Appraisal Right (Part 1)" (2008) *SA Merc LJ* 147-176 at 9.
[394] *Ibid.*

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This is cause for great concern for public companies in which a large block of shares is held by institutional investors. Therefore, based on the above, Cassim submitted that the shareholder approval threshold was very lenient and weighted more in favour of the controlling shareholders, since the draft failed to provide effective protection for minority shareholders.[395]

For the purpose of this research, it is submitted that the approval processes in terms of section 115 of the 2008 Act that have to be complied with in order to approve a fundamental transaction such as a merger can deter the very same fundamental transaction proposals for those companies that obtain resolutions through meetings.[396] This is because the processes and procedures provided for in the 2008 Act for the approval of fundamental transactions may cause delays that could lead to a company losing commercial opportunities. For example, a company may want to merge with another for the purpose of expanding its client base to make more profit. However, if such an opportunity is time-constrained it could lead to a fall-out of the whole proposed transaction due to the delay that may be caused by the approval processes and procedures that have to complied with in terms of section 115 of the 2008 Act. The approval processes cause delay in the sense that they provide that a special resolution for approving fundamental transactions has to be obtained in a meeting called for such a purpose only.[397]

Calling a meeting in terms of the 2008 Act is a process that causes delay in light of the fact that a notice has to be delivered to each shareholder with voting rights and this notice has to be delivered 15 days in advance for public companies and non-profit companies, and 10 days for other companies.[398] This meeting that is called for the approval of a fundamental transaction should serve no other purpose whatsoever than the purpose of obtaining a resolution for the proposed transaction.[399] This means that even if there were to be another meeting for a purpose other than to obtain a resolution on a fundamental transaction in a few days' time from issuing the notice, voting cannot

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[395] *Ibid.*
[396] It is stated that the predominant view among practitioners in the market appears to be that approval under section 115 of the Act is a must to be procured from a meeting and that this cannot be done in terms of a "round-robin" written resolution, as stated under section 60 of the 2008 Act. Latsky *supra* n297 at 363.
[397] Section 115(2)(a) of the Act.
[398] Section 62(1) of the Act.
[399] Section 115(2)(a) of the Act.

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take place on such a transaction, otherwise it would result in an invalid resolution, as there is non-compliance with the provision.

However, the 2008 Act provides that the 10 to 15 days' notice period, as applicable to different forms of companies, may be reduced in terms of a company's MOI.[400] However, this provision further provides that a meeting held after such a notice may proceed only if every shareholder that is entitled to vote in such a meeting is present and votes to waive the required notice for a meeting.[401] It also provides that the 10 to 15 days may even be extended, as it would be impractical when one considers it in view of institutional investors. Some of these entities may be based in a different country or even on a different continent. This may be the reason for the inclusion of a provision in the Act that allows a company to extend the notice of a meeting to more than the default 10 or 15 days in the MOI of a company if it wants to.[402] The writer submits that such an extension adds to the delay.

However, the inclusion of such a provision makes sense in light of the fact that shareholders' interests in a company count most, above all other reasons, even if that reason entails a company having to insert a shorter shareholders' meeting notice period in its MOI so that shareholders can hold meetings quickly for the purpose of obtaining a resolution. Furthermore, in consideration of institutional investors and the like in instances such as the one indicated above, the 2008 Act provides for shareholders acting other than at a meeting that a resolution may be submitted to shareholders of a company entitled to vote on such a resolution for consideration.[403]

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[400] Section 62(2) of the Act.
[401] Section 62(2A) of the Act.
[402] Section 62(a) of the Act.
[403] Section 60(1)(a) of the Act. Section 115(2) states 'fundamental transactions may be approved … in a meeting called for that specific purpose' suggesting that fundamental transactions can only be approved at a meeting. This is the view among practitioners as well as indicated in footnote 396 above. However, S 60 of the 2008 Act provides that resolutions can be obtained other than at a meeting and it does not expressly exclude resolutions of fundamental transactions. Furthermore, S 65 (2) of the 2008 Act empowers the board to propose "any" resolution to be considered by shareholders and to determine whether the resolution will be considered at a meeting or written consent in terms of section 60. The Act under section 63(2) and (3) provides for instances where there are shareholders who cannot attend a meeting, such as institutional investors, that they can attend a meeting in terms of electronic communication as long as the parties to the meeting can communicate concurrently with one another and the MOI does not prohibit this. This is still at a delay as by means of the 2008 Act to convene a shareholders meeting there must be a notice for such a meeting.

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However, the provisions further state that in such an instance, shareholders may submit their resolution within 20 days of receipt of the resolution.[404] This raises the delay threshold from the 10 to 15 days discussed above to 20 days, since there is a possibility of a further delay of 20 days, should the shareholders submit the resolution on the last day provided. For example, in considering all possibilities to the last, shareholders who are against the proposal and are most likely to vote against it may frustrate the proposed transaction, knowing that it is time-constrained, since resolutions come with detailed information in terms of section 65(4) of the 2008 Act, in order for them to make an informed decision. Such a shareholder may vote on the last day, knowing that further delay would cause a fall-out of the proposed transaction. Apart from this, the 2008 Act gives a shareholder leave to apply to court to set aside a resolution.[405] This could cause massive delay if the shareholder concerned feels that the resolution does not provide clarity, or does not come with sufficient information and explanatory material to make an informed decision.[406]

Furthermore, the 2008 Act gives power to a shareholder of the company or the company itself to apply for a court order to set aside a demand for a meeting to obtain a resolution for a fundamental transaction.[407] This application may be on the grounds that the demand is frivolous, vexatious or is for no purpose other than to consider a matter that had already been decided upon by the shareholders of the company.[408] This application may frustrate a proposed fundamental transaction that is time-constrained. However, this is further discussed in detail under the court approval analysis in this chapter.[409] A party to the proposed time-constrained transaction may start having second thoughts and doubts about the proposal and even consider other alternatives, resulting in frustration of the fundamental transaction in question. The fact that under the shareholder approval provisos powers are given to shareholders or a company to challenge a resolution on a proposed fundamental transaction, as discussed above, leads to poor allocation of financial resources, which may put a company out of pocket and end up being unable to afford the proposed fundamental

[404] Section 60 (1)(b) of the 2008 Act. Another alternative is getting shareholders to vote at a meeting but subject to the process of a notice to demand a meeting.
[405] Section 65(5) of the Act.
[406] Section 65(4) of the Act.
[407] Section 61(5) of the Act.
[408] *Ibid.*
[409] This is highlighted in para. 3.3 Court approval provisions, of this chapter.

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transaction, but this argument is further discussed in detail under the court approval provisions.[410]

In the USA a board-centric approach is followed, compared to the South African shareholder-centric approach when it comes to decision-making in the company.[411] However, shareholders have binding votes when it comes to ratifying fundamental corporate changes such as mergers.[412] Furthermore, in other structures such as sales of all or substantially all of the assets, they generally require formal shareholders' approval from the target shareholders.[413] This is a similar approach to the one followed in South Africa.

Shareholder voting in the USA has long been a necessary stride in the approval process in merger transactions and it is true for both the DGCL and the Model Business Corporation Act.[414] It has also been an important element and is taken seriously, considering the milestone cases heard. In the late 1980s there was a takeover case that established that "the shareholder franchise is the ideological underpinning upon which the legitimacy of directorial power rests."[415] Another merger and acquisition case in the late 1990s held that "because of the overriding importance of voting rights, the Delaware Supreme Court and the Court of Chancery have consistently acted to protect stockholders from unwarranted interference with such rights."[416] A merger in the USA forms one of the macro-areas in which shareholder

[410] *Ibid.*
[411] Thompson and Edelman *supra* n385 at 129-130 provide that in the USA shareholder voting plays a limited role when it comes to corporate decision-making and it is much more limited in a corporate sphere. In this respect, shareholders have binding votes only when it comes to the election of directors and ratifying fundamental corporate changes such as mergers. Goshen "Voting and the Economics of Corporate Self-Dealing: Theory Meets Reality" (2003) *California Law Review* 393-403 at 393-399 states that the idea of entrusting shareholders with the power to decide in fundamental transactions is supported by the concept that a merger is a transaction with momentous consequences for them as shareholders and therefore voting in such a transaction is the best way in which they can determine their preference.
[412] *Ibid.*
[413] Gatti *supra* n290 at 843. However, these jurisdictions are not similar. In terms of a tender offer in the USA, the board decides on a tender offer as opposed to the shareholders and the position in SA is the opposite. A tender offer is also subject to section 126 of the Act, which is the restriction of frustrating actions by the board so shareholders can have a say in terms of an offer made for their shares.
[414] Section 251 of the Delaware General Corporation Law, Title 8 and section 11.04 of the Model Business Corporation Act.
[415] *Blasius Indus., Inc. v Atlas Corp.*, 564 A.2d 651, 659 (Del.Ch. 1988). In the case of *Unocal Corp. v Mesa Petroleum Co.*, 493 A.2d 946, 959 (Del. 1985) it was held that the power rests in the shareholders, not the directors of a company, since the shareholders themselves have the power of corporate democracy at their disposal to oust the board if they are displeased with the actions of their elected representatives.
[416] *Paramount Communications Inc. v QVC Network Inc.*, 637 A.2d 34, 42 (Del. 1994).

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voting is crucial for the proper functioning of a company and courts stress the importance of a shareholder's voice in merger transactions.[417] The Delaware Supreme Court has held in mergers that shareholders are in control of their own destiny through informed voting and that this is the highest and best form of corporate democracy.[418] This belief has been reinforced by the Delaware judiciary.[419]

However, shareholder voting in a merger has been criticised because in almost half of the mergers in the USA, delay is caused by the shareholders' approval requirement.[420] Gatti submitted that this approval requisite takes between two and three months when the process is relatively swift, but in instances where it is not, it takes more than five to six months and this ensuing delay does not come cheap, especially if it is viewed in terms of opportunity costs.[421] The delay concerned can certainty put a deal at risk, as it may encourage buyer remorse about the deal in question, making the buyer pursue alternative offers and drop the initial deal. It may also discourage management in the ordinary course of business, as effective integration may be delayed, resulting in poor allocation of resources.[422] There is an argument to be made that the approval requisite may still serve as a safety measure in case of a board that has erred or acted in bad faith.[423] The approval process may also encourage directors to anticipate rejection from the shareholders in respect of poor deals and to present worthwhile deals for approval by the shareholders.[424]

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[417] Gatti *supra* n290 at at 838-839.
[418] *Williams v Geier* 671 A.2d 1368, 1381 (Del. 1996). The same sentiments as held in the last-mentioned case were quoted in the case of *Corwin v KKK Financial Holdings LLC* 125, A.3d 304, 313, n.28 (Del.2015). The Delaware Supreme Court upheld a Chancery Court's decision regarding the *Corwin* case and Chief Justice Leo Strine stated that the interested parties, which are shareholders, can always protect themselves at the ballot box by simply voting no to the proposed merger.
[419] The number of cases started with the Delaware Supreme Court 2015 decision in *Corwin v KKK Financial Holdings LLC* 125, A.3d 304, 313, n.28 (Del.2015), followed by several cases in 2016 Singh *v Attenborough*, 137 A.3d 151 (Del. 2016), *In re Volcano Corporation Stockholder litigation.*, 143 A.3d 727 (Del. Ch. June 30, 2016), *Larkin v Shah*, C.A. No. 10918-VCS, 2016 WL 4485447 (Del. Ch. Aug. 25, 2016), *In re Solera Holdings, Inc. Stockholdings Litigation.*, C.A. No. 10485-CB, 2017 WL 57839 (Del. Ch. Jan. 5, 2017).
[420] Gatti *supra* n290 at 838, 840.
[421] *Ibid.*
[422] *Ibid.*
[423] *Ibid.*
[424] Burch "Is Acquiring-Firm Shareholder Approval in Stock-for-Stock Mergers Perfunctory?" (2004) *Financial Management* 46-69 at 45-46. Shareholder voting is not seen as only beneficial to the rejection of bad deals, but also as having a positive impact on the offer price of their shares. This is in the light that when directors know that the shareholders have the power to say no to a deal, this worries them and it puts pressure on them to increase their bargaining power with the acquirer and as a result of this power given to shareholders, shareholders get to approve deals that have a more appealing offer price for their shares. As in the case of *In re Cox Comm'cns, Inc. Shareholders Litigation.*, 879 A.2d 604, 619

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That said, the shareholder approval requisite is not perfect in light of the reasons discussed above, including the fact that delay can jeopardise operations in a company and even endanger deal completion. Burch submitted that rather than having the approval requisite in all mergers, the system should be simplified to allow a vote in mergers only if a certain percentage of shareholders requests a vote in reaction to the merger proposal.[425] This is similar to how the 2008 Act holds a demand for a meeting in terms of section 61(3) (b) of the Act, which provides that a shareholders' meeting may be called if demands for the purpose are made and are signed by holders of 10% of the voting rights entitled to be exercised in relation to the matter proposed, which is to be considered at a meeting. This submission that was made in terms of the voting requisite in the USA will be discussed further in detail in Chapter 5 of this research, as it assists in shaping the recommendations that are made in this research based on the findings.

In the USA it is also noted that mergers that have to do with the Securities Exchange Commission take a long time to close, because of the significant lag in holding a meeting to let the shareholders vote.[426] The shareholders voting in a simple transaction such as a cash merger entails a host of activities, ranging from the selection of a proxy solicitor to the preparation of the preliminary proxy statement, to filing the preliminary proxy statement with the Securities Exchange Commission, to considering the Securities Exchange Commission comments on the filed preliminary proxy statement.[427] Furthermore, the meeting arranged by the board of directors cannot be held in under 10 days from approval.[428]

In addition, finalising the proxy statement after the comments made by the Securities Exchange Commission and submitting it while forwarding the copies to relevant shareholders is a further process that contributes to the delay in finalising the transaction.[429] Roe submits that the bulk of regulations that cause delay in holding a shareholders' meeting do not come from state law, but rather federal securities

(Del.Ch.2005) it was held that even though shareholders are not in the position to utilise the voting process as a way to get a last nickel out of a purchaser, they were nonetheless well positioned to police bad deals where the board of directors did not at least try to obtain a price that could be seen as fair for their shares.

[425] *Ibid.*

[426] Gatti *supra* n290 at 868.

[427] Section 240.14a-6 of the Code of Federal Regulations.

[428] Section 211-213 of the Delaware General Corporation Law, Title 8.

[429] Section 240.14a-6 of the Code of Federal Regulations.

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regulations.[430] A merger deal can also be delayed by factors other than the voting itself, such as antitrust requirements, structural complexities and other regulatory issues,[431] adding an extra layer to the procedural headache.[432] While it has been argued in the USA that out-of-pocket transaction costs and delays in relation to a merger are caused by shareholder voting, it has also been argued that the costs of a meeting in itself are not a major concern and are not enough reason or justification for doing away with the voting requirement, even though these may increase costs, since this increase will not be dramatic.[433]

The position in India and the UK in terms of the scheme of arrangement is somewhat different in terms of holding a meeting that can cause delay in light of the fact that one of the parties concerned has to make an application to court or the Tribunal that will give detail on how to hold a meeting.[434] In this regard the court or the Tribunal may give detail that provides for a shorter notice period or rule that a meeting be held in a few days from the order, considering submission of a time-constrained transaction. This was the position in South Africa under the 1973 Act prior to the 2008 Act, as indicated above. However, it is submitted that the process of making an application to court and the actual date of getting detail on how to hold a meeting on the proposed arrangement can take time as well and cause delay, unless there is a possibility of the application being brought to court on an urgent basis, as the South African High Court accommodates this for practical purposes, but in terms of the provisions provided under these Acts there is no such possibility.

Furthermore, in the 2008 Act other fundamental transactions, such as the disposal of all or a greater part of the assets of a company and an amalgamation or merger, approval is obtained in a meeting of shareholders. In India, for example, a company may call a meeting in terms of a written or electronic notice of not less than 21 days.[435] This is more than what the 2008 Act provides, but in India a shorter period for the notice may be given, provided that 95% of the shareholders who are entitled to voting

[430] In Roe "Delaware's Competition" (2003) *Harvard Law Review* 588-646 at 588-612 it was stated that shareholder voting is an overwhelming matter of federal regulation.
[431] Coates and Subramanian "A Buy-Side Model and Lockups: Theory and Evidence" (2000) *Stanford Law Review* 307-396 at 307-316.
[432] Gatti *supra* n290 at 870.
[433] Gilson & Schwartz "Understanding MAC's: Moral Hazard in Acquisitions" (2005) *Journal of Law Review Economic and Organisation* 330-358 at 333-334.
[434] Section 230 of the Companies Act and Section 896 of the Companies Act of 2006.
[435] Section 101 of the Companies Act.

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rights in the meeting consent in writing or via electronic mode.[436] This is a significant provision and may have been included in consideration of time-constrained transactions, as indicated above. In the UK a company may call a shareholders' meeting for the approval of a proposed fundamental transaction by giving at least 14 days' notice to the shareholders who have voting rights on such a transaction.[437] This is almost similar to the period provided under the 2008 Act.

However, in the UK a shorter notice period for holding a meeting than the one allowed is possible if the shareholders who hold voting rights for such a meeting consent to such a shorter period.[438] This is subject to at least 90% to 95% of shareholders agreeing to such a shorter notice period in a private company, whereas for a public company the threshold is set at 95% of the shareholders agreeing to such a shorter notice period.[439] The shareholders may also make an application to the court for the purpose of company shareholders holding a meeting.[440] Therefore, a concerned shareholder may make an application before the court to hold a shareholders' meeting after a shorter notice period in consideration of a time-constrained transaction.

There are significant provisions in the UK regulations that prove the arguments raised in this research. These provide for circumstances where shareholders' meetings in respect of mergers are not required[441] so as to eliminate further and unnecessary delay. In circumstances where there is an absorption by merger of all of the shares of the transferor company and where there is more than one transferor company, or each of these companies are held by the transferee company,[442] there are three main considerations that the court must take into account in order to make an order:[443] First, the court must be satisfied that the publication of notice of receipt of the draft terms of the merger by the registrar took place in respect of all the merging companies at least one month before the date of the courts' order.[444] Secondly, the shareholders of the transferee company must have been able to inspect copies of the merger documents in respect of both merging companies one month before the merger at the registered

[436] *Ibid.*
[437] Section 307 (1) and (2) of the Companies Act of 2006.
[438] Section 307 (4) of the Companies Act of 2006.
[439] Section 307 (9) of the Companies Act of 2006.
[440] Section 896 of the Companies Act of 2006.
[441] Section 917 of the Companies Act of 2006.
[442] Section 917(1) of the Companies Act of 2006.
[443] Section 917(2) of the Companies Act of 2006.
[444] Section 917(3) of the Companies Act of 2006.

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office and to obtain copies of such documents on request free of charge.[445] Thirdly, one or more shareholders in the transferee company who happen to hold together not less than 5% of the paid-up capital of the company, who had the right to vote at the meeting of the company, must have been able to require a meeting of each class of shareholders to be called for the purpose of deciding whether or not to agree to the merger proposal.[446] It is submitted that these exceptions to holding a shareholders' meeting to decide on mergers in the UK were made in consideration of the fact that time-constrained transactions may be frustrated by the restrictions imposed.

As an introduction to this research's follow-up argument on shareholders' approval for fundamental transactions in South Africa, the researcher reverts to the 2008 Act's draft phase criticism and comparative analysis. Bainbridge submitted that the draft as it stood was more lenient than the liberal amendments that were effected to the Model Business Corporation Act in 1999, which moved from the absolute majority to a simple majority approval requisite,[447] since it reduced the shareholder approval requisite from 50% of all the issued or outstanding shares of a company to approval by a majority of the votes that are present at a meeting and whose quorum consists of a majority of all the votes that are cast.[448] In essence a vote of just over 25% of a total of the votes of a company makes it possible to effect a merger in the USA, in contrast with more generous provisions in the South African draft, which supported the effect of a merger with as little as just over 12.5% voting rights of the total shares of a company in favour of a merger. However, it was highlighted that most of the states in the USA have not yet adopted the voting rules laid down in the Model Business Corporation Act as amended in 1999. At the time most states still applied the absolute majority vote requisite of all the issued or outstanding shares of a company as opposed to the simple majority vote requisite of all the votes cast, which is usually at a threshold of 50% of the issued shares, as in the DGCL[449] or 66,6% of the issued shares.[450]

Bainbridge submitted that while the absolute majority vote was a good concept in principle, it was not a well-suited one for South African law, as it is most likely to make

[445] Section 917(4) of the Companies Act of 2006.
[446] Section 917(5)(a) of the Companies Act of 2006.
[447] Bainbridge *supra* n245 624.
[448] Section 11.04(e) of the Model Business Corporation Act of 1984 as amended.
[449] Section 251(c) of the Delaware General Corporation Act, 2001.
[450] Bainbridge *supra* n245 at 624.

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the effectuation and approval of mergers difficult to accomplish in practice, solely based on shareholder apathy.[451] It was suggested that the simple majority principle requisite that was in the draft ought to be increased to a special majority requisite whereby a proposed merger would have to be approved by shareholders who hold at least 75% of the voting rights.[452] This is the current stance in the 2008 Act, but with a 25% quorum.

However, this 25%, which was in the draft, was disapproved and it was suggested that it had to be increased to at least 50% of the eligible shares. Bainbridge submitted that combining these two measures would ensure that a more appropriate and substantial majority of shareholders approve a merger, while at the same time remaining liberal and flexible to keep away from an unduly burdensome or preventative set of rules regulating mergers. Ultimately this would have entailed a merger having to be approved by shareholders of at least 37,5% of the voting rights in a company, which would still have been lower than the Delaware approval threshold of a majority of shareholders of all the issued or outstanding shares in a company. He further submitted that this proposal would ensure a balance of interests between the need to protect minority shareholders from the oppression of the majority and the need to effect fundamental changes in a company without that being discouraged by a troublesome minority.[453] However, the status quo provides that the 25% quorum can be increased or decreased in the company's MOI[454] but in terms of section 115(2) of the Act it can only increase for fundamental transactions.

Another factor raised was that the draft precluded shareholders of a company from inserting a clause in the company's MOI providing a higher threshold for the shareholders' approval than the default threshold. This did not improve matters in the sense that if there is a majority or controlling shareholding in excess of 50% of a company's shares, shareholders in that company may not be able to protect themselves by inserting a clause in the company's MOI providing that a merger requires a higher threshold than the default threshold provided, leaving the minority

[451] *Ibid.* In relation to the arguments to be raised in this research but under the Act if South Africa were to opt for an absolute majority vote principle in future it would eventually add to the number of undertakings that cause a conflict of rules as hypothesised in this research.
[452] Bainbridge *supra* n245 at 624450.
[453] This is the gist of what this research intends to achieve after proving that there is a conflict of rules between shareholder protection rules and fundamental transaction rules.
[454] Section 64(2) of the Act.

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shareholders to the mercy of the controlling shareholder who has the power to reject or approve a merger proposal.[455] However, this position has changed, because as indicated above, section 65(8) and (10) of the 2008 Act allows a company to set a different threshold in its MOI from the threshold provided in the 2008 Act.

For the purpose of this research, it is submitted that the resolution threshold approval processes in terms of section 115 of the 2008 Act that have to be complied with in order to approve a fundamental transaction such as a scheme of arrangement or the disposal of all or a greater part of a company's assets can deter the fundamental transaction proposals, especially if these take place in addition to the delay arguments raised above and not considered on their own.

This is in light of the fact that the processes and procedures aligned in the 2008 Act to be able to obtain a resolution to approve a fundamental transaction firstly provides for a very high *default*[456] threshold as opposed to other jurisdictions. This is to be shown below. The higher the threshold to create greater protection, the greater the chances of discouraging a party from implementing a fundamental transaction, as the approval process may appear to be more challenging. In weighing up the approval requirement against the protection of minority shareholders, it is submitted that the protection inadvertently limits the rights and options offered to the other shareholders of a company to restructure a company for its improvement.

Furthermore, although a special resolution threshold can be decreased in terms of the 2008 Act,[457] it cannot be less than 60%, since the 2008 Act provides that there must be 10% between an ordinary resolution and a special resolution.[458] In addition, an ordinary resolution cannot be less than 50%, since the 2008 Act provides that an ordinary resolution can only be increased to effect greater protection for minority

[455] Cassim *supra* n393 at 11-12. Also, on what was precluded was separate class voting in terms of a merger. Cassim submitted that the initial act should be amended so to include the facilitation of class voting especially in terms of preference shares that would result in being converted to shares of a surviving company carrying different preference and terms because of the merger, .Ssince separate class voting is seen as enhancing the protection of shareholders of that class from the abuse of the power of the majority shareholders and operating effectively and usefully as a class veto.
[456] Writers' emphasis.
[457] Section 65(10) of the Act. Except for JSE listed companies, listing requirements state that the 75% threshold cannot be lowered. JSE Limited Listing requirements (accessed 18/10/2019) https://www.jse.co.za/content/JSERulesPoliciesandRegulationItems/JSE%20Listings%20Requirements.pdf
[458] Section 65(8)(b) of the Act.

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shareholders, but not decreased.[459] This 60% is still higher than what other jurisdictions prescribe. For example, in the USA in those states that use the Model Business Corporation Act for approval of fundamental transactions, approval is granted by a majority of the votes that are present at a meeting and whose quorum consists of a majority of all the votes that are cast.[460] This means a vote of just over 25% of a total of the votes of a company makes it possible to effect a merger. Also, for those states that use the DGCL, a requisite of all the votes cast, which is usually at a threshold of 50% of the issued shares, is necessary for the approval of a merger.[461]

Moreover, in a case of the sale of all or the greater part of the assets of a company in South Africa, if 50% or more of the company's assets are being sold, a special resolution is required, whereas in the USA in regard to the DGCL a special resolution is not required unless substantially all of the company's assets are being sold.[462] By substantially all is meant essentially everything in terms of an opinion by Leo Strine of the Delaware Chancery Court on July 2004.[463] The lower threshold in this jurisdiction could be that the greater protection of shareholders ended up hampering the success of fundamental transactions as hypothesised in this research. This is based on the fact that this jurisdiction has far more experience than South Africa when it comes to takeover methods, as highlighted in Chapter 2 of this research.

Furthermore, as discussed above, the experience that all the states that used the Model Business Corporation Act in 1999 led to the Act being amended from the absolute majority to a simple majority approval requisite. This meant that the shareholder approval requisite went from 50% of all the issued or outstanding shares of a company to approval by a majority of the votes present at a meeting and whose quorum consists of a majority of all the votes that are cast. This meant that a vote of just over 25% of a total of the votes of a company makes it possible to effect a merger. As highlighted above, in the UK, company asset disposals are not subject to statutory regulations, which means that any unlisted company, private or public, in the UK can dispose of any amount of a company's assets or undertaking without getting the

[459] Section 65(8)(a) of the Act.
[460] Section 11.04 (e) of the Model Business Corporation Act of 1984 as amended.
[461] Section 251(c) of the Delaware General Corporation Act, 2001.
[462] Section 271(a) of the Delaware General Corporation Act, Title 8.
[463] *Hollinger Inc v Hollinger International Inc* 2004 CA No. 543-N.

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approval of its shareholders at all, whether by a special resolution or simple majority, as there are other protective measures that protect shareholders' interests.

Furthermore, for listed companies, private or public, there are restrictions on companies that are seeking to make a significant disposal of the company's assets. The restrictions entail that these transactions must be approved by a simple majority of the shareholders of the company that is either disposing or acquiring, which is lower than the South African threshold. Notwithstanding this, in some fundamental transactions these jurisdictions have the same or higher special resolution thresholds, but with a compromise in default quorums, as opposed to the South African jurisdiction. In the UK, for the adoption of a merger resolution 75% of the voting rights in value and each class of shareholders of each of the merging companies must be in favour of the proposed merger agreement[464], with a quorum of at least two persons present at a meeting, subject to the company's articles.[465] This is less than the South African 25% of all of the voting rights, or higher as may be required by the company's MOI or three persons if the company has more than three shareholders.[466] In India voting rights of 90% must be present at a shareholders' meeting in order to adopt a resolution that approves the merger proposal[467], with a quorum of two shareholders in a private company.[468] In the case of a public company with no more than 1000 shareholders a quorum of five shareholders is required; in a public company with more than 1000 but fewer than 5000 shareholders a quorum of 15 shareholders is required and in a public company with more than 5000 shareholders a quorum of 30 shareholders is required.[469]

3.3 Court approval provisions

3.3.1 Origins

In South Africa the first signs of court approval provisions in respect of some fundamental transactions can be seen in the 1973 Act. The court approval provisions applied to the scheme of arrangement,[470] where this fundamental transaction had to

[464] Section 907(1) of the Companies Act of 2006.
[465] Section 318 (2) of the Companies Act of 2006.
[466] Section 65(3) (a) of the Act.
[467] Section 233(1) (b) of the Companies Act of 2013.
[468] Section 103(1) (b) of the Companies Act of 2013.
[469] Section 103(1) (a) of the Companies Act of 2013.
[470] Section 113 of the 1973 Act.

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be sanctioned by the court; this could be a result of the replication of English law.[471] It might also be because in the UK a scheme of arrangement has to be sanctioned by court.[472] The provision later found its way to the disposal of all or a greater part of a company's assets or its undertaking, but under a different scenario, which will be discussed briefly below.[473] Along with the merger and amalgamation provisions in the 2008 Act[474], it was the first ever approval of its kind under a merger provision. [475]

3.3.2 The nature and effect of the provision

It needs to be noted that the court approval provision under the 2008 Act is not a self-starter provision. It is reliant on the shareholder approval provision that was discussed in paragraph 2 above, hence the need to discuss the shareholders' approval provision first and follow up with the court approval provision. This is because if a company has to seek court approval for a proposed fundamental transaction there needs to be prior shareholders' approval.[476] Then if a certain percentage of shareholders vote against the proposed transaction, the company concerned will have to seek court approval to be able to proceed with the proposed transaction.[477] This is discussed in detail below.

3.3.2.1 On the disposal of all or a greater part of the company's assets

As indicated above in paragraph 3.2.2.1 *Disposal of all or a greater part of a company's assets or undertakings*, the disposal of all or a greater part of the assets of the company or its undertaking for its approval requires that 75% of voting rights in the company be in favour of the resolution.[478] In some instances the special resolution threshold may be different from the default 75% provided under section 65(9) of the 2008 Act. The shareholders of the company may agree on a different percentage and incorporate it in the company's MOI.[479] However, even if the resolution is adopted by virtue of the company's voting rights being 75% or the percentage prescribed in the company's MOI, it may not be implemented.[480] That is obviously if it was opposed by

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[471] See discussion in para 2.2 of Chapter 2 above.
[472] See discussion in para 3.2.2.2 above.
[473] Section 112 of the Act.
[474] Section 115(1) (a) and (3) of the Act.
[475] See detailed discussion in para 3.3.2.3 above.
[476] Section 115 of the Act.
[477] *Ibid*.
[478] Section 112(2) of the Act.
[479] Section 65(10) of the Act.
[480] Section 115 of the Act.

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at least 15% of the voting rights and the company is requested to seek court approval.[481]

Similar to all the other fundamental transactions, the company in question may be requested to seek court approval by a shareholder who had voted against an adopted resolution in a meeting that was called for that purpose.[482] In this instance the company, as opposed to the shareholder who made the request, bears the costs of the application.[483] Another instance where the adopted resolution may be put under scrutiny is when one of the shareholders, within 10 business days from the day of voting, makes an application to court for a review of the adopted resolution.[484] The court may allow such an application if it is convinced that (i) the application is made in good faith and not *mala fide*, (ii) that the applicant appears to be prepared and that he can sustain the proceedings and lastly, (iii) that the applicants' alleged facts, if proven, could constitute grounds for setting aside the adopted resolution.[485] In any of these cases the court will only set aside the adopted resolution if (i) it finds that the adopted resolution is manifestly unfair to any class of shareholders of the company concerned, or (ii) it finds that the votes that were cast regarding the resolution were materially tainted by inadequate disclosure, conflict of interest, failure to comply with the 2008 Act or the company's MOI or any rules applicable to the company and material procedural irregularity.[486] In both alternatives described above, despite the resolution having been adopted, it may not be implemented until the approval of court has been obtained.[487]

3.3.2.2 On the scheme of arrangement

In South Africa the scheme of arrangement, from its inception in the 1973 Act, was a court-driven process, since shareholders could apply to court so that the court could give detail on how the meeting for resolution adoption in respect of a proposed scheme of arrangement would be held between shareholders.[488] Then once shareholders were

[481] Section 115(3) (a) of the Act.
[482] Section 115(3) (a) of the Act.
[483] Section 115(5) (a) of the Act.
[484] Section 115(3) (b) of the Act.
[485] Section 115 (6) of the Act.
[486] Section 115(7) of the Act.
[487] Section 115 of the Act.
[488] Section 311 of the 1973 Act. This section provides for creditors as well but for the purpose of this research we will focus only on shareholders.

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in agreement in a meeting prescribed by the court, it could sanction the scheme of arrangement.[489] However, the procedure has since changed under the 2008 Act because of the need to be consistent with the drive to avoid excessive formalities in company regulation so that South African company law efficiency can be increased.[490] The 2008 Act provides that a shareholders' meeting needs to be held and the company's quorum as per the 2008 Act or alternatively as per the company's MOI needs to be met. In this shareholders' meeting, all shareholders with voting rights must cast a vote for the adoption of a special resolution in respect of the proposed scheme of arrangement.[491]

The resolution will be adopted if 75% of the voting rights are in favour of the scheme of arrangement or a percentage as per the company's MOI in what constitutes a special resolution.[492] However, if the adopted resolution approving the scheme was opposed by at least 15% of the voting rights, despite the resolution being adopted the company may not continue to implement it.[493] That happens if one or more of the 15% of the dissenting shareholders of the company concerned within five business days after casting his vote against the resolution requires that the company seek court approval for such a resolution to be implemented.[494] If the company does not apply to court for approval within 10 days after the voting, the adopted resolution will be treated as nullity.[495]

Another manner in which the company may be required to obtain court approval is if within 10 days after voting one or more of the dissenting shareholders, irrespective of 15% of the voting rights being against the resolution, applies to court to have the adopted resolution reviewed.[496] However, the applicant must have obtained leave from court first and as described above, with the merger provision in paragraph 3.3.2.1 *On the disposal of all or a greater part of the company's assets*, leave is only granted if the court is satisfied that the applicant is acting in good faith, appears to be prepared and able to sustain proceedings and that he has a *prima facie* case.[497] In both

[489] Section 311 of the 1973 Act.
[490] Boardman *supra* n231 at 315.
[491] Section 115 of the Act.
[492] This was discussed in detail under paragraph 3.2.2.2 above.
[493] Section 115 of the Act.
[494] Section 115(3) (a) of the Act.
[495] Section 115 (3) (a) and (5) of the Act.
[496] Section 115 (3) (b) of the Act.
[497] Section 115(6) of the Act.

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instances of having the matter brought before the court for approval, the court will only set aside the adopted resolution if it is satisfied that that the resolution was manifestly unfair towards holders of a specific class of shares, or votes cast were materially tainted by material and significant procedural irregularities.[498] However, if the court does not find that such impairments were present during voting, the scheme of arrangement will become binding among all the shareholders of the company, including the dissenting ones.

As indicated in paragraph 3.2.2.2 *On the scheme of arrangement*, in the UK the scheme of arrangement is a court-driven process. South African jurisdiction was the same until the 2008 Act abolished such provisions. Irrespective of what is highlighted above, Boardman submitted that the provisions that came with the 2008 Act were significant in view of the fact that court approval is not required anymore, as is the current stance in the UK.[499] He further submitted[500] that such an approach removes the need to have a court hearing, which is often an inefficient and costly rubber-stamping exercise. Also, that the South African jurisdiction has alternative protection in place for minority shareholders, such as the expert report on the proposed scheme of arrangement that the minority shareholders can use, as it gives these shareholders explicit rights to oppose prejudicial actions taken by the company.[501]

However, the provisions that were introduced by the 2008 Act in terms of the scheme of arrangement did not go uncriticised. Cassim submitted that the procedure was ill-advised and that the traditional approval of a scheme of arrangement as discussed above should have been retained as law.[502] The provisions under the 1973 Act in respect of a scheme of arrangement were both a court-free and a court-approved arrangement procedure that gave companies the option to rely on either. If an envisaged transaction was multi-layered and complex, the board of directors of that company might prefer to rely on the court's approval as an additional layer of review and protection,[503] or alternatively, where there was a merger of companies that were both illiquid but wished to avoid a cash drain that could result if one of the dissenting

[498] Section 115(7) of the Act. Procedural irregularities may stem from failure to comply with the Act or a company's memorandum of incorporation or applicable rules of the company.
[499] Boardman n231 at 316.
[500] *Ibid.*
[501] *Ibid.*
[502] Cassim *supra* n393 at 24.
[503] *Ibid.*

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shareholders exercised his appraisal rights in that statutory merger.[504] This was beneficial in the interests of shareholders when they believed that restructuring of the business could yield a positive result from a negative stance, and for the purposes of this study the shareholder protection measure was balanced so as not to frustrate the realisation of the proposed fundamental transaction.

Cassim further submitted that the South African jurisdiction should have retained the traditional procedure entailed in the 1973 Act and modernised it to create greater flexibility that would grant wider powers and wider discretion to the court, so that it could render the court-approved scheme of arrangement procedure less prescriptive. This was advised because the court at the time was not given wide discretionary powers enabling it to make a wide range of orders that would include making an order to convene a meeting of shareholders, or to specify who was entitled to be heard in the application for the scheme of arrangement approval, or to request a report on the scheme of arrangement.[505]

3.3.2.3 On the merger and amalgamations provisions

As already highlighted above in paragraph 3.3.1 Origins, the South African court approval measure in the 2008 Act under the merger and amalgamation provision was a uniquely South African protection, which did not exist in jurisdictions that have merger statutes. Even the USA, being the jurisdiction that influenced the statutory merger provision in South Africa, did not have a court approving provision in a merger.[506] Davids submitted that this was a result of a policy matter and was considered appropriate protection in a jurisdiction where people are more reserved on bringing lawsuits to protect their rights.[507]

Cassim submitted that this approach of permitting a statutory merger was patently a very significant liberalisation of policy on the part of legislation. The principle of majority rule would be enough to change the nature of the company and the nature of the investment of all the shareholders in a company fundamentally. All of this could be done without the need in general for any court approval of the merger because there

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[504] *Ibid.*
[505] *Ibid.*
[506] Davids *et al supra* n276 at 347-346. Cassim *supra* n393 at 1. Boardman *supra* n231 at 306. This is discussed in detail above in paragraph 3.3.2.1 On the disposal of all or a greater part of the company's *assets*.
[507] *Ibid.*

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is a balance of the majority rule with the right of dissenting shareholders who are able to withdraw the fair value of their shares in cash through the exercise of appraisal rights.[508] Nicholls submitted that when this liberal approach taken in the 2008 Act is compared with the conservative approach in the 1973 Act, [509] the statutory merger overrides the proprietary rights of dissenting shareholders in order to afford recognition to the general public interest of a corporate law regime that facilitates fundamental transactions and business combinations.[510] Unlike in the conservative approach, the shares of the minority shareholders can easily be expropriated because of the permissibility consideration in a merger.[511]

Austin and Ramsay submitted that this liberal approach in the 2008 Act would facilitate business combinations and fundamental transactions better, seeing that fundamental transactions are increasingly seen as beneficial to the economy and to wealth creation. Furthermore, failure by the directors to run a company efficiently, as reflected by underperforming shares prices, can render a company an easy target for a takeover through fundamental transactions by a more efficient management that will introduce improved allocation and use of resources in the market.[512]

However, both the court approval provisions and the appraisal rights as briefly discussed above are available to dissenting shareholders in South Africa. The court approval measure in a merger is initiated whenever there are shareholders holding 15% of voting rights who were present in a meeting called for the purpose of adopting a resolution approving a merger or amalgamation proposal and these shareholders holding 15% of voting rights voted against the resolution, together with the fact that these dissenting shareholders required the company to have the adopted resolution approved by court.[513] The company concerned has two options when this happens; it could either apply to court for the approval of the adopted resolution within 10 days of the votes being cast and bear the cost of the application or it could treat the resolution as a nullity.[514] However, it should be noted that the above is not the only cause of

[508] Cassim *supra* n393 at 20.
[509] Nicholls "Lock-Ups, Squeeze-Outs, and the Canadian Takeover Bid Law: A Curious Interplay of the Public and Private Interests" (2006) *McGill Law Journal* 409-426 at 409.
[510] *Ibid*.
[511] Cassim *supra* n393 at 20.
[512] Austin and Ramsay *Ford's Principles of Corporations Law* (2007) in paragraph 23.080.
[513] Section 115(3) (a) of the Act.
[514] Section 115 (5) of the Act.

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action that brings about a request for the company to seek the approval of the court regarding the proposal of a merger or amalgamation. The 2008 Act further provides an alternative to the above that any shareholder who had voting rights in respect of the adopted resolution and who voted against it, within 10 days of casting such a vote, can make an application for leave to appear before the court to apply formally for a review of the proposed transaction or adopted resolution.[515]

This court approval provision has been criticised in respect of its effectiveness as a remedy that could protect shareholders in practice. First, Davids submitted that the grounds on which a court may review and set aside an adopted resolution are relatively limited, in the sense that the 2008 Act requires not merely unfairness to any class of the company's shareholders. It requires manifest unfairness and that any procedural irregularity must have materially tainted the adopted resolution.[516] This sets the bar high for any potential review to succeed, but is seen as fairly high and not inappropriately high. This was because this standard review was measured against other jurisdictions' review processes. It was found that in the USA when the Delaware courts review challenges to mergers and other fundamental transactions, they generally apply the business judgement rule.[517] This rule is found to give a high degree of deference to the decisions of directors who are not conflicted and who are acting in good faith and with due care. However, if there is conflict of interest or bad faith, courts will tend to apply the more stringent entire fairness standard of review.[518]

Secondly, Davids submitted that the potential cost of the proceedings could be a deterrent to dissenting shareholders even if the 15% threshold is met and the company in question is required to initiate review and bear most of the costs. This is because this remedy is only available to shareholders who initially voted against the adopted resolution and not shareholders who did not vote against the resolution for one reason or another. For example, preference shareholders might not have had voting rights for a particular proposed fundamental transaction.[519]

[515] Section 115(3) (b) of the Act.
[516] Davids *et al supra* n276 at 359.
[517] As was held in the case of *Gimbel v Signal Cos*, 316 A2d 599 (Del Ch 1974), *Aronson v Lewis*, 473 A2d 805 (Del 1984), *Smith v Van Gorkom*, 488 A2d 858 (Del 1985).
[518] Davids *et al supra* n276 at 359.
[519] *Ibid*.

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According to what has been discussed above, the approach in the USA is rather different from that in South Africa in respect of minority shareholder protective measures under a statutory merger. In South Africa, as described above, there are court approval provisions and appraisal rights, whereas in the USA the main recourse is appraisal rights.[520] In protecting minority shareholders these appraisal rights apply a different approach from the one provided under the court approval provisions in the South Africa jurisdiction. Cassim submitted that the statutory merger could easily be effected without hurdles, simply with the approval of the prescribed majority as per each company's MOI and without the need for any court approval. All things considered, instead of recourse to a court, a dissenting shareholder has the right to opt out by withdrawing the fair value of his shares in cash. This is done by way of an appraisal rights exercise.[521] She further submitted that this measure provides a balance between the protection of minority shareholders and the decisions of the majority shareholders in restructuring businesses.[522] Even so, the 2008 Act provides for appraisal rights, but this is not the only option for dissenting shareholders and leaves the minority shareholders with choices. One of these choices is the main focus in this section; it is a measure that frustrates a merger and will be highlighted below.

3.3.3 Observations and submissions

It is submitted that the court approval provisions in respect of fundamental transactions can prove to be a problem in a company having a successful fundamental transaction proposal. The statutory merger provision in the South African jurisdiction came into being as a result of aligning the South African jurisdiction with the best international best practices.[523] It was influenced by the US style of merging companies, as indicated in paragraph 3.3.2.3 On *the merger and amalgamations provisions*, above. However, in the very jurisdiction from which this statutory merger was adopted, the court approval provision does not apply. This is possibly a result of not wanting to burden

[520] Of course South African jurisdiction has both appraisal rights and court approval provisions, but for the purpose of this research and especially this chapter, we focus on the South African court approval provisions frustrating the approval of a merger. In the USA, they have noted this and have only appraisal rights that consider the interests of all shareholders. This is in light of the fact that the minority shareholders are afforded protection by being given a way out if they do not want to be part of the proposed merger. Also, the majority shareholders are given approval for their proposal of a merger. This will be highlighted in para 3.3 Court approval provisions, to follow.
[521] Cassim *supra* n393 at 1.
[522] *Ibid.*
[523] This was highlighted in para 1.1.3 of Chapter 1 above.

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the procedure and make it questionable as a favourable business restructuring mechanism in the corporate sector, as it is most likely to lead to the abandonment of fundamental transactions by companies.

The court approval provision makes shareholder approval seem like a rubber-stamping exercise because the 2008 Act provides that

> "despite a resolution having been adopted as contemplated in subsection (2) (a) and (b), a company may not proceed to implement that resolution without the approval of a court if … the resolution was opposed by at least 15% of the voting rights that were exercised on the resolution and, within five business days after the vote, any person who voted against the resolution requires the company to seek court approval ..."[524]

This is based on the fact that a small number from the majority of shareholders voted against the proposed transaction, whereas measures such as resolutions are meant to resolve the differences of shareholders in a company by way of majority rule and assist its members in reaching one decision by which all members will abide. Moreover, the provision makes an unreasonable assumption and renders the adoption of the resolution questionable by stating that a company may not continue to implement an adopted resolution without the approval of court if 15% of the voting rights were against the resolution.

Furthermore, the 2008 Act provides that for a special resolution to be approved by shareholders of a company the resolution needs to be supported by at least 75% of the voting rights exercised on it.[525] It continues by providing that a company's MOI may stipulate a different percentage of voting rights from the 75% default in order to approve a special resolution.[526] This allows shareholders of a company to make a special resolution easier to approve by providing for a lower percentage of voting rights. For the purposes of this research, shareholders may provide for a lower percentage for the approval of a special resolution in the company's MOI with the objective of making things easier for themselves in adopting a resolution that is in favour of a fundamental transaction, considering the fact that section 115 requires a

[524] Section 115(3) (a) of the Act.
[525] Section 65(9) of the Act.
[526] Section 65(10)(a) of the Act.

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special resolution rather than an ordinary resolution for the approval of a fundamental transaction. However, the provisions of court approval under section 115 undermine this part of the 2008 Act, which empowers shareholders as discussed above to make things easier for themselves in adopting resolutions. The fact that a mere 15% having a different view can bring the resolution into question, as indicated in the above paragraph, poses challenges to processes that shareholders may have created for themselves since the 2008 Act allows them to do so.

The submissions are in consideration of the fact that the court approval provisions are enacted for the protection of minority shareholders but as they currently stand, they disadvantage the rights of the majority and a balance should be effected. This is because they can force the majority to abandon proposed transactions instead of finding a way out for dissenting shareholders, such as the appraisal remedy.[527] Especially if a company wants to enter into a time-constrained transaction, a dissenting shareholder may utilise the provision to delay the implementation of the transaction as per the adopted resolution, since court proceedings can take time. In addition, court approval comes with legal costs.[528] This in itself leads to the facilitation and allocation of financial resources into wrong places, such as litigation as opposed to the proposed transaction, especially if the transaction was to be used as a takeover mechanism. This can result in the company being out of pocket and unable to continue with the proposed transaction.

A similar instance would be where the company decides to abandon a proposed fundamental transaction simply because the profits that would come from the proposed transaction are close to if not above the costs of litigation in obtaining court approval. This argument is similar to one that was raised in the USA against litigation and takeovers, that a bidder will be expected to abandon a takeover bid if during litigation its expected returns from the eventual takeover will not justify the marginal costs of continued litigation. This could occur in an instance where the target company reveals unexpected legal powers and imposes direct legal costs on the acquiring

[527] The appraisal remedy forms part of this research and will be discussed in detail in CHAPTER 4.
[528] Section 115(5)(a) of the Act.

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company, causing the acquiring company to drop out in order to avoid future legal costs.[529]

In the USA it is also known that defensive litigation is common when takeover bids are contested and that commencing such litigation merely serves two purposes. Firstly, it causes delay in the bid process so that the board of the target company can think of other defensive measures or obtain other bidders. Secondly, it causes delay and depending on the nature and merits of the case, could thus halt the bid altogether.[530] This second reason is similar to the argument raised above in terms of court approval in the 2008 Act, in that a dissenting shareholder may bring an adopted resolution before court with the intention to cause delay in order to halt the adopted resolution.

Apart from a balance between majority and minority shareholders' interests being achieved under section 115 as suggested above, the interests of minority shareholders can be accommodated under the provisions of section 163 of the 2008 Act. This is because the court approval provisions are similar but not the same as the oppression remedy provided under section 163 of the 2008 Act. Under section 115(7) of the 2008 Act it is stated that a court, when reviewing an adopted resolution that is based on an application by one or more of the shareholders of a company, and having granted leave, may set aside an adopted resolution on certain grounds.

The first ground is if the adopted resolution was manifestly unfair to a class of shareholders in the company.[531] Turning to section 163 of the 2008 Act, it is stated that a shareholder may apply to the court for relief, if an act of the company has had a result that unfairly disregards the interests of the applicant, who may be a shareholder in a certain class of shareholders in the company.[532] These grounds are similar and if there should be a need for their interpretation by a court, it is believed they would be interpreted as meaning the same thing. Furthermore, just on this one similar ground, a shareholder may bring an application to court because a shareholder merely has to prove one ground rather than two under the provisions of the court approval, since section 115(7)(a) and section 115(7)(b) are separated by "or", not

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[529] Jarrell "The Wealth Effects of Litigation by Targets: Do Interests Diverge in a Merge" (1985) *Journal of Law and Economics* 151-177 at 159.
[530] Kershaw "The Illusion of Importance: Reconsidering the UK's Takeover Defence Prohibition" (2007) *International and Comparative Law Quarterly* 267- 307 at 279.
[531] Section 115(7)(a) of the Act.
[532] Section 163(1)(a) of the Act.

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"and". Significantly, under the provisions of section 163 of the 2008 Act, the shareholder does not need to have voted against the adopted resolution as required under the provisions of section 115, which makes the protection provided under section 163 even better.

As a second ground the court approval provisions refer to the voting being conflicted, inadequate disclosure, failure to comply with the company's MOI or other significant procedural irregularity.[533] These cases are accommodated under the provisions of section 163, as these acts may prove to be oppressive and unfairly prejudicial towards any shareholder in a company, for which section 163 provides. It is also noted that other jurisdictions that have been chosen for this research do not have court approval provisions in respect of fundamental transactions; the South Africa jurisdiction it is the only jurisdiction that has these provisions. Rather, these other jurisdictions have provisions that allow them to approach a court with similar provisions as indicated under section 163 of the 2008 Act, including court approval provisions.

Davids submitted that the provisions under section 163 of the 2008 Act offer a far better remedy and are more useful than the provisions under the court approval remedy. This view was based on the fact that the provisions under section 163 could be used by any shareholder rather than only shareholders who had voted against the adopted resolution, as required by the provisions under the court approval measure.[534] Also, the provisions under section 163 were found to have been providing broader grounds for the court to intervene rather than the provisions under the court approval measure, which only allowed the court to set aside an adopted resolution on the basis of manifest unfairness or material procedural irregularity.[535] Furthermore, the provisions under section 163 provided the court with a broad range of remedial powers. These powers included the varying or setting aside of a transaction or any transaction to which a company is party and compensating any party to the transaction or agreement in question[536] and ordering the payment of compensation to any aggrieved party subject to any other provisions in law that entitle that party to compensation.[537] It may make any order for the trial of an issue it may determine as

[533] Section 115 (7)(b) of the Act.
[534] Davids *et al supra* n276 at 363.
[535] Section 115(7) of the Act.
[536] Section 163(2) (h) of the Act.
[537] Section 163(2) (j) of the Act.

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court.[538] The provisions in section 163 may provide a way out for a dissenting shareholder while not forcing a company to abandon a proposed fundamental transaction. As indicated above, court approval provisions have the potential to force the majority to abandon proposed transactions instead of offering a way out for dissenting shareholders, such as the appraisal remedy.

It has also been held that a party may not be able to have an adopted resolution set aside under the provisions of section 163, as under section 115(7) of the 2008 Act it is stated that court may only set aside an adopted resolution on the grounds provided in that section.[539] However, it is submitted that this is not the case, because as indicated and highlighted above, court approval provisions are similar to the provisions falling under section 163 of the 2008 Act. It was also submitted by Davids that in as much as the provisions under section 115(7) of the 2008 Act are better interpreted as applying only in the context of reviewing a fundamental transaction initiated in terms of provisions under section 115(5) or (6) of the 2008 Act, it is arguable that it cannot be read as limiting the court's remedial powers under section 163 of the 2008 Act.[540]

He further submitted that the provisions under section 163 of the 2008 Act are just like any other court procedure and have the disadvantages of being costly and time-consuming, as indicated above. He stated that as much as the provisions of court approval entail the advantages and disadvantages of court procedures, they at least imply that the company that is required to seek court approval bears the costs of obtaining court approval and not the shareholder who requires the company to obtain such approval.[541] This in light of the fact that section 115 of the 2008 Act provides that when 15% of the voting rights have voted against the adopted resolution, the company concerned may be required by a shareholder to seek court approval for the resolution. This means that the company concerned has to make an application to court seeking approval for the adopted resolution as opposed to the shareholder relying on these provisions.

It is also noted that the other jurisdictions chosen for this research do not have the court approval provisions indicated in section 115 of the 2008 Act in respect of

[538] Section 163(2) (l) of the Act.
[539] Cassim *supra* n277 at 173.
[540] Davids *et al supra* n276 at 363.
[541] *Ibid.*

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fundamental transactions. These may be utilised against a company to approach court for the approval of an adopted resolution in respect of a fundamental transaction. In the USA, the appraisal right serves as a pre-court measure, since a dissenting shareholder is given an opportunity to exit the company and get the fair value of his shares in the company.[542] This procedure is followed rather than blocking the adopted resolution that is in favour of a fundamental transaction, like the court approval provisions in the 2008 Act. The company will make an offer for the value of his shares and if the shareholder is not satisfied, he may ask for a better offer.[543] Only when the shareholder is not satisfied with the offered value for his shares may he approach a court of law about such an unfair valuation.[544]

The appraisal rights are an attempt to remedy the situation before it reaches the court, unlike the court provisions under section 115 of the 2008 Act. Even so, the appraisal rights do not block the adopted resolution that is in favour of the fundamental transaction. The issue is the fair market value of the dissenting shareholders' shares.[545] In South Africa this remedy does not serve as a pre-court method as it serves in the USA as shown above in situations where the minority shareholders are not in agreement with the majority in a company. Rather, in South Africa this remedy serves as one of the alternatives a shareholder may use when not in agreement with an adopted resolution. Nevertheless, its initial purpose following its enactment was for the South African jurisdiction to attain an appropriate balance of interests of all the shareholders in a company by avoiding either minority oppression by the majority or minority dictation that can prevent improved management in a company that may result from a merger.[546] This provision will be discussed in detail in the chapter to follow.

3.4 Conclusion

In as much as shareholder protection tends to encourage investment at the right level by preserving the integrity of the market, which in turn enhances shareholders' willingness to invest in equity, it can also deter potential bidders, which in this case are

[542] Section 13.02 of the Model Business Corporation Act.
[543] Section 13.24 of the Model Business Corporation Act.
[544] Section 13.26 of the Model Business Corporation Act.
[545] It should be noted that the appraisal remedy will be discussed in detail in CHAPTER 4 of this research.
[546] Cassim *supra* n393 at 22.

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investors, if takeover regulations overemphasise the protection of shareholders by making takeovers burdensome, expensive and inefficient.[547] Therefore, the South African jurisdiction needs to provide for a level of shareholder protection that encourages investment rather than protection that deters investment. It is realised that the greater the protection of a company's shareholders, the weaker the chances of a company's fundamental transaction proposal success. This calls for the South African jurisdiction to ensure a balance between the shareholder protection rules and the fundamental transaction rules. The level of protection from each jurisdiction will obviously vary and this will depend on that jurisdiction's constitution for the markets and expectations of each country's market users, as highlighted in paragraph 2.5 Conclusion. [548]

It should also be noted that this research does not imply that one should do away with the shareholder and court approval requisites for all fundamental transactions. It is simply examining whether it is necessary for shareholders to vote in all circumstances and whether the court approval measure should serve as one of the first available options for a solution when a shareholder is in disagreement with an adopted resolution, as opposed to a pre-court measure such as the appraisal remedy. This is necessary, since it can be inferred from the above that the shareholder and court approval provisions as they currently stand have the potential of frustrating the realisation of fundamental transactions at times.

From the above it is evident that shareholder approval provisions in South African corporate law are a result of replication of English law and that they now apply to the approval of fundamental transactions, which affects the alteration of all shareholders' investment in a company. The rationale is that shareholders of a company should have an opinion on what happens to their investment. These rights now apply to all fundamental transactions in the 2008 Act. This position was compared to other jurisdictions chosen for this research and different results were found.

The shareholder approval processes in all selected jurisdictions for this research were found to be different from one another when an analysis was done to find the delay in each process. It was found that in other jurisdictions there was less delay in the

[547] Boardman *supra* n231 at 312.
[548] *Ibid.*

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processes. However, it was found that in some jurisdictions some processes created delay, which could have adverse consequences. For the purpose of this research this substantiated the fact that the South African shareholder approval process as hypothesised can cause delays that can lead to fundamental transactions being frustrated at times. Therefore, it was highlighted that shareholder approval is really not necessary in all fundamental transactions and that exceptions should perhaps be made in certain circumstances, but with certain prerequisites.[549] Substantiating this argument was the fact that in some of the jurisdictions shareholder approval did not apply at all to certain fundamental transactions so as not to affect the ease of processes, especially where that is in the best interest of the company.

In the analysis it was found that these shareholder approval processes had thresholds where a certain percentage of votes among the shareholders of a company needed to be in favour of a proposed transaction to allow its implementation. The higher the threshold, the more difficult it became for a fundamental transaction to be approved, which could result in the frustration of the realisation of the fundamental transaction. It was found that in South African jurisdiction, the high threshold in the Act was a result of increasing minority shareholder protection. It was further highlighted that the South African threshold, when compared to other jurisdictions, was very high, irrespective of the fact that it could be altered to a lower threshold. It was likewise substantiated that the other jurisdictions did not have a high threshold because legislators were probably aware of the fact that this could easily become a burden that could make it difficult for a fundamental transaction resolution to be adopted. It became evident that the other jurisdictions considered for this research have shareholder approval provisions that do not ordinarily apply resolution thresholds under certain fundamental transactions. Conversely, these only applied in circumstances where the interests of shareholders were going to be altered significantly.

Furthermore, it can be inferred from the above that court approval provisions existed as minority shareholder protection if the shareholder approval protection measures in place were insufficient for a dissenting shareholder to rely on them. It was highlighted that the court approval provision under fundamental transactions is a uniquely South Africa provision that is not found in the takeover regulations of other jurisdictions. This

[549] Recommendations are to be discussed in detail in Chapter 5.

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was to stress that the South African provisions are unique and have no counterpart in any other jurisdiction, especially those chosen for this research.

It was indicated that court approval provisions have the potential to frustrate a fundamental transaction, since these provisions lead to litigation, which can cause delay and frustrate a time-constrained transaction. Considering the amount of time it takes to bring a matter before a court and to deliberate the matter in court, as well as the postponements before an order is made, it was also highlighted that these provisions can lead to litigation costs. These may use up the money that was budgeted for the proposed fundamental transaction, forcing the company to abandon the proposed transaction. These provisions are also codified in such a manner that they serve as a next step for a dissenting shareholder who is not in agreement with the majority and can force the company to bear the costs of court approval.

The above was compared with other jurisdictions and it was found that in the USA there is a remedy that deals with the difference of opinion on a fundamental transaction and at the same time balances the interests of majority and minority shareholders. This method is court-free and allows the majority shareholders to continue with a fundamental transaction and the dissenting minority to get a fair market value for their shares if they do not want to form part of the company anymore. Only when there is disagreement on the fair market value of shares may a court interfere, but not in the approval of a fundamental transaction. This method is available in the South African jurisdiction and is discussed in detail in the chapter to follow.

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CHAPTER 4

Dissenting shareholders

4.1 Introduction

The purpose of this chapter is further exploration of one of the main issues explored in CHAPTER 3, which is to highlight that shareholder protection provisions in the 2008 Act in relation to fundamental transactions frustrate the realisation of the fundamental transaction proposals.[550] This chapter analyses appraisal rights in relation to fundamental transactions. Furthermore, this chapter will briefly analyse shareholder protection that was available before the introduction of the right to appraise. This will be done with the intention of exploring whether the rules that applied prior to the appraisal remedy frustrated the realisation of fundamental transactions or not, as well as to establish whether or not the right to appraise was a step in the right direction.

4.2 Appraisal rights

4.2.1 Origins

In South Africa the provisions of appraisal rights were adopted for the first time in the 2008 Act.[551] There were no appraisal right provisions in the 1973 Act. For more than a century, company law in South Africa was firmly rooted in the laws of the UK, as discussed in Chapter 2, in the pivotal principle of majority rule.[552] Furthermore, the body of South African common law displays clear traces of Roman-Dutch law[553], specifically the 1973 Act. In addition, the company law judgments of South African courts have always drawn heavily on and relied on UK legal principles.[554] The

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[550] See 1.4 Purpose of the research and methodology, above.
[551] Yeats "Putting Appraisal Rights into Perspective" (2014) *Stellenbosch Law Review* 328-360 at 328.
[552] Beukes "An Introduction to the Appraisal Remedy as Proposed in the Companies Bill: Triggering Actions and the Differences between the Appraisal Remedy and Existing Shareholder Remedies" (2008) *South African Mercantile Law Journal* 479–495 at 495.
[553] Lee "Roman-Dutch Law in South Africa" *The Law Quarterly Review* 61-75 at 62 (1924).
[554] *Ibid.*

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appraisal rights in the 2008 Act originated from and were developed in the USA and have been on that country's statute books for more than a century.[555]

In the USA, the first appraisal rights were granted to shareholders of a company by statutory provisions at the end of the 19th century simultaneously with general provisions that regulated companies.[556] However, before the enactment of provisions that regulated companies in the USA, the common law rule that applied in most of the states was the requirement of unanimous consent of all the shareholders of a company.[557] This also applied in circumstances where one company wanted to consolidate or merge with another company.[558]

Shareholders' rights to consolidate or merge or even dispose of the assets of a company or to amend a charter were protected by courts.[559] The protection these courts offered minority shareholders was indistinguishable from what the appraisal rights catered for. In instances where a company was merging or entering into consolidation or was even selling its assets by a simple majority approval of shareholders, the minority shareholders who were against these transactions were entitled to sue a company for payment of the fair value of their shares. Another option

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[555] Allen and Kraakman *supra* n378 at 427-429. Cassim *supra* n393 at 19.
[556] Wertheimer "The Shareholders Appraisal Remedy and How Court Determines Fair Value" (1998) *Duke Law Review* 613-716 at 618. Carney "Fundamental Corporate Changes, Minority Shareholders and Business Purposes" (1980) *American Bar Foundation Research Journal* 69-132 at 77.
[557] *Ibid.*
[558] *Idem* at 619. He points out that there was no flexibility in respect of consolidations and mergers and that there was a possibility of minority shareholders being bound by a decision of the majority. Also, in the case of *Chicago Corp. v Munds* 172 A.452, 455 (Del. Ch.1934) it was observed that at common law power was vested in any single shareholder to prevent a company from proceeding with a merger. When the idea became accepted that in the interest of adjusting corporate mechanisms to the requirements of business and commercial growth, mergers were allowed irrespective of minority opposition. Also, statutes were enacted in many states that took the power from the single shareholder to prevent a company from merging with another. However, the loss of the right in respect of the single dissenting shareholder was compensated for by giving him the option to retire completely from the company and receive a fair value of his shares in money.
[559] Siegel "Back to the Future: Appraisal Rights in the Twenty-First Century" (1995) *Harvard Journal* 79-144 at 86. In the case of *Mason v Pewabic Mining Co.*, 133 U.S.50, 58 (1980) the court made a decision that bound the minority shareholders of a company by forcing this minority to become shareholders of a new company by sale of assets for shares. However, this was a subsequent turn from cases such as *Treat v Hubbard-Elliott Copper Co.*, 4 Alas. 497 (Dist. Ct. 1912), a case which had to do with the sale of assets, McCray v Junction R.R., 9 Ind. 358 (1857), which had to do with consolidation, *Stevens v Ruthland & B.R.R.*, 29 Vt. 545 (Ch. Chittenden County 1851), which had to do with a charter amendment, *Tanner v LLindell Ry.*, 180 Mo.1, 79 S.W. 155 (1904), which had to do with consolidation, *Lange v Reservation Mining & Smelting Co.*, 48 Wash. 167, 93 P.208 (1908), which dealt with asset sale, and *Theis v Spokane Falls Gaslight Co.*, 34 Wash. 23, 74P. 1004 (1904). In these cases the courts relieved minority shareholders from companies that were attempting to make changes to a company without the required unanimous consent of shareholders.

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was to bring an action before a court, pleading that the proposed transaction be set aside.[560]

Therefore, with the introduction of appraisal rights the requirement of unanimous consent was replaced by the rule prescribing that minority shareholders had the right to leave a company when in disagreement with the decisions that were made by the majority and to give back the company's shares in return for their fair market value.[561] The end of the 19th century was a time when the industrial revolution took place and companies needed to adapt to market changes. Unanimous consent became an obstacle for all companies that wanted to change so they could grow, since under the unanimity requirement any shareholder in a company was able to block changes from which a company could benefit.[562]

Appraisal rights were at first not easily accepted; in 1909 only five states in the USA provided for appraisal rights, while the rest still operated under the majority voting rule in respect of mergers and consolidations. However, these rights were accepted across the USA between the second and third decades of the 20th century.[563] Since then, there have been some theories concerning their purpose and role. The first theory that supported the traditional point of view was that appraisal rights offered protection for both minority and majority shareholders. The majority were not prevented from introducing changes to the company and from making decisions that were considered an advantage to the company and the minority were not forced to remain in the company that had become different from the company they were involved in before.[564]

[560] Lattin "Remedies of Dissenting Stockholders under the Appraisal Statutes" (1931) *Harvard Law Review* 233-270 at 234. In some cases the court awarded a resolution similar to the appraisal right: *Tanner v Lindell Ry*., 180 Mo. 1, 79 S.W.115 (1904), *Wunsch v Consolidated Laundry Co., 116 Wash*. 44, 198 Pac. 383 (1921), *Kremer v Public Drug Co*., 41 S. D. 365, 170 N. W. 571 (1919), *Kaszubowski v Buffalo Telegram Corp*., 131 Misc. 563, 570, 227 N.Y. Supp. 435, 441 (1928), which had to do with the sale of the company's assets. After an application by a minority shareholder against the company, the court held that the assets be returned, as well as the purchase price and that the parties be placed in the status quo. Similarly, in the case of *Garret v Reid-Cashion Land & Cattle Co*., 24 Ariz. 45, 274, 270 Pac. 1044, 1054 (1928) it was held that the transfer of assets was an unlawful act that entitled the minority shareholder to legal interest from such time.

[561] Thompson "Exit, Liquidity and Majority Rule: Appraisal's Role in Corporate Law" (1996) *Georgia Law Journal* 1-60 at 11. Hagan "First Western Bank Wall v Olsen: An Interpretation of Fair Value for Minority Shares as found within the South Dakota Dissenters Rights Statutes" (2003) *South Dakota Law Review* 83-103 at 89-90.

[562] *Ibid* at 13. Balotti and Finkelstein *The Delaware Law of Corporations and Business Organisations* (2009) (Aspen publishers, New York) 10-115.

[563] *Ibid* at 14.

[564] Levy "Rights of Dissenting Shareholders to Appraisal and Payment" (1930) *Cornell Law Review* 420-444 at 421. Lattin *The Law of Corporations* (1971) (Foundation Press, Brooklyn) at 591.

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Appraisal rights from the above point of view are viewed as a relief in favour of all dissenting shareholders who are no longer able to block the will of the majority or rather to prevent the majority from upholding decisions, and are seen as a substitute of the minority shareholders' previous right to veto the majority shareholders' decisions.[565] The right to payment is regarded as an option that lets a company continue with a new venture, without necessarily regarding the payment as validating the company's actions or rendering the actions constitutional.[566]

The above approach to the role of appraisal rights was confirmed in the comments to the Uniform Business Corporation Act of 1928. This Act stated that the majority are under an obligation to carry out the policies that seem to be in the best interest of the company. Nevertheless, the minority have a right not to have to bear the consequences of the majority's adoption of unexpected measures.[567] This approach was supported by the courts, which held that minority shareholders had a right to separate from a company with which they no longer agreed in terms of the direction or decisions taken by the majority.[568]

Notwithstanding this, the modern justification of the right to appraise is that it serves as protection for minority shareholders against being paid out at an inadequate price of value.[569] This is regarded as the "remedy for unfairness" justification,[570] since the directors of the company, rather than its shareholders, are the ones who negotiate the terms of the merger and the directors could easily disregard their duty to obtain the best price for the company.[571]

The above may occur especially in instances where directors are tempted by various side payments offered as an inducement to them personally by the other merging company. The shareholders of the company may never become aware of such side payments, making the safeguarding of shareholder approval of the merger an

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[565] Kanda "The Appraisal right and the Goal of Corporate Law" (1985) *University of California at Los Angeles Law Review* 429-473 at 430-434. Letsou "The Role of The Appraisal in Corporate Law" (1998) *Boston College Law Review* 1121-1174 at 1121.
[566] Levy *supra* n564 at 427.
[567] Thompson *supra* n561 at 19.
[568] *Cole v National Cash Credit Ass'n*, 156 A. 183, 187 (Del. Ch. 1931), *Johnson v Baldwin*, 69 S.E.2d 585, 591 (S.C. 1952).
[569] Pinto and Branson *Understanding Corporate Law* (1999) (LexisNexis, New York) at 127-128. Also Allen and Kraakman *supra* n378 at 452-453. Also, Hamilton *The Law of Corporations in a Nutshell* (2000) (West Academic Publishing, Minnesota) at 628.
[570] Clark *Corporate Law* (1986) (Aspen Publishers, New York) at 445.
[571] *Ibid.*

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ineffective measure on its own. This is because of the possibility of inadequate information disclosure by directors to shareholders and possible shareholder apathy.[572] Therefore, the right to appraise, apart from the discussed perspective above, also serves as a check on poor business judgements by directors, because the greater the number of dissenting shareholders, the more likely it is that the board would be persuaded to reconsider its stance regarding a merger.[573]

Therefore, there are several justifications that serve as reasons for the appraisal remedy.[574] However, for the purpose of this research there are two relevant justifications for the adoption of the appraisal remedy. The first is that the remedy balances the right of the majority shareholders to be able to proceed with making changes in a company by any proposed fundamental transaction, even though the minority shareholders are not in agreement. The second is that it protects the minority shareholders against being involuntarily dragged along in a fundamental transaction adopted by the majority shareholders with which they disagree.[575]

4.2.2 Nature and effect of the provision

It is a known fact that the affairs of the company are decided upon by the votes of the majority shareholders in a company. However, even though matters have been decided upon in this manner for a long time, this has disadvantages for minority

[572] Cassim *infra* n277 at 158.

[573] Eisenberg "The Legal Roles of Shareholders and Management in Modern Corporate Decision Making" (1969) *California Law Review* 1-181 at 85-86. Also, Kanda and Levmore "The Appraisal Remedy and The Goals of Corporate Law" (1985) *University of California in Los Angeles Law Review* 429-473 at 436-442 provides that appraisal rights should be able to assist shareholders to prevent and uncover wrongful behaviour of management of a company and that such wrong behaviour by the management of the company may be magnified especially when a company undergoes some fundamental transactions or rather fundamental changes. That is because instead of management negotiating in the best interest of the company and its shareholders, it would be tempted to accept deals that are less attractive as such but more attractive to the management, for example if these have to do with remuneration or other incentives. Therefore, in certain instances shareholders are concerned about the legitimacy of a transaction or a change and the real motivations of management for taking these actions. Also, Clark *supra* n570 at 445.

[574] The justification for the appraisal remedy is to compensate the minority shareholders for their loss of veto power in the company, to enable the majority shareholders to carry out proposed fundamental transactions and at the same time enable a cash exit by the minority shareholders from the company instead of them being dragged into such transactions against their will. Hagan "First Western Bank Wall v Olsen: An interpretation of Fair Value for Minority Shares as Found within the South Dakota Dissenter's Rights Statutes" (2003) *South Dakota Law Review* 83 at 89-90.

[575] Eisenberg *Cases and Materials on Corporations* (1988) (Foundation Press, New York) at 1104.

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shareholders,[576] in the sense that they may be compelled to abide by the decisions of the majority, even if they hold a different opinion.

The obvious solution for these dissenting shareholders, if they do not want to abide by the decision of the majority, would normally be to sell their shares, but usually there is no ready market.[577] However, in some jurisdictions, such as the USA, as indicated in the above paragraph 4.2.1 Origins, through appraisal rights[578] minority shareholders are given an option to be bought out by their company, should they disagree with the decision of the majority on approving one or more of the fundamental transactions.

Following the lead of jurisdictions such as the USA, as indicated in paragraph 4.2.1 Origins, section 164 of the 2008 Act provides for appraisal rights. Solely for the purpose of this study, the focus will be on the trigger of the appraisal rights when a company gives notice to all its shareholders on a meeting to consider adopting a fundamental transaction.[579] In the USA, for those states that apply DGCL, it provides for appraisal rights under section 262 and these are triggered when a company proposes a merger.

Therefore, it means that these rights are triggered when an action that may have a profound effect on the company and its shareholders is taken. This also constitutes an implied acknowledgement of the significant consequences of these transactions for shareholders in view of the fact that both the nature of their rights and the nature of the company have the potential of being changed as a result.[580]

4.2.2.1 On the scheme of arrangement

As indicated above, in South Africa appraisal rights apply to fundamental transactions and these include the scheme of arrangement.[581] However, appraisal rights need to be properly executed and this means that a shareholder needs to complete a number of formal procedural steps within a prescribed time, as will be shown below.

[576] Beukes *supra* n552 at 479.
[577] *Ibid.*
[578] Ch 13 of the Model Business Corporation Act.
[579] Section 164 (2) (b) of the 2008 Act. Yeats *supra* n551 328-360 at 332.
[580] Cassim *et al infra* n277 at 796.
[581] S 164(2) (b) of the 2008 Act.

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4.2.2.1.1 Notice of objection

When a resolution for the scheme of arrangement is about to be voted on, any shareholder may give the company in question a written notice objecting to the resolution. This may happen any time before the voting.[582] If the proposed resolution is adopted, the company must notify this dissenting shareholder of this fact within 10 days,[583] subject to the dissenting shareholder having met all the requirements and procedures set out in the 2008 Act.[584]

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[582] Section 164 (3) of the 2008 Act.

[583] Section 164 (4) of the 2008 Act.

[584] Examples of South African cases that had to do with the procedure of appraisal rights: In the case of *Loest v Gendac (Pty) Ltd and Another* 2017 (4) SA 187 (GP) the applicant wanted access to information on the respondent companies. The information that the applicant wanted had to do with the bank accounts and contracts entered into by the respondent companies. The applicant relied on appraisal rights, arguing that for a determination of the fair market value of his shares he needed access to the respondent's bank accounts and contracts entered into. This was after the applicant had received a notification for conversion of shares in the respondent companies to which the applicant objected and exercised his appraisal rights. He was offered R250 000 for his shares, which he refused. However, in this matter the court held that the applicant had not established a basis explaining why the information was required for the exercise of his appraisal rights. It held that the court that has to determine the fair value of those shares is the court that is enabled to determine whether or not access to stipulated information is required in order to exercise appraisal rights. In the case of *Cilliers v LA Concorde Holdings Limited and Others 2018 (6) SA 97 (WCC)* the court was required to determine whether or not appraisal rights in regard to the minority shareholders in a holding company were established where a subsidiary of the holding company was disposing of all or a greater part of the subsidiary's assets or undertaking. The court held that the minority shareholders had a right to be treated fairly and the appraisal provisions provided just that. It held that should the dissenting shareholders choose to exit the company in the context of appraisal provisions, they too had a right to be paid a fair value for their shares and that treating these shareholders any different would be undermining the purpose of the appraisal right as a protection measure. It held that minority shareholders in a holding company can exercise appraisal rights in regard to a subsidiary of the holding company. In the case of *Standard Bank Nominees (RF) (Proprietary) Limited and Others v Hospitality Property Fund Limited* 2020 (5) SA 224 (GJ) Standard Bank Nominees and others (SB) were registered shareholders of Hospitality Property Fund (HPF) until July 20015. On July 2015 HPF gave notice to all its shareholders of a meeting on a resolution for a scheme of arrangement. This resolution triggered appraisal rights and HPF received a proxy for voting in the meeting in favour of Fund Advisors (FA) by SB. In August 2018 FA voted against the resolution and later demanded a fair value of shares in HPF, supposedly held by SB and others. HPF made an offer, which the FA rejected. The FA made an application to court in terms of S.164 (14) of the 2008 Act for the determination of a fair market value for its shares in HPF 30 days after the offer was made. Affidavits between the two parties were exchanged regarding the locus standi of FA. HPF made distributions and excluded SB and others, since in terms of S.164 they were only entitled to the fair value of their shares. The court held that the requisite notice and demand and prerequisite steps of the appraisal right had not been taken and that there was no valid enforcement of the right. It held that SB and others were supposed to institute an application to court within 30 days of an offer being made by HPF if not satisfied, but had failed to do so and they thus lost their right of appraisal. In the case of *Justpoint Nominees (Pty) Ltd and Others v Sovereign Food Investments Limited and Others (BNS Nominees (Pty) Ltd and Others Intervening) [2016] ZAECPEHC 15* Justpoint Nominees (JN) were shareholders in Sovereign Foods (SF) and SF proposed a scheme of arrangement between itself and its shareholders, enabling it to repurchase its own shares. JN expressed unhappiness and sent a demand in terms of section 164(6) of the 2008 Act to be paid a fair value of its shares to exit the company. SF in the transaction documents sent to all shareholders had indicated that should 5% or more of its shareholders object to this transaction, it would not be implemented unless it waived this condition within 25 days of notice being sent to shareholders. BNS Nominees, also holders of shares

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4.2.2.1.2 Notice of demand

The dissenting shareholder may proceed and demand from the company in question that he be paid a fair market value of the shares that he holds in the company.[585] He may do this within 20 days after receiving a notice that the proposed resolution has been adopted or if he does not receive the notice he may do so within 20 days after learning of such adoption.[586] This is provided that the dissenting shareholder did send a notice of objection, as stated above, and voted against the resolution.[587] An exception would be where the company in question failed to send out a notice of a meeting or sent out the notice without including a statement stipulating the shareholders' rights.[588] In contradistinction, in the USA in those states that utilise the Model Business Corporation Act, the notice to demand payment of what constitutes a fair market value of a shareholder's shares needs to be issued within 10 days from the date when the company's proposal of the share exchange became effective.[589]

4.2.2.1.3 Demand withdrawal

In the 2008 Act, when the dissenting shareholder has demanded the fair market value of his shares from the company, he will no longer have rights in respect to those shares, except the right to be paid the fair market value of those shares,[590] unless the dissenting shareholder withdraws the demand for the fair market value of his shares before an offer is made by the company in question. If the offer has been made, then the shareholder can allow the offer to lapse.[591] In terms of the 2008 Act the offer can

in SF, objected to the transaction, this amounting to the 5% that would cause the proposed transaction not to be implemented. SF had failed to waive this condition within the 25 days of notices being sent to shareholders. SF revised a new transaction, which intended to repurchase 5% of its shares, making the transaction not subject to appraisal rights and excluding dissenting shareholders from voting, since they had exercised the appraisal rights in the initial transaction and were only entitled to the fair value of their shares. The court held that the shareholders were not prevented from voting on the revised transaction and that the non-waiver of a condition meant that the transaction had failed and could consequently not be used to rely on section 164(9) of the 2008 Act in order to deny shareholders their right to vote on a separate transaction unless they withdrew their appraisal rights.

[585] Section 164 (5) of the 2008 Act.

[586] Section 164 (7) of the 2008 Act.

[587] Section 164 (5) of the 2008 Act.

[588] Section 164 (6) of the 2008 Act.

[589] Section 13.22 (b) of the Model Business Corporation Act. This comparison does not indicate that there is a scheme of arrangement in the USA. However, in as much as there is no scheme of arrangement in the USA, there is share exchange, which is under the provisions of a scheme of arrangement in South Africa and appraisal rights are applicable to both. See section 114(1)(d) of the 2008 Act and section 11.03 of the Model Business Corporation Act.

[590] Section 164 (9) of the 2008 Act.

[591] Section 164 (9) (a) of the 2008 Act.

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lapse if not accepted within 30 days after it was made.[592] Another circumstance is if the company itself fails to make the offer compelled by certain practical circumstances, which will be discussed below in paragraph 4.2.3 Observations and and the dissenting shareholder withdrawing the demand.[593] This may result in the company adopting another resolution that revokes the adopted resolution in favour of a fundamental transaction that gave rise to the dissenting shareholders' appraisal rights.[594] For those states under the Model Business Corporation Act, the dissenting shareholder has a right to withdraw the appraisal demand, but may only do so within 20 days.[595]

4.2.2.1.4 Written offer made by the company

Notwithstanding the above, in the South African jurisdiction, if there is no demand withdrawal in any of the given circumstances above, the company must send each of the dissenting shareholders a written offer for his or her shares. This should be done within five days, with an offer that the company's directors regard as the fair market value for each dissenting shareholder's shares.[596] The offer should also be fair in the sense that shares of the same class or series are based on the same terms and conditions.[597] Should the dissenting shareholders decide to take up the offer, they must tender their share certificates to the company if their shares are evidenced by certificates.[598] If their shares are not evidenced by certificates, they can transfer their uncertificated shares to the company in terms of section 53 of the 2008 Act.[599] As soon as this has been done, the company must pay these dissenting shareholders the agreed amount within 10 days.

If the dissenting shareholders are not satisfied with the offer that they were made and are of the view that the offer is inadequate or the company failed to make a suitable offer, they may apply to the court for a determination of the fair value of their shares

[592] Section 164 (12) (b) of the 2008 Act.
[593] Section 164 (9) (b) of the 2008 Act. This is a contentious issue and forms part of the arguments raised in para 4.2.3 Observations and submissions, of Chapter 4.
[594] Section 164 (9) (c) of the 2008 Act.
[595] Section 13.22 (b) of the Model Business Corporation Act.
[596] Section 164 (11) of the 2008 Act. In terms of sub-section 16 the offer must further comprise a statement that highlights how the value that is being offered was determined. Moreover, this value should be determined on the date and time on which the company in question adopted the resolution.
[597] Section 164 (12) of the 2008 Act.
[598] Section 164 (13) (a) of the 2008 Act.
[599] Section 164 (13) (a) of the 2008 Act.

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and an order to compel the company to pay the fair value as determined.[600] Under the Model Business Corporation Act the dissenting shareholder needs to notify the company if he is not satisfied with the offer made to him before approaching court and he needs to do this within 30 days from the date of offer. [601] If he does not express his dissatisfaction in writing to the company regarding the offer, he will automatically waive his right to further demand what he deems to be the fair value and will only be entitled to payment of the company's offer.[602]

4.2.2.1.5 Court intervention

In South Africa when shareholders make an application for a court to intervene, the court may require that all the dissenting shareholders who have not accepted an offer from the company be joined as parties and be bound by the decision of the court.[603] The company must notify each of these affected dissenting shareholders of the place and time of the hearing and inform them of their right to participate in these proceedings, as they will bear the consequences of the application.[604] In the USA, after a shareholder has made a demand in writing for payment but the demand remains unsettled, the company in question is obliged in terms of the Model Business Corporation Act to commence court proceedings. This must be done within 60 days from receiving this demand for payment and a petition must be submitted to the court so it can determine the fair value of the shares and the accrued interest.[605] The reason for this is that if the company in question does not commence proceedings within the prescribed 60 days, it will have to pay each shareholder the amount that each of the shareholders demanded in cash, plus interest.[606] This approach is different from what the South African Act provides, as discussed above.

In South Africa, the court determines the fair value of the dissenting shareholders' shares and may even appoint an appraiser to assist in its determination of fair value in respect of the shares concerned. In doing this, it may allow a reasonable interest rate to be payable for the period between the adopted resolution and the date of payment and end with an appropriate order of costs, in consideration of an offer made

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[600] Section 164 (14) of the 2008 Act.
[601] Section 13.26 (a) of the Model Business Corporation Act.
[602] Section 13.26 (b) of the Model Business Corporation Act.
[603] Section 164 (15) (a) of the 2008 Act.
[604] Section 164 (15) (b) of the 2008 Act.
[605] Section 13.30 (a) of the Model Business Corporation Act.
[606] *Ibid.*

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by the company and the determination of the final fair value.[607] This position is similar to that of the Model Business Corporation Act in view of the fact that the court may appoint one or more persons as appraisers to receive evidence and recommend a decision on a fair share value.[608] The court in question will also assess the expenses and fees of experts and counsel for the respective parties in amounts the court finds equitable.[609] This may be against the company in favour of all or any of the shareholders demanding the appraisal, particularly if the court finds that the company in question did not substantially comply with the appraisal steps discussed above.[610] However, a South African court, in so doing, must also make an order that requires the dissenting shareholders to withdraw their demands or tender their shares in return for payment of the amount determined by the company. The court must also make an order that requires the company to pay the determined fair value of shares of each qualifying shareholder.[611]

Another contentious issue for the purposes of this research, which will be discussed in detail under paragraph 4.2.3 Observations and is the fact that a company may be unable to comply with the payment obligated by a court order as discussed above, because it may be unable to pay its debts as they fall due and become payable for the ensuing 12 months.[612] The company may make an application to the court to vary its obligations in these circumstances and the court can make an order that is just and equitable to ensure that the company will pay at the earliest date possible that is compatible with meeting its other financial obligations.[613]

4.2.2.2 On the disposal of all or a greater part of a company's assets

In South Africa the appraisal procedure under the disposal of all or a greater part of the assets of a company or its undertaking applies in the same manner as in the scheme of arrangement discussed above in paragraph 4.2.2.1 On *the scheme of arrangement*. In the USA, for those states that use the Model Business Corporation Act, appraisal provision grounds are wider than in the DGCL, where they are very limited. This is because under the Model Business Corporation Act, for the purpose of

[607] Section 164 (15) (c) of the 2008 Act.
[608] Section 13.30 (d) of the Model Business Corporation Act.
[609] Section 13.31 (b) of the Model Business Corporation Act.
[610] Section 13.31 (b) (1) of the Model Business Corporation Act.
[611] Section 164 (15) (v) of the 2008 Act.
[612] Section 164 (17) of the 2008 Act.
[613] Section 164 (17) (a) and (b) of the 2008 Act.

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this research, they apply to the consummation of a merger to which a company is a party and the approval of shareholders is required, a consummation of a share exchange in a company whose shares will be acquired and where a shareholder is entitled to vote on the exchange and a consummation of a disposition of assets pursuant to section 12.02, if the shareholder is entitled to vote.[614] On the contrary, under the DGCL they only apply to mergers or consolidations, to be discussed in paragraph 4.2.2.3 On the *merger and amalgamation provisions*.

Exceptions to the above apply to a merger where a shareholder in a company holds shares of any class or series that remain outstanding after the consummation of the merger or a case where the company concerned is a subsidiary and the merger is governed in terms of section 11.05 of the Model Business Corporation Act.[615] The consummation of a share exchange is also not available to any shareholder of a company with respect to any class or series of shares of the company that is not exchanged.[616]

Under the 2008 Act shareholders are given notice of a meeting regarding a disposal of all or a greater part of the assets of the company with a right to appraise.[617] Similarly, under the Model Business Corporation Act, it is provided that if a company should propose the sale of all or part of its assets, this proposition should be submitted to a shareholders' meeting for a vote. The notice of the meeting directed to the shareholders of the company should disclose a copy of Chapter 13 of the Model Business Corporation Act, which deals with the right to appraise.[618]

4.2.2.2.1 Notice of objection

Furthermore, under the 2008 Act, when the proposal of the disposal of all or a greater part of the assets of the company is about to be voted on, any shareholder may give the company in question a written notice objecting to the resolution.[619] In instances where the proposed resolution is adopted, the company must notify this dissenting shareholder of this fact within 10 days.[620] This is similar to the fact that under the Model

[614] Section 13.02 (a) (1-4) (6-8) of the Model Business Corporation Act.
[615] Section 13.02 (a) (1) of the Model Business Corporation Act.
[616] Section 13.02 (a) (2) of the Model Business Corporation Act.
[617] Section 164 (2) of the 2008 Act.
[618] Section 13.20 (a) of the Model Business Corporation Act.
[619] Section 164 (3) of the 2008 Act.
[620] Section 164 (4) of the 2008 Act.

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Business Corporation Act, should a shareholder see a need to exercise his right to appraise in respect of any class of shares or series of shares in regard to the proposed transaction at a shareholders' meeting, the shareholder must deliver a written notice of his intention to demand payment to the company before the vote is taken, in case the transaction in question is effectuated.[621]

4.2.2.2.2 Notice of demand

Furthermore, under the 2008 Act, from this point onward the dissenting shareholder may proceed and demand from the company in question that he be paid the fair market value of the shares that he holds in the company.[622] However, he may only do so within 20 days after receiving a notice that the proposed resolution has been adopted,[623] provided of course that the dissenting shareholder did send a notice of objection as stated above and voted against the resolution.[624] The voting against is similar to the Model Business Corporation Act requisite, which provides that the shareholder must not vote, or permit to be voted with any shares of a certain class or series, in favour of the proposed transaction.[625] Should a shareholder fail to adhere to these prerequisites, he is not entitled to payment from the company.[626]

However, the number of days within which the notice to demand payment needs to be submitted differs in that in South Africa, as highlighted above, it is within 20 days, whereas under the Model Business Corporation Act jurisdictions the notice of appraisal rights needs to be no earlier than the date the company's proposal became effective and no later than 10 days after such date. It has to state when the company needs to receive such notice, but this may not be less than 40 days or more than 60 days since the notice was sent.[627] It must also state that the shareholder shall be considered to have waived the right to demand appraisal in regard to the shares, unless the notice is received by the company on a specified date. It would also state a date by which a notice to withdraw should be received, which must be within 20 days.[628]

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[621] Section 13.20 (a) (1) of the Model Business Corporation Act.
[622] Section 164 (5) of the 2008 Act.
[623] Section 164 (7) of the 2008 Act.
[624] Section 164 (5) of the 2008 Act.
[625] Section 13.20 (a) (2) of the Model Business Corporation Act.
[626] Section 13.20 (b) of the Model Business Corporation Act.
[627] Section 13.22 (b) of the Model Business Corporation Act.
[628] Section 13.22 (b) of the Model Business Corporation Act.

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It also needs to certify that the shareholder did not vote in favour of the proposed transaction, because if the shareholder fails to make this certification, the company in question may decide to treat the shareholders' shares as "after acquired" shares. Furthermore, if the shareholder concerned has certificated shares, he needs to submit these certificates along with the notice on a specified date. When all of this is done, the shareholder loses all rights to his shares unless he withdraws the notice to appraise.[629] The position of losing all right to shares is the same in the South African jurisdiction. This is because the 2008 Act provides that when a dissenting shareholder has demanded the fair market value of his shares from the company, he will no longer have rights in respect to those shares, except the right to be paid the fair market value of the shares.[630]

After the shareholder has submitted all the required documents as discussed above and perfected the right, the company in question must pay in cash the amount that the company itself estimates to be the fair value of the shareholder's shares plus interest.[631] Furthermore, the payment to this shareholder will be accompanied by the company's financial statements, which will include a balance sheet, income statement and a statement of changes in the shareholder's equity. The statement of the company's estimate of the fair value of the shares must also be included. Lastly, a statement should be included to the effect that the shareholder has a right to demand further payment and that if this demand is not made within a stipulated date, the company's offer shall be deemed to have been accepted.[632] Under the South African Act the inclusion of the company's balance sheet, income statement and a statement of changes is not a requisite from the company in question during the process of paying the fair value of the shareholders' shares.

4.2.2.2.3 Court intervention

The approach followed in South Africa when a dissenting shareholder is not satisfied with an offer made by the company for his shares is slightly different from that of the Model Business Corporation Act. This is because under the 2008 Act, the dissenting shareholder may make an application to court for a determination of a fair value of his

[629] Section 13.23 (a) of the Model Business Corporation Act.
[630] Section 164 (9) of the 2008 Act.
[631] Section 13.24 (a) of the Model Business Corporation Act.
[632] Section 13.24 (b) of the Model Business Corporation Act.

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shares,[633] whereas under the Model Business Corporation Act, if the shareholder concerned is dissatisfied with the payment or offer, he should notify the company in question in writing of his dissatisfaction by rejecting the offer. He should also make his own estimate of the fair value of the shares and demand payment of that estimate plus interest first.[634] Only after a shareholder has made a demand in writing for payment that remains unsettled, the company in question is obliged in terms of the Model Business Corporation Act to commence proceedings within 60 days from receiving this demand for payment and petition court to determine the fair value of the shares and the accrued interest.[635] The reason for this is that if the company in question does not commence proceedings within the prescribed 60 days it will have to pay the cash amount demanded by each dissatisfied stakeholder, plus interest.[636] Such a company needs to commence proceedings in the county where the company is based or where it has its registered office. If the company in question is a foreign company without a registered office in that state, it must commence proceedings in the state where the principal office or registered office of the domestic company merged with the foreign company was located at the time of the transaction.[637]

The court in the jurisdiction stated above in which proceedings are commenced is plenary and exclusive. This court may appoint one or more persons as appraisers to receive evidence and recommend a decision on fair share value. These appraisers shall have all the powers as detailed in the court order or on any amendment to it. The shareholders demanding payment in terms of the right to appraise are entitled to the same discovery rights as parties in other civil proceedings. However, there is no right to a jury trial.[638]

The company in question must make all shareholders, including shareholders who are not residents of that state, whose demands remain unsettled parties to the proceedings in an action that is against their shares and all these parties must be served with a copy of the petition. Those who are not residents of the state where the company is based may be served by registered or certified mail or by publication as

[633] Section 164 (14) of the 2008 Act.
[634] Section 13.26 (a) of the Model Business Corporation Act.
[635] Section 13.30 (a) of the Model Business Corporation Act.
[636] *Ibid.*
[637] Section 13.30 (b) of the Model Business Corporation Act.
[638] Section 13.30 (d) of the Model Business Corporation Act.

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provided by law.[639] All shareholders who are made parties to the proceedings are entitled to judgement (i) for the amount, if any, which the court in question may find to be the fair value of the shareholders' shares, plus interest, and (ii) for the fair value, plus interest of the shareholders' shares for which the company elected to withhold payment.[640]

The court in appraisal proceedings as discussed above must determine all costs of the proceedings. These will include the expenses of appraisers appointed by the court in question itself and reasonable compensation. The court will assess the costs against the company, except that the court will assess the costs against all or some of the shareholders demanding appraisal in an amount that the court finds equitable, to the extent the court finds such shareholders acted vexatiously, arbitrarily or not in good faith with respect to the rights that are under the appraisal right chapter of the Model Business Corporation Act.[641]

The 2008 Act, as far as costs are concerned, is not expressly clear, whereas when applying the Model Business Corporation Act the court in question will also assess the expenses and fees of experts and counsel for the respective parties in amounts the court finds equitable.[642] This may be against the company in favour of all or any of the shareholders demanding the appraisal. That would occur if the court finds that the company in question did not substantially comply with the appraisal steps discussed above.[643] It may also apply to either the company in question or a shareholder demanding appraisal and be in favour of any other party in the proceedings, if the court finds that the party against whom the expenses and fees are assessed acted vexatiously, arbitrarily or not in good faith with respect to the rights under Chapter 13 of the Model Business Corporation Act.[644]

However, if the court in question finds that the services of counsel for any shareholder were of substantial benefit to the other shareholders, the fees for those services should not be assessed against the company.[645] The court will award such counsel reasonable fees to be paid out of the amounts awarded to the shareholders who also

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[639] Section 13.30 (c) of the Model Business Corporation Act.
[640] Section 13.30 (e) of the Model Business Corporation Act.
[641] Section 13.31 (a) of the Model Business Corporation Act.
[642] Section 13.31 (b) of the Model Business Corporation Act.
[643] Section 13.31 (b) (1) of the Model Business Corporation Act.
[644] Section 13.31 (b) (2) of the Model Business Corporation Act.
[645] Section 13.31 (c) of the Model Business Corporation Act.

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benefited from those counsel services.[646] In instances where the company fails to make payment as required, the shareholders may sue the company directly for the amount owed and if successful will be entitled to recover from the company all expenses and costs of the suit, including counsel fees.[647]

4.2.2.3 On the merger and amalgamation provisions

The appraisal right process discussed above in paragraph *4.2.2.1 On the scheme of arrangement*, also applies to mergers and amalgamations in South Africa as per the 2008 Act. In the USA, for those states that use the DGCL, appraisal rights are provided under section 262 and only apply in mergers or consolidations.

However, even though they only apply to mergers, these include many types of mergers. Section 262 of the DGCL provides that appraisal rights must be available to shareholders of a constituent corporation in (a) a merger of domestic companies, excluding those mergers where a vote of shareholders is not necessary for authorisation of such a merger, (b) a merger of foreign and domestic companies, (c) a merger of a domestic company and a joint share or other association, (d) mergers of non-share companies, (e) mergers of foreign and domestic non-share companies, (f) mergers of domestic share and non-share companies, (g) mergers of domestic and foreign share and non-share companies, (h) mergers of domestic companies and partnerships, and (i) a merger of a domestic company and a limited liability company. Irrespective of this, there are other mergers that are excluded from appraisal rights. These are market exceptions, market-out exceptions or market exemptions.

4.2.2.3.1 Notice to shareholders

The position of providing shareholders with a notice of a meeting for the purpose of voting on a merger and informing the shareholders of their appraisal rights in that notice seems to be similar in the South African jurisdiction, the Delaware jurisdiction and those states using the Model Business Corporation Act. This is because the 2008 Act provides that when a company issues a notice on meeting that is to be held to decide on a merger, a notice of the right to appraise needs to be attached as well. [648]

[646] Section 13.31 (c) of the Model Business Corporation Act.
[647] Section 13.31 (d) of the Model Business Corporation Act.
[648] Section 164 (2) of the 2008 Act.

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Under the DGCL it is also provided that a company has to issue a notice to each and every shareholder in the company who has voting rights, informing them that they are entitled to exercise appraisal rights in anticipation of a merger.[649] This happens when the company in question sends out this notice within 20 days prior to convening this meeting where a merger proposal is to be discussed.[650] This notice that is sent out to the shareholders must be accompanied by a comprehensive statement notifying the shareholder of his right of appraisal. If the company in question fails to send this comprehensive statement to a shareholder, that can serve as a valid ground of excuse on behalf of that shareholder in the event of failure to comply with the procedure owing to insufficient information.[651] In the South African jurisdiction, if the notice is not sent to the particular shareholder, that serves as an exception for the shareholder not to perfect the appraisal step. Where the company failed to send out a notice of a meeting or sent out the notice without including a statement stipulating the shareholder's rights, the shareholder would be excused from perfecting the rule.[652]

Under the Model Business Corporation Act the parent company of a subsidiary must notify in writing all the shareholders of the subsidiary company who are entitled to exercise their right of appraisal when the company action becomes effective. This notice is sent within 10 days after the company action became effective and should include the materials that are described in section 13.22.[653]

4.2.2.3.2 Notice of objection

Under the 2008 Act, when a resolution on a merger is about to be voted on, a shareholder may give the company written notice objecting to the resolution before the voting.[654] This is similar to the position in DGCL, since when the shareholder is not in agreement with the proposed merger resolution, he must submit a written demand for appraisal to the company in question before the company votes on the merger

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[649] Section 262 (d) (1) of the Delaware General Corporation Law, Title 8.
[650] *Ibid.*
[651] *Raab v Villager Industry Incorporation* 335 A.2d 888, 894 (Del.1976). In this case the Delaware Supreme Court extended the scope of the company's pre-merger notice by imposing on all companies under Delaware an obligation to include in its notice an instruction of perfecting appraisal rights by shareholders. This court in its later case of *Enstar Corp. v* Senouf, 535 A.2d 1351, 1356-1357 (Del.1987) stated that proper directives are such that they disclose a material fact that is deemed necessary to allow a reasonable person to perfect his appraisal rights.
[652] Section 164 (6) of the 2008 Act.
[653] Section 13.20 of the Model Business Corporation Act.
[654] Section 164 (3) of the 2008 Act.

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resolution.[655] However, the position is different in the sense that this written demand sent to the company under Delaware must disclose the identity of the shareholder, must disclose the intention of the shareholder in demanding the appraisal of his shares and must be precise.[656] It is also noted that a letter of proxy or a vote against the resolution is not a demand in any form from the company in question.[657] What is of significant importance is the timely demand on the company within the timeframe determined by the statute, because failure to meet this timeframe would amount to loss of the right.

However, this written demand requisite has been criticised for being one of the major burdens that are imposed on the minority. This is because it may be difficult for a shareholder to declare his dissent before the voting on a merger has happened. Such procedural compliance also raises transaction costs for minority shareholders who are acting in good faith, despite being unfairly cashed out.[658] It has also been held that appraisal rights are complicated to such an extent that a dissenting shareholder has to navigate a variety of hurdles to perfect his rights, such as a written demand.[659]

Notwithstanding this, following the demand requirement above, the company in question must notify each and every dissenting shareholder who did not vote in favour of the merger resolution and who has made a demand to the company that the company has effected the merger. The company needs to notify these dissenting shareholders within 10 days from the effective date of the merger.[660] In instances where the merger is effected in terms of the short-form merger or by written consent, the notice must be given before the effective date or 10 days afterwards.[661] This position is similar to the one provided under the 2008 Act in South Africa. This is because section 164(4) of the 2008 Act provides that when a proposed resolution is adopted, the company in question must notify a dissenting shareholder of this fact within 10 days.

[655] Section 262 (d) (1) of the Delaware General Corporation Law, Title 8.
[656] *Ibid.*
[657] *Ibid.*
[658] Ventoruzzo "Freeze-Outs: Transcontinental Analysis and Reform Proposals" (2010) *Virginia Journal of International Law* 841-918 at 857.
[659] Geis "An Appraisal Puzzle" (2011) *North Western University Law Review* 1635-1678 at 1635.
[660] Section 262 (d) (1) of the Delaware General Corporation Law, Title 8.
[661] Section 262 (d) (2) of the Delaware General Corporation Law, Title 8.

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4.2.2.3.3 Notice of demand

Still on the DGCL, the dissenting shareholder, having fulfilled the requirements stated above, may make a demand on the company in question for a statement detailing all the shares pertaining to him. This request by the shareholder must be adhered to within 10 days from the date of such demand or 10 days after the expiration of the period of delivery for demands of appraisal.[662] The purpose of this statement is believed to have been making the shareholder aware of other dissenting shareholders initiating the right and probably assisting in the guidance of his decision to file an appraisal petition.

4.2.2.3.4 Appraisal petition

The appraisal petition can be filed within 120 days after the effective date of the merger.[663] This petition can be filed by either the shareholder who qualifies for this right or the company in question at the Delaware Court of Chancery, demanding a determination of the value of all the shares in respect of all the shareholders demanding the appraisal.[664] After this petition has been filed, the company in question needs to file with the registry in Chancery a verified list containing the names and addresses of all the shareholders within 20 days. These shareholders must have demanded payment for their shares and a settlement or agreement must not have been reached.[665] It is possible that this verified list could have been filed with the petition if the petition should have been filed by the company in question in the first instance.[666]

After the processes above have been complied with, a general notice on a hearing is sent to the parties in question, being the company and the shareholders in the verified list, by registered or certified email.[667] This notice must indicate the time and place for the hearing. Then the registry of Chancery will issue a notice in a newspaper with general publication in all states that utilise Delaware or as approved by court at least

[662] Section 262 (e) of the Delaware General Corporation Law, Title 8.
[663] *Ibid.*
[664] *Ibid.*
[665] Section 262 (f) of the Delaware General Corporation Law, Title 8.
[666] *Ibid.*
[667] Section 262 (f) of the Delaware General Corporation Law, Title 8.

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one week before the day of the hearing. The costs of this notice and publication are borne by the company in question.[668]

The Court mandates two hearings in respect of the petition. The first hearing is for the company to raise objections to the claim by the dissenting shareholders in respect of those shareholders who did not perfect their rights.[669] The second hearing is for the shareholders to rebut the claims that are being made by the company where required and assert their right. Each shareholder asserts his right individually, not collectively. This is because even in the case of *Re Universal Pictures Incorporation*[670] it was held that the burden falls upon a dissenting shareholder to establish his right to an appraisal and payment. This was also held in the case of *Tabbi v Pollution Control Industry Incorporation*,[671] where the court confirmed that the party seeking an appraisal must bear the burden of proving compliance with the provisions of section 262. It should be noted that the court determines which shareholder has perfected the appraisal right and is entitled to exercise such a right. It also reserves the right to dismiss the claims of shareholders who had not sufficiently perfected the right.[672]

The appraisal right does not become operational until 60 days after the merger was effected. During this period the shareholder can withdraw this appraisal demand from the company in question and accept the terms of the proposed merger.[673] However, a written request by the company in question is needed after the 60 days benchmark of the effective date. Where the petition has been filed, court approval will be required before the shareholder can withdraw the demand.[674]

From paragraph 4.2.2.1 On *the scheme of arrangement*, and 4.2.2.3 On *the merger and amalgamation provisions*, above, it is submitted that it can be inferred that the triggering events for appraisal rights in both South Africa and the Delaware jurisdictions are similar. The procedural requirements are also similar in nature when considering the notice of a meeting by a company, the voting for a proposed transaction in a meeting, the sending out of a written demand by a shareholder for

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[668] *Ibid.*
[669] Section 262 (g) of the Delaware General Corporation Law, Title 8.
[670] 37 A.2d 615, 618 (Del. Ch. 1944).
[671] 508 A.2d 867, 869 (Del. Ch. 1986).
[672] Section 262 of the Delaware General Corporations Law, Title 8.
[673] Section 262 (e) of the Delaware General Corporation Law, Title 8.
[674] *Ibid.*

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appraisal on the company, a notice of a resolution to proceed with the transaction being sent out and the issuance of a statement showing the shares.

However, the differences are also noted in the South African jurisdiction because the shareholder is responsible for making a petition for determination of what constitutes a fair value of his shares and this must be done before the offer made by a company lapses, similar to what is indicated in paragraph 4.2.2.2.3 Court *intervention*. The shareholder is the only one who can bring an application to court in respect of such determination, whereas in all Delaware jurisdictions both the company and shareholder can approach a court for determination of such value; see paragraph 4.2.2.2.3 Court *intervention*, above. In South Africa this gives a company an edge over a shareholder in the appraisal proceeding, since a shareholder must act timeously or would else be barred from making the court application. For example, the shareholder incurs the expenses of bringing such an application; he may not even be able to afford to institute such proceedings, let alone within the given time and therefore he can be left with an unfavourable determination made by the company.

It is submitted that in those states that use Delaware, companies are likely to bring an application if the shareholder does not, because defiance of the timing will result in determining the amount that the shareholder wants for his shares, which is binding on all the parties. Furthermore, under Delaware a comprehensive list, which joins other dissenting shareholders, must be filed in court along with a petition, whereas in South Africa a company is not under any obligation to file such a list. However, a shareholder must join the other dissenting shareholders in his application to court; see paragraph 4.2.2.2.3 Court *intervention*.

Another significant difference between the two jurisdictions is that in states that use Delaware, companies within that jurisdiction are mandated to publicise the process in a newspaper that is generally accepted within that jurisdiction. Furthermore, the notice of the petition hearing is sent to the company and the shareholders in question through registered mail. This feature is not included in the South African appraisal provisions. It is submitted that such a process would make things easier for shareholders in South Africa as it does in the USA, since it attempts ensure that all the parties to the proceedings are informed.

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Furthermore, under the DGCL appraisal rights are not available to every shareholder, especially shareholders whose shares are either listed on a national securities exchange or are being held on record by more than 200 holders on the date on which the shareholders are entitled to receive notice of the meeting of shareholders to vote on a merger.[675] The application of this provision is not limited to shares that are issued by the surviving company after a merger, but also applies to shares of an acquired company. Similarly, exceptions indicated above still apply, regardless of the form in which a merger was approved, whether it was approved by the written consent of shareholders or whether shareholders voted in a general meeting.[676]

In addition to the above, appraisal rights are not available to shareholders who hold shares in a surviving company in a case where the merger does not require approval by voting of shareholders.[677] A comparable exception of appraisal rights under Delaware, which can also be found in the Model Business Corporation Act, is the one that provides that appraisal rights are not available to holders of shares that can easily be sold in a liquid market. In essence this applies to those shares that are traded in an organised market, are covered by the Securities Act and have at least 2000 holders and a market value of at least 20 million dollars or are issued by a management investment company.[678]

Another exception under the DGCL is a provision that limits the above exception, which states that appraisal rights are not available to shareholders of the surviving company in the case of a merger that did not require approval by voting. This provision grants appraisal rights to holders of shares of any class or a series of shares of a constituent company only if holders of such shares are required by the terms of the agreement of a merger to accept consideration in the form of cash, shares or a mixture of the two.[679] However, the consideration that is received by these shareholders must be different from the shares that they held before a merger. This means that this exception does not apply to those shareholders of a surviving company whose shares are not affected by the merger.[680] In the context of the South African jurisdiction it is

[675] *Ibid.*
[676] Welch *et al Folk on the Delaware General Corporation Law: Fundamentals* (2010) (Aspen, New York) at 733.
[677] Section 251 (f) of the Delaware General Corporation Law, Title 8.
[678] Section 13.02 (b) (1) of the Model Business Corporation Act.
[679] Balotti and Finkelstein *supra* n562.
[680] Welch *et al infra* n676 at 736.

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submitted that some of these exceptions should be incorporated into the 2008 Act. It is believed that they will lessen the chances if not eliminate the failure of a proposed fundamental transaction that may be caused by the appraisal remedy. Ways in which the appraisal remedy may possibly frustrate a proposed fundamental transaction are discussed further in detail in paragraph 4.2.3 Observations and of this chapter. These exceptions could be included under the appraisal provisions that the appraisal remedy applies to a proposed merger, except in instances such as the ones listed above.

The appraisal remedy in its draft phase under the 2008 Act was criticised, especially its application under the statutory merger. In agreement with Cassim, it was submitted that this remedy, as much as it was in favour of minority shareholders, was somehow skewed more in favour of the company, since the minority shareholder loses his right to appraise, should he fail to comply with certain procedural steps within a specified time.[681] Such a failure implies that minority shareholders fail to send the company a written notice of objection and a written demand where a resolution has been adopted, as indicated above in paragraph 4.2.2.1 On *the scheme of arrangement*. On the other hand, the company suffers no consequences it if should fail to send the required notices described in paragraph 4.2.2.1 On *the scheme of arrangement*, above. These are a notice on a shareholders' meeting to vote on a fundamental transaction resolution together with a statement of available shareholders' rights and notice to dissenting shareholders informing them that the resolution has been adopted, as indicated in paragraph 4.2.2.1 On *the scheme of arrangement*.

Even where the company fails to make a written offer to the dissenting shareholders to pay the fair market value of their shares as per their demand notice, it suffers no adverse consequences.[682] On the contrary, the minority shareholder has 30 days to apply to court from the date of the company's offer so it can determine the fair market value of his shares, should he feel that the company's offer is not fair. Should he fail to do so within 30 days, he loses his right to apply to a court for a judicial appraisal, as discussed in paragraph 4.2.2.1.4 Written *offer made by the company*.

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[681] Cassim supra n277 at 164.
[682] *Ibid*.

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It was submitted that the imbalance inherent in these provisions operate in favour of the company and harshly against minority shareholders. This results in great potential for unfairness to a dissenting shareholder who may possibly lose his right to appraise because of an unknowing failure to comply with one of the technicalities and the complex steps discussed above.[683] Apart from the instances discussed above, a minority shareholder as opposed to a company would not have access to ready funds for legal representation and proper guidance in complying with the complex procedural steps.[684]

The underlying purpose of these procedural steps is to promote and encourage settlement between the company and the dissenting shareholders without either of the two resorting to judicial appraisal. Nevertheless, it is found that the balance drawn by the then draft, which is now the 2008 Act, between the company and the dissenting shareholder has to be adjusted.[685] Cassim further submitted that what was to form part of the 2008 Act should provide for greater latitude for shareholder compliance with its procedural obligations.[686] Court should be given wider discretion to extend the prescribed time limits for dissenting shareholders to comply with the prescribed procedural steps and where suitable to condone shareholder non-compliance with the procedure.[687] It is hoped that this will enable courts to interpret the dissenting shareholders' procedural requirements as flexibly and leniently as possible, thus to excuse the lack of strict compliance by a shareholder despite a genuine attempt to comply with the prescribed requirements.

Another procedural flaw of the appraisal right is the delay experienced by the dissenting shareholder when he exercises his right to appraise, in view of the fact that after sending the written demand to the company in regard to the fair market value of his shares, he loses all further rights in respect to those shares other than to be paid a fair value for them.[688] This fair value for the shares is only paid at the end of the appraisal proceedings and during this period the dissenting shareholder is deprived of the use of his funds. Cassim submitted that requiring the company to pay in cash a

[683] *Ibid.*
[684] *Ibid.*
[685] *Idem* at 165.
[686] *Ibid.*
[687] *Ibid.*
[688] *Ibid.*

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provisional amount, which is the company's estimate of what constitutes a fair market value of the relevant shares, at an earlier stage would be a better approach.[689] This would mean that the dissenting shareholder has immediate use of his funds,[690] while in the meantime any dispute between the dissenting shareholder and the company is settled in court. The balance of fair market value could then be determined at the judicial appraisal proceedings after the initial payment has been made. This approach has been adopted in the Model Business Corporation Act[691] but not under DGCL.[692]

Another procedural element that was criticised by Cassim was the one that deals with costs in appraisal proceedings. The draft at the time, which is now the 2008 Act, provided that court has the discretion to make an appropriate order of costs by considering the offer made by the company and the final determination of the fair value by the court itself.[693] It was submitted that even though the discretionary nature of the costs order might to a certain extent encourage parties to reach an agreement in good faith on the fair value of shares without thoughtlessly resorting to court, these costs should not serve as a deterrent to the submission of the right to appraise by a shareholder.[694]

Furthermore, valuation is not an exact science but just an estimate or a mere prediction and a judicial determination of what constitutes a fair value creates uncertainty. Moreover, it poses a substantial risk that the shareholder's estimate of what constitutes the fair value of his shares may be higher than the valuation made by court.[695] Conversely, to the shareholder's detriment the court's determination may be less than what the company offered in the first place.[696] For these reasons the right to appraise was found to be prohibitively costly to a dissenting shareholder.[697]

From the above Cassim inferred that to improve the bill at the time, which is now the 2008 Act, legislators had to consider widening the discretion of the court to enable it to assess the costs as it finds equitable against the company or the dissenting

689 *Ibid.*
690 *Ibid.*
691 Section 13.24 of the Model Business Corporation Act.
692 Cassim *supra* n277 at 166.
693 *Ibid.*
694 *Ibid.*
695 Pinto and Branson *supra* n569 at 128.
696 *Ibid.*
697 *Ibid.*

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shareholder in a case where court finds that either has acted unreasonably, displeasingly or in bad faith. This is the position in some of the states in the USA, especially those that apply the Model Business Corporation Act.[698] She believed that this would give the court wider discretion that would enable it to avoid imposing a costs order on a dissenter despite the court's estimation of what constitutes fair value in the company's offer, in a case where the shareholders' ideas of what constitutes a fair value was not unreasonable, displeasing or in bad faith.[699]

Moreover, on the valuation of shares it is noticeable that under the DGCL the task of share evaluation in appraisal proceedings is performed by the Delaware Court of Chancery, which is a specialist court that is rather more experienced in valuation than most South African courts.[700] Cassim therefore submitted that South African law should follow the richly developed Delaware jurisprudence on the valuation of what constitutes fair value of shares in appraisal. Even under Delaware the discounted cash flow methodology was difficult for untrained judges in valuation to apply.[701] Courts under Delaware as a result ended up appointing their own experts in appraisal cases.[702] This exercise is similar to the one under the 2008 Act, which makes provision for the discretionary appointment by court of appraisers to assist in determining what constitutes fair value.[703]

Delaware also clearly defines that the dissenting shareholder's claim is a pro rata claim to the value of the company as a going concern.[704] This implies that the underlying principle of an appraisal proceeding is to value the company itself, to value it on a going concern basis rather than on a liquidated basis and not to value the shares that are held by a shareholder.[705] In the Delaware Court it was also stressed that the fair value did not equate to a market value alone. Where the shares are undervalued on the market, the market price of the shares will not reflect the fair value of those

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[698] Section 13.31 (b) of the Model Business Corporation Act.
[699] Cassim *supra* n1681 at 166.
[700] Bainbridge *Mergers and Acquisitions* (2008) (Foundation Press, UK) at 640.
[701] Cassim *supra* n277 at 166.
[702] Allen and Kraakman *supra* n378 at 456.
[703] Cassim *supra* n277 at 170.
[704] *Cavalier Oil Corporation v Hartnett* 564 A 2d 1137 (SC Del, 1989) at 144-5. Also Allen and Kraakman *supra* n378 at 455.
[705] *Ibid.*

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shares[706] and this is a position that has long been accepted in the USA.[707] The impact of this in the South African jurisdiction is that shares that have been valued in terms of the market value have been incorrectly valued, since according to the market value, shares can be undervalued, which would not reflect the fair value of those shares.

Furthermore, it was pointed out that the issue of what constitutes a fair market value under the 1973 Act as opposed to the provisions contained in the bill, which have now been incorporated into the 2008 Act, was considered in the context of the oppression remedy under section 252.[708] The same happened with the mandatory acquisition of shares of minority shareholders under section 440K.[709] However, the arguments and factors that were raised on this matter do not necessarily apply, especially in cases where the fair value is being assessed for the purpose of the appraisal remedy. The difference lies in the fact that in this situation the minority shareholder is beneficially being forced out of the company and with the appraisal remedy this is not necessarily the case.[710]

A further procedural element that was criticised was the fact that provisions in the bill that is now the 2008 Act, as indicated above, place the burden on a dissenting shareholder instead of the company to initiate judicial appraisal proceedings. It was submitted that the South African jurisdiction should follow the approach that applies in jurisdictions that use the Model Business Corporation Act.[711] This approach provides that a company needs to commence appraisal proceedings within 60 days from the receipt of the dissenting shareholder's demand.[712]

4.2.3 Observations and submissions

The traditional appraisal right point of view in the USA, as indicated in paragraph 4.2.1, was widely spread and accepted by courts until 1962 when Bayless Manning criticised

[706] Conard "Amendments of the Model Business Corporation Act Affecting Dissenter's Rights (Section 73, 74 and 80)" (1979) *Business Lawyer* 2587-2606 at 2596.
[707] *In re Valuation of Common Stock of Libby*, *McNeill* & *Libby*, 406 A 2d 54 (SC Del, 1979) at 60, *The Chicago Corporation v Munds* 172 A 452 (Ch C Del, 1934).
[708] The oppression remedy is discussed in detail in paragraph 4.3.2.1 Relief from oppressive and unfairly prejudicial conduct, below.
[709] Cassim *supra* n277 at 168.
[710] *Ibid.*
[711] *Idem* at 168.
[712] Section 13.30 (a) and (b) of the Model Business Corporation Act.

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it in an essay.[713] He stated that appraisal rights do not mainly serve to protect the rights of the outvoted shareholders against changes and decisions that are made by the majority shareholders. Instead, their application enables the majority shareholders, or rather management to be precise, who are acting on behalf of majority shareholders, to take actions more easily and with greater mobility.[714] This happens with the assistance of the courts, which prefer that the minority shareholders revoke or exercise their appraisal rights rather than to accept the dissenting shareholders' court application to set aside the proposed transaction.[715]

Manning stated that the development of the appraisal rights took place at the same time as the development of American corporate law, which was in the direction of the will of the majority and that these rights were promoted by perspicacious legislative agents of management,[716] also manifesting the possibility that the appraisal rights are just a remedy for the majority shareholders to proceed with their decisions irrespective of what the minority shareholders recommend. He further stated that even without the statutory appraisal rights, courts would probably have supported the will of the majority over the will of the minority, in view of the fact that it is no longer feasible to let an objecting individual block a transaction approved by the majority.[717]

He stated that the exercise of these rights can prove to be a burden, since any shareholder who opts for them must incur the costs of the procedure, even if those costs are not significant. That shareholder also remains in uncertainty about the result of the proceedings, which often take a long time to conclude.[718] Instead of opting for the appraisal rights, such shareholders thus rather sell their shares in the open market when considering the long and expensive judicial procedure associated with the appraisal right, as indicated above.

He stated that the efficiency of a remedial procedure is key to the usefulness of the remedy at law and that the application of the appraisal rights is hindered by the long and complicated statutory provisions and by courts that are prone to strict

[713] Manning "The Shareholder's Appraisal Remedy: An Essay for Frank Coker" (1962) *Yale Law Journal* 223-265 at 233.
[714] *Idem* at 227.
[715] *Ibid.*
[716] *Ibid.*
[717] *Idem* at 229-230.
[718] *Ibid.*

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interpretation and application of statutory provisions.[719] With that fact in mind, when the market value of shares of dissenting shareholders in a company is not known, the estimation of the value of those shares by court becomes unpredictable, the proceedings become expensive because of delays and their outcomes are uncertain.

With reference to the above and for the purpose of this research, the writer submits that appraisal rights impose restraints on companies. This is because when a company enters into a fundamental transaction that could trigger appraisal rights, the management of those companies do not know and are unable to estimate how many dissenting shareholders there would be who could exercise their appraisal rights. This situation creates great uncertainty, especially if one views things from the economic perspective. In a situation where there are many dissenting shareholders who exercise their appraisal rights and need to be paid the aggregate sum of the value of their shares in cash, this could cause liquidity problems in a company, which may end up abandoning the proposed fundamental transaction in question.

Financial problems in a company that are caused by dissenting shareholders who exercised their appraisal rights have the potential to hinder the decisions that are taken by the majority. For example, a company that adopted a resolution to merge with another company actually does not know at the time of adopting the resolution how many dissenting shareholders will exercise their appraisal rights and how much money the company will need to buy their shares.[720] These issues are contrary to the purpose and role given to appraisal rights as indicated above; their role is to protect not only minority shareholders but also majority shareholders in respect of being able to proceed with resolutions that were adopted.

These considerations substantiate Manning's thoughts when he states that appraisal rights have failed to provide simultaneous protection to both dissenting shareholders and the decision of the majority. The majority should be able to proceed with the

[719] *Idem* at 231. Manning provided that the appraisal provisions became longer and more complex over time compared to earlier provisions, which did not provide answers on key questions in respect of the appraisal remedy and procedure. These were questions such as who bears the costs of the procedure, how long the procedure is, what the legal grounds of judicial review are and when a shareholder ceases to be a shareholder in a company.
[720] *Idem* at 235.

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adopted resolution for a fundamental transaction as per the appraisal rights traditional point of view, as discussed in paragraph 4.2.1 above.[721]

The writer submits that this position would not have changed even if some of the submissions that were made against the 2008 Act while it was in its draft phase had been implemented. For instance, as discussed above in paragraph 4.2.2.3.4 *Appraisal petition*, it was submitted that there needs to be provisional payment when a minority shareholder has exercised his right to appraisal. A similar approach is applied in some of the states in the USA, especially those that use the Model Business Corporation Act. It is submitted that this would put a company in a more detrimental position than it is in the current circumstances.

The above submission is made because the company having to pay an amount that it deems a fair market value during the period of engaging in a fundamental transaction could lead to it not being able to afford to proceed with the transaction, since it might be unable to pay the dissenting shareholder and engage in the proposed transaction at the same time. Moreover, at the end of the appraisal proceedings it might have to pay more if the court finds in favour of what the shareholder regards as a fair value for his shares.

Furthermore, the writer submits that another consideration apart from the above is the fact that the proceedings that will get the court to decide on what constitutes a fair market value of the dissenting shareholders' shares add to the drain on the financial resources that the company needs to have. This is because the company would need to get legal representation for these proceedings and delays in the proceedings may lead to even higher costs. This may be considered a poor allocation of financial resources, especially if the court decides that the company's offer to the dissenting shareholders was unfair. However, legal representation in these proceedings adds to the finances that the company has to have at its disposal should it not abandon the proposed fundamental transaction against which the appraisal rights are being exercised. This could lead to the company being out of pocket, should it choose to proceed with the proposed fundamental transaction.

[721] *Idem* at 236.

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The submission needs to be considered that the South African jurisdiction should follow the position under the Model Business Corporation Act as discussed above in paragraph 4.2.2.3.4 *Appraisal petition*, that a company should be the party that initiates appraisal court proceedings instead of a shareholder if there is no agreement between the company and the dissenting shareholders on what constitutes the fair market value of these shareholders' shares.

The writer submits that the above position, especially for the purposes of this study, does not make matters any easier for a company, particularly if the company cannot afford simultaneously funding the proposed transaction and the fair market value demand of the dissenting shareholders shares, having made an offer that the dissenting shareholders refused. The above position would mean that the company in question will have to abandon the proposed transaction, since it cannot afford to initiate appraisal court proceedings as required because it would not be in a position to afford further costs for legal representation that would assist the company in the proceedings.

Further arguments can be made on the issue of a company not being able to afford both the proposed fundamental transaction and the fair market value of the dissenting shareholders' shares. The writer submits that what is commendable in the 2008 Act is its stance on instances where a company and dissenting shareholders are engaged in appraisal court proceedings, and the court holds that the company in question has to pay a certain value, which it considers the fair market value of the dissenting shareholders' shares. It might happen that the company will be unable to comply with this court order, since it may be unable to pay its debts as they fall due and payable for the ensuing 12 months.[722]

The 2008 Act attempts to provide a solution by allowing the company in question to make an application to court to vary its obligations in these circumstances. The court can make an order that is just and equitable, ensuring that the company will pay at the earliest date possible that is compatible with meeting its other financial obligations. However, this applies at the stage of appraisal court proceedings and a court order having been made. It is submitted that this is a process that is only available when there is a court order that states that the company in question should pay a certain

[722] Section 164 (17) of the 2008 Act.

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value, which it holds as the fair market value of the dissenting shareholders shares. It would also apply if the company made an offer to the dissenting shareholders for their shares and these shareholders accepted the offer, but the company is not in a position to effect the payment of this offer within the required 10 days as per the 2008 Act.

Therefore, the writer submits that the problem here is that the section does not consider the instances that are raised in this section where a company cannot afford both the proposed fundamental transaction and the fair market value of the dissenting shareholders' shares, but can afford to pay one. The court will grant an order of relief should it find that the company in question will be unable to pay its debts as they become due in the ensuing 12 months but not where the company can pay the fair value of the dissenting shareholder shares but only if it abandons the proposed fundamental transaction.

This situation of considering both the fundamental transaction and the payment of the dissenting shareholders' shares is used by the writer because in practice a company is most likely to propose a fundamental transaction if it has the financial means to do so. This is also supplemented by the fact that the merger provisions of the 2008 Act require the boards of both merging companies to consider the fact that after the merger both merging companies will meet the solvency and liquidity test.[723] This test requires that a company be able to pay its debts as they become due in its ordinary course of business.

Furthermore, under this section it is stated that the court will grant relief after having regard to the financial circumstances of the company[724] and that the dissenting shareholder must be paid at the earliest possible date.[725] In consideration of the above practical circumstance, the writer submits that the court will know that the company can afford to pay the fair market value of the dissenting shareholders at the earliest possible date but only if it abandons the proposed fundamental transaction.

In another point varying from the above, Manning, as indicated in the paragraph above, stated that in the USA shareholders remain in uncertainty regarding the result of the appraisal proceedings, since the court can take long to reach a conclusion. It is

[723] Section 113 (4) and 4 (1) of the 2008 Act.
[724] Section 164 (17) (b) (i) of the 2008 Act.
[725] Section 164 (17) (b) (ii) of the 2008 Act.

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submitted that in the South African jurisdiction this does not apply to only the shareholders but to the company in question as well, especially for the purposes of this study. The fact that a company that has proposed a fundamental transaction has to consider the effects of the exercise of appraisal rights by the dissenting shareholders in the company makes the company uncertain about pursuing the proposed transaction further.

In other words, the writer implies that the appraisal proceedings put deal certainty at risk, as the company may consider options other than the one challenged by the appraisal rights, forcing the abandonment of the fundamental transaction. This means succumbing to effects such as the ones discussed in this paragraph above that a company may not be able to afford both the proposed fundamental transaction and the fair market value of the dissenting shareholders' shares.

Scholars have also criticised this traditional point of view, for example Fishel, who regards appraisal rights as an implied contractual term,[726] which provides for the minimum price at which a company's shares or part of these can be sold in situations where particular groups are likely to try to appropriate wealth from other groups rather than maximising the value of the company' shares.[727] He argues that by setting a minimal price for the company's shares the appraisal rights protect all shareholders from entering into a transaction where the value of their shares is reduced by a bidder and as a result of the appraisal rights all the shares in the company subject to a transaction are traded at a higher price.[728] The writer agrees with this view as far as the protection of shareholders is concerned.

Fishel argues that appraisal rights also have an effect in the process of negotiation of a transaction by the management of the company,[729] since this process sets the price that will be approved by the shareholders of the company. According to this theory shareholders are more likely to support a transaction if they know in advance that their shares will not be sold at a price below a certain level and that the higher price paid for these shares is a result of the appraisal rights.[730]

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[726] Fishel "The Appraisal Remedy in Corporate Law" (1983) *American Bar Foundation Research Journal* 875-902 at 878. Letsou *supra* n565 at 1125 describes this theory as wealth appreciation theory.
[727] *Idem* at 876.
[728] *Ibid.*
[729] *Ibid.*
[730] *Ibid.*

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In South Africa this appraisal remedy does not serve as a pre-court method as in the USA in situations where the minority shareholders are not in agreement with the majority in a company.[731] Rather, in South Africa this remedy serves as one of the alternatives a shareholder may utilise when not in agreement with an adopted resolution. The exclusivity of appraisal rights has been raised in the USA where other potential remedies such as damage actions are not available to dissenting shareholders. In such a case the triggering event does not justify potential remedies other than the right to appraise, which is to be bought out of their shares by a company at the fair value determined by court.[732] This exclusivity of the right of appraisal results in courts extinguishing shareholders' claims other than appraisal claims.[733]

However, it should be noted that the exclusivity of the right to appraise does not apply in all states in the USA. Some of the states provide that the appraisal right is exclusive in certain circumstances and with some exceptions. Moreover, in some of the states the right to appraise is not exclusively determined.[734] This was the situation under the DGCL until it was interpreted differently in the Delaware Supreme Court discussed below, as it is merely silent in regard to the right of appraisal exclusivity. It was an issue that remained unresolved for a long time and even resulted in controversial litigation cases that were determined in Delaware courts. In early cases that were determined under these courts it was held that the right to appraise was an exclusive remedy for dissenting shareholders except in situations that involved fraud or illegality.[735]

The Delaware Supreme Court in its later judgements held that dissenting shareholders could actually claim to enjoin a merger if they could prove that the merger was inadequate, unfair and did not serve a proper business purpose.[736] It could also be argued that a class action suit was an option that was available to dissenting shareholders if they needed to obtain rescissory damages from an acquiring company

[731] See Chapter 3 para 3.3 in this regard.
[732] Pepin "Exclusivity of Appraisal - The Possibility of Extinguishing Shareholder Claims" (1992) *Case Western Reserve Law Review* 955-991 at 955-956.
[733] *Ibid.*
[734] Vorenberg "Exclusiveness of the Dissenting Stockholder's Appraisal Right" (1963-1964) *Harvard Law Review* 1189-1217 at 1189-1190. Also, Seligman "Reappraising the Appraisal Remedy" (1983-1984) *Georgia Wash Law Review* 829-871 at 835-836. Examples of states where appraisal rights have the right of exclusivity are Georgia and Ohio.
[735] Fishel *supra* n726 at 898. *Stauffer v Standard Brands*, 187 A.2d 78 (Del. 1962) and *David J. Greene & Co. v Schenley Industries*, 381 A.2d 30 (Del. Ch. 1971).
[736] *Singer v Magnavox Co.*, 380 A.2d 969 (Del. 1977).

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based on the breach of fiduciary duty or misrepresentation in regard to a tender offer.[737] These court cases therefore meant that dissenting shareholders could actually bring a class action suit claiming rescissory damages or an injunction action as a collateral action to the right of appraisal proceeding. The application of these two decisions and the pursuit of collateral actions by minority shareholders meant that appraisal rights as a remedy at law had lost its importance.[738]

However, this situation changed in 1983 when the Delaware Supreme Court in the case of *Weinberger v UOP*, *Inc.*,[739] gave a decision that forms the basis of the current application of the appraisal right exclusivity in Delaware. This court, in making its decision, held that the right to appraise is the exclusive remedy for a dissenting shareholder even in a case of a cash-out merger.[740] The dissenting shareholder's only allegation is an appropriate cash value of his shares as determined by the directors of the company in question.[741] However, the court also held that the right to appraise is not the exclusive remedy of a dissenting shareholder in a case where there is misrepresentation, fraud, self-dealing, deliberate waste of a company's resources and palpable overreaching.

Therefore, since the above Delaware Supreme Court decision, several conditions have had to be met in order to invoke the exclusivity of the right of appraisal with regard to company decisions that trigger appraisal rights.[742] These are (a) an all cash-out freeze-out merger, and that (b) a dissenting shareholder's claim must not concern directors' other decisions, (c) a dissenting shareholder's claim must declare only an appropriate cash value of that shareholder's shares determined by the directors of the company in question, and (d) a dissenting shareholder's claim only requires cash relief excluding allegation of facts sufficient to justify non-damage relief.[743]

However, the decision in the *Weinberger v UOP Inc* case in respect of the exclusivity of appraisal rights has been criticised for not expressly clarifying whether the right to appraise is the exclusive remedy of dissenting shareholders in cash-out mergers. It was also argued that the Delaware Supreme Court did not intend to declare the

[737] *Lynch v Vickers Energy Corp*., 429 A.2d 497 (Del. 1981).
[738] Fishel *supra* n726 at 899.
[739] 457 A.2d 701 at 714.
[740] *Idem* at 703-704.
[741] *Ibid*.
[742] Pepin *supra* n732 at 968.
[743] *Idem* at 968-972.

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appraisal right an exclusive remedy.[744] It was submitted that appraisal right exclusivity is a function of entire fairness and that this function is reinforced by courts that follow the assumption of the appraisal right exclusivity, which is not provided in the appraisal statutes.[745] Irrespective of the criticism, the issue of the right of appraisal exclusivity in the short-form merger is less complicated, since it is settled in case law and it is implied that if a controlling shareholder holds at least 90% of shares in a company the minority shareholders may be cashed out without the shareholders' vote. This means that the exclusive remedy of the dissenting shareholder is the appraisal right.[746]

The writer submits that the problem with the South African appraisal right is that it does not have the exclusive right in respect to merger-triggering events as the one under Delaware jurisdictions, as discussed in the paragraph above. This allows the dissenting shareholder to try alternative remedies that can halt a proposed fundamental transaction, as highlighted in paragraph 3.3 of Chapter 3.

4.3 Position prior to the appraisal remedy

4.3.1 Introduction

The position prior to the appraisal remedy is analysed to see whether the shareholder protection rules that applied before the appraisal remedy did not frustrate the realisation of fundamental transactions. This is done because in paragraph 3 of Chapter 1 of this research it was submitted that appraisal rights at times tend to frustrate proposed fundamental transactions. Furthermore, the aim is to see whether the position prior to the introduction of the appraisal remedy in South African law was better or not and it is submitted that this will provide full analysis in regard to the appraisal right.

4.3.2 Minority shareholders protection

The daily operations and affairs of a company are presided over by the board of directors.[747] However, when it comes to the decisions that have to do with fundamental

[744] Coleman "The Appraisal Remedy in Corporate Freeze-Outs: Questions of Valuation and Exclusivity" (1984) *South Western Law Journal* 775-798 at 782-786.
[745] *Idem* at 795.
[746] Steinberg "Short-Form Mergers in Delaware" (2002) *Delaware Journal of Corporation Law* 489-498 at 491. Glassman v Unocal Exploration Corp., 777 A.2d 242, 248 (Del. 2001) and In re Appraisal of Aristotle Corp., C.A. No. 5137-CS (Del. Ch. Jan. 10, 2012).
[747] Section 66 (1) of the 2008 Act.

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transactions, these decisions are taken by the shareholders of the company in terms of a vote in a meeting called for that specific purpose.[748] Normally the shareholders with the majority of votes in that company will have absolute control and determine the decisions of that company. This is because differences in decisions of the company are resolved through voting in a meeting. This voting in a meeting could be to the advantage of the majority shareholders and to the disadvantage of the minority shareholders, considering the fact that a majority shareholder with the controlling vote will apply it in the manner that suits him best without considering how it suits the rest of the shareholders.[749]

In a case where a majority shareholder makes a decision in respect of the company despite this not being in the best interest of the company, the board of directors of that company are saddled with the responsibility of instituting legal proceedings on behalf of the company, as will be shown below, to address the wrongs that are being done against the company. This is because the 2008 Act provides that the board of a company must act in the best interest of the company and in doing so protect the interests of all shareholders in the company.[750]

However, in practice the board of directors in a company is normally put together by the majority shareholder. This board of directors is mindful of the fact that it exists because of the majority shareholder and would normally act in according with the suitability to the course of the majority shareholder. In many instances this is most likely to be to the disadvantage of the minority shareholders. The wrongdoer will be the majority shareholder who has the board of directors on his side and it is highly likely that the board will not take any action to redress the wrongdoing against the company unless the minority shareholders take a stand.

Even so, when the minority shareholders take a stand and put the matter to the vote, as indicated above, differences are settled by vote in a meeting. The majority shareholders would vote in their own favour and for what is in their best interest. In instances where the matter is brought before the court, the majority shareholders are still strengthened by the corporate rule of instituting legal action on behalf of the company. Any wrongdoing must be against the company as a whole, not against

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[748] Section 115 of the 2008 Act. This was discussed in detail in Chapter 3 of this research.
[749] Hicks *Cases and Materials on Company Law* (2001) (Blackstone Limited, New York) at 222.
[750] Section 76 of the 2008 Act.

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specific shareholders, and this wrongdoing must be addressed by only the company.[751] This is a principle that was well pronounced in the case of *Foss v Harbottle*[752]*,* where was affirmed that the company and not the company's shareholders can bring an action against any wrongdoing done to the company. This serves to protect the company from unwanted and harmful litigation. The only exception to this rule is where minority shareholders institute an action that involves violation of a personal right as guaranteed under the MOI of the company or there is fraud against the minority shareholders.[753]

However, the above position has since changed, because the 2008 Act provides that a prescribed officer, shareholders, directors and a registered trade union may bring an action on behalf of the company.[754] Unfortunately, as a result minority shareholders are left vulnerable and without the protection of the board of directors, as the directors are most likely to support the majority, as discussed above. It is therefore submitted that this situation introduced the idea of having protection measures in favour of the minority in a company. These protection measures that applied before the introduction of the appraisal remedy and still apply are relief from oppressive and unfairly prejudicial conduct[755], which was referred to in paragraph 4.2.3 above, and derivative action.[756]

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[751] *Burland v Earle* [1902] A.C 83 at 93 (P).
[752] (1843) 2 hare 461; 67 ER 189.
[753] Cilliers *Corporate Law* (1992) (Butterworths, Cape Town) at 290. In the case of *Greenhalgh v. Arderne Cinemas Ltd* [1951] Ch 286, [1950] 2 All ER 1120 an exception was provided to the *Foss* v. *Harbottle* rule. In this case Mallard was a controlling shareholder in Ardene Cinemas Ltd and he entered into an agreement with Sheckman for the sale of his shares. This agreement was authorised in the general meeting by a special resolution, which at the same time changed the articles of association. The articles of association stated that if shares were transferred, existing shareholders in the company would be considered first. Mallard did not advise that the money with which his shares were bought was going to come from the company and not Sheckman. Greenhalgh, who was a minority shareholder, sought a declaration that the resolution that approved the transaction was fraud on him and other minority shareholders and asked for compensation. The court in this matter held that it is common that an outside party makes an offer to a company to buy all the shares, prima facie, if the shareholders think it is a fair offer and vote in favour of the resolution; it is no ground for impeaching the resolution that they are considering their own position as individuals. In this case the action was not brought on behalf of the company but by the minority shareholders themselves.
[754] Section 165 (2) of the 2008 Act.
[755] For the purpose of showing the protection as existing prior to the appraisal remedy section 252 of the 1973 Act is applied. Section 163 of the 2008 Act shows that the protection measure is still in existence.
[756] The protection measure used to be under section 266 of the 1973 Act but is now under section 165 of the 2008 Act.

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4.3.2.1 Relief from oppressive and unfairly prejudicial conduct

Minority shareholders under this remedy could seek relief for any conduct that was found to be prejudicial or even oppressive towards any of them within the company.[757] This included any actions that were commenced upon by the majority shareholders through their decisions that affected the interests of the minority shareholders, as long as these actions that occurred as a result of decisions taken by the majority were deemed oppressive and were declared unfair to the minority shareholders.[758]

The oppression remedy still exists in South African law and its frame has been expanded; a director of a company can now seek relief under this remedy.[759] Also, the conduct that can be complained of now includes an act or omission of the company or a related person, or conduct or carrying on of business of the company or related person in an oppressive manner. Lastly, it refers to the exercise of the powers of a

[757] Section 252 of the 1973 Act.
[758] *Bayless v Knowles* (2010) (4) SA 548 (SCA).
[759] Section 163 (1) of the 2008 Act. The issue of who has *locus standi* to utilise the oppression remedy has been analysed. An article by Oosthuizen and Delport, "Rectification of the Securities Register of a Company and the Oppression Remedy" (2017) *Tydskrif vir Hedendaagse Romeins-Hollandse Reg* 228-252 at 230,251, dealt with the issue of whether a party claiming a right to be entered into the register of shareholders of a company who is not indicated as a shareholder has the right to bring an application to court in terms of the oppression remedy against the company to rectify such a register to be registered as a shareholder. It was found that historically a party needed to be a member of the company and not necessarily a shareholder. However, currently section 163 of the 2008 Act is clear that only a shareholder or a director may apply for relief under the provisions of the oppression remedy. It is stated that the 2008 Act does not provide for an extended definition of what constitutes a member or discretionary standing as in the UK. It is stated that under the 2008 Act the scope of the derivative action has been extended in respect of who has the right to utilise it. The scope includes not only shareholders, but parties to be registered as shareholders, directors, prescribed officers of a company, trade unions and representatives of employees of a company. Furthermore, the court has the discretion to grant standing to any person where it finds it necessary to protect the legal right of such a person. In an LLM dissertation by Abbey, titled "An Insightful Study of the Oppression Remedy under South African and Canadian Corporate Law (2012), and submitted to the University of Western Ontario, Canada 54,60,90,91,105, the application of the appraisal remedy as it applied in South African jurisdiction is criticised. It is provided that the appraisal remedy under section 163 of the 2008 Act places the South African jurisdiction in a predicament, since South Africa has limited its oppression remedy to the interests of shareholders and directors, because the statute does not clearly set out the duties for each individual and strict application of the statute. It is advised that the reason for this is that when discussing the duties and rights of a shareholder or a director, the first point of reference is the memorandum of incorporation and only after this one considers whether the provisions in the memorandum of incorporation comply with the statute. It is advised that this predicament originates from the 1862 Companies Act, specifically under section 18, where it is provided that shareholders are the corporation, whereas this is not true; shareholders are separate from the corporation, which is a juristic person. Also under section 11 the governing document of the company was not a statute but a statute-based contract. The statute failed to clarify that the reason why the company exists is not the contract but the statute. It is advised that the *Salomon v Salomon* case did clarify this position by directing one to the statute as the first point of reference through which the company was created. However, the *Burland v Earle* case emphasised the predicament and the South African jurisdiction followed this procedure because of the influence of English company law. It was suggested that the binding aspect of the memorandum of incorporation be removed.

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director or prescribed officer of the company or person related to the company in an oppressive manner.[760]

The key element in all of this is unfairness. In the case of *Scottish Co-operative Wholesale Society Ltd v Meyer*,[761] the plaintiff, which is a holding company, deliberately utilised its controlling power to deprive its subsidiary company from carrying on business. The subsidiary company was manufacturing rayon. The holding company's intention was to make sure that the business of the holding company was transferred to one of its departments instead of the subsidiary. This act of the holding company led to the subsidiary's breakdown of business and dwindling share prices. The minority shareholders were granted relief on the ground that the act of the holding company in question had effectively been carried out by its nominees on the board, which was against the interest of the company.

A minority shareholder seeking to use the oppression remedy as relief must not only prove that there was conduct or an act by the majority shareholders, but that the act of these majority shareholders was unfairly prejudicial or oppressive towards him as a shareholder. Furthermore, he must prove that the majority shareholders unfairly disregarded his own interests as a minority shareholder in the company.[762] In a case where there is voting in respect of a fundamental transaction, the minority shareholder would have to establish unfairness and lack of fair dealing. These acts will be noted in instances where majority shareholders merely use their greater voting power in an unfair manner to prejudice the minority. It can also be noted where majority shareholders use this voting power knowing that it will exclude minority shareholders from running the business of the company.[763]

However, it should be noted that not all actions by majority shareholders that are against the will of minority shareholders will be regarded as oppressive or unfair. It is a known fact that whenever shareholders, including the minority, form part of a company they will be ruled by the will of the majority, as highlighted in paragraph 4.3.2 Minority *shareholders protection*, above. It is submitted that an honest vote by majority shareholders that stifles the interests of minority shareholders will not be

[760] *Ibid*.
[761] [1958] 2 All ER 66, [1959] AC 324, House of Lords.
[762] Cassim *supra* n329 at 757.
[763] *Barnard v Carl Greaves Brokers (Pty) Ltd* 2007 JDR 0047 (c) 2.

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regarded as oppressive. Therefore any action brought by the minority that is based on the fact that decisions are always going against them in the company or that they are always outvoted in meetings would not be justifiable on the basis of oppression in court.

The writer submits that the above discussion highlights that it will be difficult for minority shareholders to block a proposed fundamental transaction that they are against. Minority shareholders would have to go along with the adopted resolution on a fundamental transaction. Therefore, with the suppression of minority concerns comes the success of fundamental transactions. The writer submits that this proves that in terms of the purpose of this research the position prior to the introduction of the appraisal remedy was better, since it prevented fundamental transactions from being hindered by shareholder protection rules.

The reason is that the oppression remedy is complex, since an applicant is required to prove an element, whereas under the appraisal remedy dissenting shareholders need not prove anything to get the court to order a company to pay the fair market value of their shares, bearing in mind that such an order by court may result in a company being out of pocket and ending up abandoning the proposed fundamental transaction.

The dissenting shareholder under the oppression remedy needs to prove that there was prejudice on the part of the majority shareholders of the company. This proves to be difficult, since the approval of a proposed fundamental transaction would have been obtained through fair voting. This is in favour of the proposed transaction if it means that paying the fair market value of the dissenting shareholders' shares would have made a company abandon the transaction as a result of being out of pocket. Under the appraisal remedy the dissenting shareholders do not need to prove anything, merely to carry out the exercise appraisal process, as indicated in paragraph 4.2.2.1 *On the scheme of arrangement*, above.

The reason for this is that it could come to a point where the court becomes involved and makes an order that dissenting shareholders be paid what it regards as a fair market value of their shares, which ultimately results in a company being out of pocket and abandoning the proposed fundamental transaction. The oppression remedy that existed prior to the appraisal remedy requires proof of prejudice by a company against

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the dissenting shareholders for a court to even make such an order, which is difficult to prove if the fundamental transaction was approved by fair voting of majority shareholders.

It is against the above background again that the appraisal remedy was introduced in the 2008 Act. The appraisal remedy as indicated in paragraph 4.2.1 Origins, above provides a way out of a company as opposed to the oppression remedy, where the minority shareholder is still locked in the company with the same majority shareholders he finds oppressive. However, this does not mean that a minority shareholder cannot exit the company by using other remedies. Even with the oppression remedy a minority shareholder can still exit a company that he does not want to be part of anymore or request a court to order the company in question to be wound up.[764] However, it is submitted that the court will be reluctant to grant such an order, as it will be applying the same oppressive conduct to the majority shareholders that it is trying to rectify as per the powers given to it by the statute.

4.3.2.2 Derivative action[765]

Derivative action is one of the remedies that were available to shareholders prior to the introduction of the appraisal remedy in the 1973 Act. Even though derivative action

[764] Section 252 (3) of the 1973 Act.

[765] Du Plessis "The South African Statutory Derivative Action: Background, Comparisons and Application" in Hugo and Kelly-Louw (ed) Jopie: Jurist, Mentor, Supervisor and Friend: Essays on the Law of Banking, Companies and Suretyship (2017) 261-281 at 264, 274, 280-281. This article analyses South African derivative action. It is pointed out that section 165 of the 2008 Act provides a far wider remedy than section 266 of the 1973 Act. It is stated that there is little doubt that the provisions of section 165 of the 2008 Act are based on provisions provided in section 236-239 of the Australian Companies Act, although there are some significant differences, namely the drafting of the provisions, the terminology used and some other vital aspects. An example of this is the fact that section 165 of the 2008 Act provides that a trade union that represents the employees of a company or another representative of the employees of the company also has the right to serve a demand upon a company to commence or continue legal proceedings or take related steps to protect the legal interests of the company, which can trigger statutory derivative action if the demand is not met and the court approves the commencement of the derivative action. Furthermore, it is provided that the fact that South African courts for good reason use Australian precedents in interpreting section 165 of the 2008 Act supplements the fact that this section is taken from the Australian Companies Act. However, it is noted that in the case of *Mbete v United Manganese of Kalahari (Pty) Ltd* [2017] ZASCA 67 the Supreme Court of Appeal emphasised the importance of the differences between the Australian and South African derivative actions and that the derivative action in the 2008 Act has the potential to be an effective remedy for the parties who have standing to bring such an action. Lastly, it is indicated that the discretion of the court to refuse or grant leave for the statutory derivative action provides a safeguard against frivolous and vexatious actions, which have the potential to be disruptive for corporations to do what they are meant to do, for example to conduct business and create long-term sustainable growth for these corporations. Therefore, when corporations conduct business with this in mind and act responsibly that will not only be in the best interests of society but will also contribute to economic prosperity for their countries.

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was brought on behalf of a company by a member, it was also for the benefit of the shareholders themselves,[766] since what is in the best interest of the company is also in the best interest of the shareholders, apart from other stakeholders.[767] This view is based on the fact that what affects the company affects the shares of the shareholders. The action would normally be brought by any member on behalf of a company to protect the legal interests of the company or assert the right of the company.[768] As indicated above, the board of a company has to act in the best interest of the company, which means that it has the authority to institute legal proceedings on behalf of the company. However, failure of the board to proceed with any action would mean that any shareholder within the company can start derivative action to institute such action on behalf the company.[769]

Common law and statutory derivative action under the 1973 Act could only be brought by a member where the company in question had suffered damage or loss or was denied any benefit as a result of wrong done to the company or a breach of trust by the director or officer of the company.[770] It is duly noted that such actions would not have been given consent and not acted upon by the company in question.[771] The 2008 Act as an improvement provides notable additions to statutory derivative action. This is because the 2008 Act has broadened the scope of common law and statutory derivative action under the 1973 Act as a remedy, since it abolished the limited

[766] Section 266 of the 1973 Act.
[767] For the purpose of this study the researcher will focus on the shareholder.
[768] Cassim *supra* n329 at 775.
[769] In an article by Du Plessis, "Company Law Developments in South Africa: Modernisation and some Salient Features of the Companies Act 71 of 2008" (2012) *Australian Journal of Corporate Law* 46-71 at 58-64, it is indicated that whenever a company decides to enter into a transaction apart from other instances, should it be found that the latter does not meet the liquidity and solvency test, parties affected by this can rely on derivative action for corrective measures under section 163(3) of the 2008 Act. It is indicated in this article that other parties that are affected by this will have to rely on other remedies than derivative action. It is provided that creditors cannot institute an action against directors for loss or damages suffered as a result of consequences because of the liquidity and solvency test not being satisfied. Furthermore, it is stated that section 218(4) of the 2008 Act seems to be wide enough to accommodate actions that could be brought by creditors against directors when the solvency and liquidity test is not satisfied. It is indicated that the Australian company law as well is most likely to follow suit and utilise sections that are broad enough for multiple parties to bring an action where a company has been wronged by directors. Lastly, it is highlighted that since the injunction remedy section 20(4) of the 2008 Act is not linked to the damages and loss remedy under section 218(2) of the 2008 Act, third parties in South Africa will be able to claim for damages or loss suffered in circumstances where no injunction is sought.
[770] Section 266 of the 1973 Act.
[771] Cilliers *supra* n753 at 300.

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common law and statutory derivative action under the 1973 Act [772] and the rule provided under the case of *Foss v Harbottle*. Statutory derivative action under the 2008 Act now allows a director, a shareholder,[773] a prescribed officer,[774] a registered trade union representing the employees or another employee representative,[775] or any other person with the leave of the court to institute legal action to protect the interests of the company.[776]

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[772] Section 165 (1) of the 2008 Act. In an article by Keay, "Assessing and Rethinking the Statutory Scheme for Derivative Actions under the Companies Act 2006" (2016) *Journal of Corporate Law Studies* 39-68 at 41-43, 51-53, it is stated that derivative action merely exists to hold directors and managers accountable for their actions while in their posts. Furthermore, it can function as a way of strengthening the process of monitoring directors by shareholders, since instead of shareholders only complaining about directors' actions, they can do more. In addition, it is provided that if the derivative action is successful, this can lead to the company being compensated in relation to the wrong that has been done to it. Lastly, it is stated that the action can permit something to be done, especially if there is a dispute within the company about what the directors of the company have done. However, it is provided that this can always be seen as interference in the management of the company and that courts in the UK are careful about interfering in the internal affairs of a company unless there are very good grounds for doing so. It is stated that there are obviously grounds to require that a shareholder should obtain permission before continuing with derivative action. It is submitted that without this requirement a number of proceedings could be commenced requiring the company to address them all, which will result in unreasonable cost and time, leading to partial paralysis of a company's operations. It is stated that this requirement contributes to the position in the UK that there should not be interference in the management of companies generally and if there is interference, there must be substantial reasons for it. It is submitted that legislation should provide that an application could be made by anyone who appears to the court to be interested in the company and then the court will decide whether the person has a direct financial interest in the affairs of the company or a particular legitimate interest in the way that the company is being managed. It is provided that this would ensure that the floodgates would not be opened as far as applications are concerned. Lastly, it is stated that it is not a good state of affairs that case law has decided that multiple derivative actions may be brought by a shareholder under common law but not under the statutory scheme. It is argued that the statutory scheme was designed to deal with derivative actions in general and obviously fails to do so as far as multiple derivative actions are concerned. It is advised that this causes confusion and leads to the existence of two parallel schemes with different principles, which is not helpful.

[773] Section 165 (2) (a) of the 2008 Act.

[774] Section 165 (2) (b) of the 2008 Act.

[775] Section 165 (2) (c) of the 2008 Act.

[776] However, section 20 (2) of the 2008 Act provides that if a memorandum of incorporation restricts, limits or qualifies the purposes, activities or powers of that company, or even limits the authority of the directors to perform an act on behalf of the company, the shareholders by special resolution may approve any action by the company or the directors that is inconsistent with any such limit, restriction or qualification. It is submitted that if this section were to be applied to limit the powers of the shareholders or directors to bring an application to the High Court on behalf of the company, it would not succeed. The reason is that section 20(3) of the 2008 Act provides that any action that is contemplated in terms of section 20 (2) of the 2008 Act may not be approved if it is in contravention of the 2008 Act. This means that since section 165 is law and grants shareholders and directors powers to bring an application on behalf of a company to protect the interest of the company, these rights cannot be limited in the memorandum of incorporation. Also, in comparison, section 232 of the Australian Corporations Act provides that a court may make an order which it deems fit as per the provisions set out under section 233 to stop any proceedings if the conduct of a company's affairs, or an actual or proposed act or omission by or on behalf of a company or a resolution or proposed resolution of members or a class of members of a company is either inconsistent with the interests of the members as a whole or is oppressive, unfairly prejudicial or discriminatory towards the members or a member, whether in that capacity or another capacity.

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However, the court will only grant leave if it is of the opinion that such an action is necessary to protect the legal interest of the company as claimed by the applicant.[777] Furthermore, the action in terms of the 2008 Act as opposed to the 1973 Act poses less hindrance and less financial encumbrance, since the applicant only needs to make a demand to the company in question[778] and that company itself is the one that takes the necessary steps to redress the damage by appointing an independent expert to investigate the matter and report back to the board.[779] Only when the application is rejected can the applicant apply to court to enforce the action.[780] Irrespective of this, the applicant has the option of bypassing demand on the company to investigate if it is confirmed that the damage caused to the company would be irreparable or for the purpose of this research would result in substantial prejudice to the shareholder if there is delay in bringing the application.[781]

This is one of the protection remedies provided to shareholders under the 1973 Act.[782] The writer submits that even though the derivative action is brought on behalf of the company,[783] it is also in favour of the shareholders in light of the fact that what is in the best interest of the company is also in the best interest of the shareholders as owners of the company, as indicated above. However, the writer submits that the derivative action applied under fundamental transactions was not of much assistance to minority shareholders, since a shareholder could initiate proceedings against a director or officer or past director, but not against another shareholder. For the purpose of this research, fundamental transactions are adopted in terms of a resolution that is voted on by majority shareholders. However, derivative action under the 2008 Act did not have this limit. Also, under the 1973 Act the company would have to suffer damage or loss as a result of the proposed fundamental transaction, which would prove to be difficult if the transaction has not been implemented.

As one of the shareholder protection rules highlighted above, if one considers whether this measure has the potential to frustrate the realisation of a fundamental transaction,

[777] Section 165 (2) (d) of the 2008 Act.
[778] Section 165 (2) of the 2008 Act.
[779] Section 165 (4) of the 2008 Act.
[780] Section 165 (5) of the 2008 Act.
[781] Section 165 (6) of the 2008 Act.
[782] Section 266 of the 1973 Act.
[783] Cassim *supra* n329 at 775.

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it is clear that it certainly does not have this potential. Furthermore, it would not serve as a good shareholder protection method in takeovers.

4.4 Concluding remarks

The writer submits in light of the above that the right to appraisal promulgated in the 2008 Act was borrowed from the appraisal remedy that applies in the USA. This remedy is not South African in origin, since it was not created in South Africa. This appraisal remedy applies differently to different states in the USA, where some states apply the Model Business Corporation Act and others the DGCL. The South African remedy was found to be a combination of both these statutes.

4.4.1 Appraisal right

It is submitted that the exclusivity of the right to appraise does not apply in South African jurisdiction as opposed to its counterparts from which the right to appraise was adopted. From the discussion above, it is clear that in some jurisdictions such as the USA the appraisal remedy is seen as a solution to ensure that the company is enabled to engage in a fundamental transaction without dissenting shareholders halting the process. It is evident from the discussion on these jurisdictions that the right to appraise is an exclusive means and that other remedies available to dissenting shareholders are not applicable until the appraisal remedy has been exhausted, especially in instances where a company is engaging in fundamental transactions that are seen as being in the best interest of the company. This therefore disregards the other remedies[784] that could frustrate the realisation of a prospective fundamental transaction.

However, even if the South African appraisal remedy should serve as an exclusive right under fundamental transactions as opposed to the other available remedies, it is submitted in view of the discussion above that it has the potential of frustrating the realisation of fundamental transactions. This is because when a company proposes a fundamental transaction it is possible that many of its shareholders may exercise their right to appraise, thus causing liquidity problems for the company and forcing the

[784] Examples of these remedies could be a civil action or court approval in terms of section 115 of the 2008 Act.

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company to abandon the proposed fundamental transaction. This was the core of this chapter.

Furthermore, it was highlighted that the main objective of the appraisal remedy is to make sure that the majority shareholders are able to proceed with the proposed fundamental transaction without being blocked by the minority shareholders. At the same time the minority shareholders who are against the proposed fundamental transaction are provided with the solution of leaving the company and not going along with the proposed fundamental transaction. However, the writer submitted that even if the appraisal remedy attempts to satisfy both the majority and minority shareholders, the fact remains that the proposed fundamental transaction voted in favour of by the majority of shareholders is unlikely to succeed. The reason for this is that the company concerned is unlikely to be able to afford to finance the proposed transaction as well as pay the fair market value of all the dissenting shareholders' shares. This will inevitably lead to the company abandoning the proposed transaction, as entering into the transaction is not legally binding like the obligation to pay the fair market value of the dissenting shareholders' shares, especially if the dissenting shareholders are not satisfied with the offer made by the company for their shares and these shareholders approach a court for a fair determination.

It is thus clear that prior to the enactment of the right to appraise in the 2008 Act there was no frustration of realisation of fundamental transactions in regard to the element that the right to appraise brings, which is being out of pocket. This was effected through the shareholder protection rules that were already available to shareholders at the time. Supplementing the submission above is the fact that the appraisal remedy was not resolving a problem that the South African jurisdiction was encountering at the time, except to harmonise South African company law with international standards. South Africa wanted to promote investment in its economic markets and ensure that the interests of minority shareholders were protected and therefore introduced the right to appraise.

4.4.2 Oppression remedy

It is also clear from the earlier discussion that the oppression remedy serving as a position prior to the appraisal remedy had little or no effect in frustrating the realisation of fundamental transactions. The reason for this is that whenever minority

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shareholders were not in agreement with majority shareholders' vote in favour of a fundamental transaction resolution, they could only use the oppression remedy if there was an allegation of "foul play" in the voting process, which resulted in minority shareholders suffering some form of prejudice. If no foul play had taken place, minority shareholders had to abide by the decisions of the majority. In contrast to the appraisal remedy, the minority shareholders who had a different opinion from the majority could not halt a transaction unless there was prejudice on the side of the minority.

4.4.3 Derivative action

The common law and statutory derivative action under the 1973 Act, serving as one of the remedies that were available to minority shareholders prior to the introduction of the appraisal remedy in the 2008 Act, likewise had little effect on frustrating the realisation of fundamental transactions, as it did not serve as an effective shareholder protective measure under fundamental transactions. The common law and statutory derivative action under the 1973 Act could be initiated against a director or officer or past director but not against another shareholder. For the purposes of this research, fundamental transactions are adopted by majority shareholders and the fact that proceedings could not be brought against them under this remedy meant that it could not halt fundamental transactions.

In light of the aforementioned discussion, as well as preceding chapters, Chapter 5 will provide some conclusions and recommendations on how the position in South Africa can be enhanced to find the right balance between the shareholder protection rules and fundamental transactions.

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CHAPTER 5

Conclusions and recommendations

5.1 Introduction

This thesis set out to highlight the conflict between two rules, namely shareholder protection rules on the one hand and fundamental transaction rules on the other hand. These are rules that promote two separate purposes of the 2008 Act: (1) the development of the South African economy[785] and (2) the promotion of investment in the South African markets.[786] These rules were incorporated into the South African corporate law jurisprudence from different jurisdictions across the world.[787] Some light was also shed on the conflict between these two rules, which tends to frustrate the realisation of the intended purpose of the rules.[788]

The main purpose of this study was to argue that South Africa needs to adopt a takeover legal system with characteristics that are unique to the South African context, while at the same time catering for market practices. The following research question connected to the main purpose was answered by the analysis in this thesis:

(1) Whether the 2008 Act struck the right balance between facilitating business restructuring through fundamental transactions and shareholder protection.[789]

Apart from the stated central focus of this thesis, it also intended to gather knowledge from different jurisdictions across the world in order to provide an analysis on whether the 2008 Act's provisions regarding takeover rules are aligned with international

[785] See S.7 of 2008 Act as well as discussion in paragraph 4 of Chapter 1.
[786] *Ibid.*
[787] The jurisdictions that were analysed in the entire research are the USA in consideration of the fact that there are states that apply the Model Business Corporation Act and those that apply the Delaware General Corporation Law. Other jurisdictions that were analysed are the UK and India as part of the common law family.
[788] This was also indicted in paragraph 4 of Chapter 1.
[789] This was discussed in paragraphs 3 and 4 of Chapter 1.

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trends. This is in line with one of the purposes of the DTI policy guidelines (the precursor to the 2008 Act), which was to ensure compatibility and harmonisation with the best practice jurisdictions internationally.[790]

A summary of the findings from this thesis will now be discussed.

5.2 Findings

5.2.1 Influence of shareholders' protection provisions[791]

In Chapter 2 the influences of takeover rules and their objectives were discussed and the conflict between shareholder protection and fundamental transaction rules was highlighted. It was found that the South African landscape codified rules that could be traced back to jurisdictions such as the UK and the USA.[792] The result of this was a concoction of conflicting takeover rules adopted from different jurisdictions that were invented with differing objectives in mind.[793]

In the discussion it was shown that South African company law had gone through several reforms since its inception. However, what was of importance was the fact that these reforms in their initial phases were influenced mostly by colonial law, since South Africa used to be a colonial state under the rule of England.[794] Therefore, this also meant that South African company law before the 1973 Act underwent continual change that was cultured by socio-economic advances and development in the UK.[795] It is evident that South African company law borrowed and incorporated principles and developments largely from the UK.

In light of the aforementioned, India as a former country of the British Empire was chosen as part of the common law family, like South Africa, which followed English law as its foundational system. It was found that the position in India was similar to that of the South Africa, especially in respect of the influence of takeover regulation. Even after decolonisation in 1947 the influence of colonial laws continued in Indian company law legislation.[796]

[790] This was also indicated in paragraph 4 of Chapter 1 of this study.
[791] This was discussed in Chapter 2.
[792] This was highlighted in paragraph 2.4.4 of Chapter 2.
[793] This was discussed in paragraph 2.5 of Chapter 2.
[794] This was discussed in paragraph 2 of Chapter 2
[795] This was highlighted in paragraph 2.2 of Chapter 2.
[796] This was discussed in paragraph 2 of Chapter 2.

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It was found that takeover rules in the UK were influenced by professionals who were involved in takeovers and who acted as institutional investors.[797] The result was that these institutional investors as shareholders at the time looked only after their own interests and thus better shareholder protection was crucial, which is evident even today in the UK.[798] It was also found that the reason why institutional investors lobbied for stronger takeover regulation protection to regulate hostile takeovers was that investors as shareholders were no longer given an opportunity to decide on bids. This exclusion of shareholders from deciding was based on the fact that management started to apply defensive actions against bids. The reason for this was that bidders at the time had started to replace management with their own preferred management in companies of which they took control.[799]

In contrast to the position found in the UK, the USA has developed takeover regulation on state level reflecting the opinions and views of those who are professionally involved in takeovers. The approaches, however, are different because the UK uses a more shareholder-centric approach whereas the USA uses a more board-centric approach.[800] In the USA there are also differences of influence for takeover regulation on both federal and state level. It is clear that most US states passed anti-takeover laws in response to the appeals of companies that claimed that they were under threat of takeovers and wanted some kind of protection. This was done by most states in 1982 and 1989. The boards of the target companies specifically had more influence in the development of takeover rules in the USA.[801] It was also found that the states' response to takeovers was influenced by the fact that states were looking to maximise the number of companies that were incorporated within their jurisdictions and therefore managerial preferences were of great concern to them. As a result, they passed anti-takeover laws that offered more protection against takeovers. The intention was to attract more companies that could be incorporated and thus resulted in role players within the corporate space shaping takeover regulations in the USA.

The position in South Africa regarding the development of takeover rules is in stark contrast, as role players or professionals in the South African takeover domain were

[797] This was indicated in paragraph 2.4 of Chapter 2.
[798] See paragraph 2.5 of Chapter 2.
[799] See end of paragraph 2.1 of Chapter 2.
[800] See paragraph 2.5 of Chapter 2.
[801] This was discussed under paragraph 2.5 of Chapter 2.

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not involved; the legislation was rather a result of replicating English law as in the earlier developmental phases.[802] It is also clear that owing to the alignment of South African company law with international trends at the time,[803] these rules where absorbed from takeover provisions from other jurisdictions.[804] Participants in the South African 2004 corporate law reform process were consequently guided heavily by developments in foreign jurisdictions[805], which led to some of the rules in the 2008 Act having very distinct foreign characteristics.[806]

The 2008 Act still kept this umbilical cord as well: the provisions that applied in the 1973 Act were retained in the 2008 Act. As discussed above, the 2008 Act merely incorporated rules that were influenced by foreign jurisdictions rather than approaching matters like its counterpart, India, which through its various reforms of Indian company law ended up with the 2013 Companies Act. This Act was formulated in response to problems that were unique to India's corporate setting and local conditions and not an absorption of rules from foreign jurisdictions. India, in taking this decision, also decided to stop following English court judgments, whereas in South Africa English court judgments still have a huge influence.[807]

Although it was established that shareholder protection rules from the USA and the UK were influenced by a different objective and interests, South Africa nonetheless incorporated shareholder protection rules from both these jurisdictions.[808] This could be the reason why shareholder protection rules in the 2008 Act taken from differing jurisdictions conflict with fundamental transactions rules as hypothesised in paragraphs 1.3 and 1.4 of Chapter 1. This leads to the next findings on how shareholder protection rules conflict with fundamental transaction rules.

[802] See paragraph 2.2 and 2.5 of Chapter 2.
[803] This was indicated in paragraph 1 of Chapter 1.
[804] For example, the appraisal remedy from the USA and the mandatory offer remedy from the UK. In turn this answered one of the purposes of this study, which was to highlight if South African takeover laws were aligned with international trends, since one of the purposes of the DTI policy guidelines were to ensure compatibility and harmonisation with best practice jurisdictions internationally.
[805] This was discussed in footnote 130 of Chapter 2.
[806] See paragraph 2.4.4 of Chapter 2.
[807] This satisfied one of the purposes of this study: in as much as it is important to regulate the South African takeover market with a set of well-designed takeover rules, it is also important to recognise that it needs to adopt a takeover legal system with South African characteristics that caters for its market practices. This is also discussed under the recommendations of this study in paragraph 5.3.1 of this chapter.
[808] This was highlighted in Chapters 3 and 4.

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5.2.2 Approval by shareholders and court[809]

5.2.2.1 Shareholders' approval

In Chapter 3 it was found that shareholder approval as a protection measure has the potential to frustrate the realisation of a proposed fundamental transaction because technical procedures are involved whenever shareholder approval resolutions are obtained through a meeting. These procedures cause delays, which may result in the frustration of a proposed fundamental transaction, especially if that fundamental transaction is time-constrained.[810] This may be the case especially when one considers the fact that the 2008 Act requires that for the approval of a fundamental transaction, a special a meeting has to be called for that purpose. The default notice for such a meeting for all types of companies is not less than 10 days[811] but this notice period may be increased or reduced in a company's MOI.

However, a reduced notice period appears to be impractical when considered from an institutional investor perspective. In view of the fact that the 2008 Act requires all shareholders to be present at a meeting and some institutional investors' headquarters may be based on a different continent from the one of the proposed meeting venue, it may be impossible for such shareholders to be present at the meeting at such short notice. It such a case it makes sense to increase the notice period to cater for logistical purposes in instances that include institutional investors.[812] Also, the 2008 Act provides for instances where shareholders meetings can be conducted electronically unless the MOI expressly prohibits this.[813] However, a notice period for such a meeting still has to be complied with which adds to the delay as opposed to the solution proposed in paragraph 3.2.3 of Chapter 3 and paragraph 5.3.2.1 below.

It is also evident that the 2008 Act provides for alternative instances where shareholders may vote on a resolution other than being physically present in a meeting and the 2008 Act thus requires resolutions to be submitted within 20 days.[814] The writer submitted that this caused an increase in the delay from the notice period of 10 days required to convene a meeting to 20 days of submitting resolutions. It was

[809] This was discussed in Chapter 3.
[810] This was discussed in paragraph 3.2.3 of Chapter 3.
[811] See section 62(1) of the 2008 Act.
[812] This was highlighted in paragraph 3.2.3 of Ch. 3.
[813] See section 61 (10) and 63 (2) of the 2008 Act.
[814] See section 60 (1) of the 2008 Act.

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consequently concluded that an acquiring company engaged in a time-constrained fundamental transaction may end up having second thoughts about the proposed transaction because of the delay caused by the legal procedures that have to be complied with. It was further submitted that this may lead to buyer's remorse, causing the acquiring company to abandon the proposed fundamental transaction and look for other alternatives.[815]

It was also found that the South African approach, in contrast to the US approach to the approval requirement for a merger, causes delay and could place the certainty of the deal at risk, as such a delay could possibly encourage buyer's remorse about the proposed transaction. The effect of this could be that potential buyers could pursue alternative offers after dropping out of the initial deal, as the delay in the approval requirement may be between two and three months, even up to five or six months, depending on the swiftness of the process as well as the host of other activities that should be completed.[816]

In India and the UK a court or tribunal, especially when it concerns a scheme of arrangement after one of the parties makes an application, provides the terms for holding a meeting, where shareholders can vote in respect of a proposed fundamental transaction. This was also the position in South Africa prior to the 2008 Act. Notwithstanding this incorporation, it appears delays could be encountered, as court proceedings can take time. The only way to circumvent this effect is to bring an application to the High Court on an urgent basis rather than taking it up with the tribunal. In the UK, however, especially in mergers, it was found that the shareholders' approval requirement is not requisite in certain circumstances, with the objective of curbing delay, as discussed above.[817] This is allowed in circumstances where a transferee company is absorbing another transferor company with all of its shares in terms of a merger, as well as instances where more than one transferor company are

[815] This highlighted the main focus of this study, which was to highlight the frustration of the realisation of fundamental transactions by the shareholder protection rules. In this particular instance the shareholders' approval requirement was utilised as one of the shareholder protection rules under takeover rules that tend to frustrate proposed fundamental transactions. Also, it highlighted how when there is realisation of a shareholder protection rule, there is transgression of a fundamental transaction as a sub-purpose of the main focus, which is to shed light on how the conflict between the two rules as indicated above tends to frustrate the realisation of what these very rules are intended for. Furthermore, this fulfils one of the purposes of this study, which is to contribute to the existing body of knowledge, particularly in respect of the takeover law regime in South Africa, but from a conflict of rules perspective.
[816] See discussion in paragraph 3.2.3 of Ch. 3.
[817] See section 917 of the UK Companies Act of 2006.

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being absorbed by the transferee and all these companies' shares are held by the transferee company.[818]

Furthermore, in the UK this is allowed in instances where the court for one is satisfied that the publication of a notice of receipt of the draft terms of the merger by the registrar took place in regard to all the merging companies at least one month before the date of the courts' order. Secondly, it is allowed if shareholders of the transferee company were able to inspect copies of the merger documents in respect of both merging companies and to obtain copies of such documents on request free of charge one month before the merger at the registered office of the transferee company.[819]

Lastly, one or more shareholders in the transferee company who happen to hold together not less than 5% of the paid-up capital of the company and carried the right to vote at the meeting of the company would have been able to require a meeting of each class of shareholders to be called for the purpose of deciding on whether or not to agree to the merger proposal.[820]

In addition to the findings above, it was found that the 2008 Act in terms of its special resolution favours shareholder protection rather than increasing the chances of having more successful fundamental transaction proposals. Compared to takeover regulations in the jurisdictions discussed, the South African jurisdiction takeover regulations provide for a higher default threshold for approving a fundamental transaction than the jurisdictions discussed.

It was also found that despite the fact that the 2008 Act provides that the default threshold for a special resolution may be decreased, it was still higher than the thresholds provided in the jurisdictions discussed: the 2008 Act's default special resolution threshold is 75% of voting rights that can be decreased to not less than 60%.[821] This is compared to the 25% of the Model Business Corporation Act and the 50% of the DGCL.[822]

The measure of greater protection for shareholders in the 2008 Act was found even in the fact that under the DGCL a special resolution is not required for the sale of assets

[818] See discussion in paragraph 3.2.3 of Chapter 3.
[819] See discussion in paragraph 3.2.3 of Chapter 3.
[820] *Ibid.*
[821] This was shown in paragraph 3.2.3 of Chapter 3.
[822] *Ibid.*

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in a company unless it is for a sale of all the assets of the company. However, under the 2008 Act it is required for even a greater part of the company being sold. It was submitted that the USA had far more experience as far as takeovers are concerned than South Africa. The reason for the USA being less stringent in respect of shareholder protection in such fundamental transactions could be to balance the success of fundamental transactions with shareholder protection.

The above findings were compared with the position in the UK and it was found that a special resolution is not required to approve asset disposal in an unlisted company. This is because asset disposals in the UK are not subject to takeover regulations. In terms of mergers, it was also found that even though the special resolution threshold is similar to that of the South African jurisdiction, in the UK the quorum is at least two persons, making it easier to reach a decision in favour of the proposed transaction than when applying the 25% of all the voting rights required by the 2008 Act.

5.2.2.2 Court approval

In this section of Chapter 3 it was found that court approval as a protection measure under fundamental transactions has the potential to frustrate transactions. It was found that the South African jurisdiction adopted the statutory merger provision from the USA but court approval provisions in a statutory merger under the USA do not apply as they do in South Africa. It was found that an appraisal right applies as a shareholder protection measure in a statutory merger in the USA, whereas in South Africa court approval does apply as a shareholder protection measure in a statutory measure apart from the right to appraise.[823]

As a result of the above, it was found that a US statutory merger can easily be effected without hurdles simply with the approval of the prescribed majority as per the company's MOI and without the need for the court to approve the proposed transaction. If needs be, dissenting shareholders have the right to opt out of a company by withdrawing the fair market value of their shares in cash without seeking recourse to a court. It was found that this provides a balance between protecting minority shareholders and the decisions of majority shareholders.[824]

[823] This was discussed in paragraph 3.3.2.3 of Chapter 3.
[824] *Ibid.*

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In contradistinction, it was found that in South Africa any shareholder in a company can seek court approval for a merger and that any shareholder can apply to court to have a company seek the approval of a court for a merger. Furthermore, when 15% of the voting rights were against a fundamental transaction resolution, any shareholder can request the company to obtain court approval. It was found that this subjects the resolution to scrutiny, suggesting that unfairness played a part. The unfairness is related to the same section under section 115(7)(a) and (b), as it is advised that a court may make an order against the resolution if it should find that it was unfair towards other shareholders or the voting was materially tainted, there was conflict of interest, etc.

In the same process it was learnt that court proceedings can take time and be costly, which could easily lead to facilitation and allocation of financial resources to wrong purposes such as litigation rather than the proposed merger, especially where the merger was going to be used as a takeover mechanism. This could put a company out of pocket and unable to proceed with the proposed merger.[825] It was found that this is unlikely to be a possibility in the USA, as the appraisal remedy that applies, as discussed above, is not a court-driven process. The court would only be involved when there is disagreement on what constitutes a fair market value of shares.[826]

Furthermore, it was found that the consequences of the costs of court approval may be that a company may opt to abandon a merger simply because the profits that would emanate from the merger are insufficient to justify the costs of litigation in getting court to approve the merger resolution. In comparison with the jurisdictions discussed, it was found that a bidder of a target company is normally expected to abandon a takeover if during litigation it is discovered that the expected returns from the takeover will not justify the marginal costs of continued litigation.[827]

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[825] This highlighted the main focus of this study, which was to highlight the frustration of the realisation of fundamental transactions by the shareholder protection rules. In this particular instance the court approval requirement was utilised as one of the shareholder protection rules under takeover rules that tend to frustrate proposed fundamental transactions. Furthermore, this fulfils one of the purposes of this, study which is to contribute to the existing body of knowledge, particularly in respect of the takeover law regime in South Africa, but from a conflict of rules perspective.
[826] See discussion in paragraph 3.3 of Ch. 3.
[827] This highlighted how when there is realisation of a shareholder protection rule there is transgression of a fundamental transaction, since another purpose of this study was to shed light on how the conflict between the two rules as indicated above tends to frustrate the realisation of what these very rules are intended for.

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With reference to the above, it was found that in the jurisdictions discussed defensive litigation was familiar in respect of takeovers that are contested and that litigation merely served two purposes.[828] One purpose was to delay a bid process with the objective that the bidder would abandon the takeover. With that in mind, it was found that even with the court approval process in South Africa, this could be utilised as a mechanism to frustrate a proposed time-constrained fundamental transaction.

It was therefore found that South Africa ended up with a concoction of conflicting takeover rules adopted from different jurisdictions that were invented with differing objectives in mind.[829] It was found that when the statutory measure was adopted in the 2008 Act, along with the minority shareholder protection measure, which is the appraisal right, the exclusivity of this right in regard to the statutory merger, as is applicable in the USA, was omitted.

It was found that in the USA when the statutory merger was created the best minority shareholder protection rule was the appraisal right rather than any other protection measure. The reason for this is that majority shareholder interests are protected, as the majority could proceed with the proposed merger while the minority shareholders could not stand in the way of the proposed merger but could exit with a fair value of the shares in cash. This balanced both interests in regard to minority and majority shareholders.[830]

From the above it was found that the appraisal remedy seems to be a better solution than court approval for the purposes of this study, even though it has its own disadvantages.[831] It was also found that the provisions under the oppression remedy provide better protection to minority shareholders than court approval.[832] Furthermore, the court approval provisions in the 2008 Act can be accommodated under the oppression remedy, as these shareholder protection measures are similar even though they are not the same. The grounds for seeking an oppression remedy and the court approval measure were compared and found to be similar if not the same. This

[828] The second purpose is to create delay in the bid process so that the board of the target company can think of other defensive measures or obtain other bidders. This is not relevant for the argument in question.
[829] This was indicated in paragraph 5.2.1 above.
[830] See paragraph 3.3 of Chapter 3.
[831] These disadvantages were discussed in Chapter 4.
[832] This was discussed in paragraph 3.3 of Chapter 3.

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finding was also based on what an applicant for both these remedies may seek as a resolution to the matter raised.[833]

5.2.3 Dissenting shareholders[834]

5.2.3.1 The appraisal right

According to what was stated above in paragraph 5.2.2.2 on the appraisal remedy, rather than minority shareholders blocking a merger, they can find a way out by asking for a fair market value for their shares and letting the majority of the shareholders continue with the proposed merger. However, it was found that the appraisal remedy as a minority shareholders' protection measure has the potential to frustrate the realisation of a fundamental transaction.[835]

The above is because whenever the management of a company propose a fundamental transaction, they are unable to predict if there will be any dissenting shareholders, whether these dissenting shareholders will exercise their right to appraise and if that happens how many will do so. This causes great uncertainty for the management in the company.[836]

This may have serious consequences for a company when the above events are viewed from an economic perspective, for example where a fundamental transaction is proposed and many shareholders of the company choose to exercise their appraisal rights. Such shareholders need to be paid an aggregate sum of the value of their shares in cash. That may cause liquidity problems in a company, which could force it to abandon the proposed fundamental transaction.[837]

Furthermore, it was found that as a result of the above the appraisal remedy failed in providing the perfect balance of protection between majority and minority shareholders, as implied by its main objective, which is to allow the majority to proceed with the proposed fundamental transaction while the minority shareholders opt out of

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[833] For a broader discussion of this view see paragraph 3.3 of Chapter 3.
[834] This was discussed in Chapter 4.
[835] See paragraph 4.2.3 of Chapter 4.
[836] *Ibid.*
[837] For an example of where there is frustration of realisation of a proposed fundamental transaction as a result of the appraisal remedy, see the discussions in paragraph 4.2.3 of Chapter 4 and paragraph 3 of Chapter 1. This highlighted the main focus of this study, which was to highlight the frustration of realisation of fundamental transactions by the shareholder protection rules. Furthermore, this fulfils one of the purposes of this study, which is to contribute to the existing body of knowledge, particularly in respect of the takeover law regime in South Africa, but from a conflict of rules perspective.

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the company by receiving an aggregate sum of the value of their shares from the company. This substantiates the argument that the realisation of shareholder protection rules frustrates the realisation of the fundamental transaction.[838]

It was also found that should dissenting shareholders under the appraisal remedy further challenge the company's offer of what it considers the fair market value of their shares, this may lead to legal proceedings. The financial implications of representation in legal proceedings and the uncertainty of victory in court arise from the possibility of being awarded an order of costs against and confirmation of what the dissenting shareholders consider an aggregate sum of the value of their shares. This could force a company's management to abandon the proposed fundamental transaction, considering the fact that continuing with the proposal may lead to poor allocation of financial resources.[839]

It was found that the appraisal remedy in the 2008 Act as a minority shareholder protection remedy in all fundamental transactions had been absorbed from the USA. It was found that in the USA, especially in states that use the DGCL, it only applies in a merger, not in an asset disposal or a scheme of arrangement as it does in South Africa. This raised suspicion that the creation of an appraisal remedy was not necessarily a shareholder protection mechanism designed for asset disposal and a scheme of arrangement.[840]

It was found that the reasons why it does not apply to all fundamental transactions in the USA are firstly that there is no scheme of arrangement in the USA and secondly, even though there is an asset disposal mechanism, the appraisal remedy does not apply, as it is believed that there are other effective minority shareholder protection mechanisms in place. This submission is similar to the one raised in paragraph 3.2.2.1 in Chapter 3 under approval protection measures, that shareholders' approval does not apply to asset disposals in the USA because it is believed that there are other sufficient mechanisms in place that protect minority shareholders.[841]

It was further submitted that the reason why the USA is less stringent in respect of shareholder protection in such a fundamental transaction could possibly be to balance

[838] See paragraph 4.2.3 of Ch. 4.
[839] *Ibid.*
[840] See paragraph 4.2.2.1 and 4.2.2.2 of Chapter. 4.
[841] *Ibid.*

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the success of fundamental transactions with shareholder protection. Expressly for the purpose of this study, this could serve to limit the frustration of realisation of fundamental transactions by multiple shareholder protection rules. This could be the same reason why the appraisal remedy does not apply in all fundamental transactions in the USA, namely to limit the frustration of fundamental transactions, should it lead to the situations raised in this study.[842]

In supplementation of the above, it was found that appraisal rights in South Africa apply to all merger formations, whereas in the USA, as much as they apply in a merger, especially in states that use the DGCL, they do not apply to all formations of mergers.[843] Perhaps this decision resulted from the fact that they wanted to limit the frustration of the realisation of mergers should those merger proposals face the challenges raised in this study. Appraisal rights in specific merger proposals, for example those that apply to shareholders of the surviving company where their shares are not affected, are seen as a delay in the process; and delay in fundamental transactions can cause buyer's remorse, as highlighted in paragraph 3.2.3 of Chapter 3.

As discussed above, it was found that the appraisal remedy was a result of adopting the statutory merger into the 2008 Act and the right to appraise serving under the said fundamental transaction as a protective measure in favour of minority shareholders. However, prior to this position of the appraisal remedy, there were shareholder protection measures in place that were in favour of minority shareholders. On analysing the position prior to the enactment of the right to appraise, it was found that shareholders' approval, court approval, the oppression or the prejudicial remedy and derivative action served as shareholder protection measures at the time.[844] However, the shareholders' approval and court approval rules were not analysed further, as they had already been discussed in Chapter 3. It was found that court approval rules can be accommodated under the oppression remedy provisions. Because of this and the fact that it had already been analysed, the oppression remedy was discussed further as a position prior to the appraisal remedy.[845]

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[842] See paragraph 4.2.2.1, 4.2.2.2 and 4.2.3 of Chapter 4.
[843] This was indicated in paragraph 4.2.2.3 of Chapter 4.
[844] This matter is discussed more broadly in paragraph 4.3 of Chapter 4.
[845] The oppression remedy was discussed further in paragraph 4.3.2.1 of Chapter 4.

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In this study it was found that the oppression remedy had little effect in terms of frustrating the realisation of fundamental transactions, as opposed to the appraisal remedy, which as highlighted above could put the company out of pocket. It was also found that this came at the cost of compromising the rights of minority shareholders, since they had to go along with the proposed fundamental transaction against which they had voted. This differs from the appraisal remedy's attempts to provide a way out of the company for the minority shareholders by being paid the fair market value of their shares in cash. The right to appraise was probably introduced at a later stage in an attempt to balance the two rules.[846]

The reason for the above is that the oppression remedy had little or no effect in blocking a proposed fundamental transaction, since whenever a minority shareholder used the oppression remedy, he not only had to prove that the majority shareholders had taken action, but also that this act by the majority shareholders was unfairly prejudicial towards him.

Still on the position prior to the appraisal remedy, the common law and statutory derivative action under the 1973 Act was analysed and it was found that it had no effect on the potential of frustrating the realisation of proposed fundamental transactions. This was because the 1973 Act applied prior to the enactment of the appraisal remedy in the 2008 Act. In analysis of the 1973 Act it was found that a shareholder could bring legal proceedings against a director or past director or officer but not against another shareholder.[847]

In fundamental transactions shareholders vote on adoption, which makes it impossible for an applicant who is a minority shareholder to bring an action against the shareholders who have voted in favour of the proposed fundamental transaction, since the common law and statutory derivative action under the 1973 Act does not allow a shareholder to bring legal proceedings against another shareholder, but only against a director or past director or officer of the company.[848]

Furthermore, even if the shareholder brings legal proceedings against the board of directors who proposed the fundamental transaction, in a case where the board of

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[846] See paragraph 4.3.2.1 of Chapter 4.
[847] See paragraph 4.3.2.2 of Chapter 4.
[848] *Ibid.*

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directors are the parties that submitted the merger agreement to the shareholders for consideration, this would mean that the company in question would have to have suffered damage or loss as a result of the proposed fundamental transaction. This would to be difficult to prove, since the transaction at the point of adoption had not been implemented.[849]

5.3 Recommendations

5.3.1 Recommendations on the influence of shareholder protection provisions

It is recommended that the South African jurisdiction learn from all the jurisdictions discussed and that in its corporate law reform processes it should involve business role players, especially in the takeover regulation aspect.[850] However, to prepare the 2008 Act a draft bill was distributed so corporate role players and academics could comment;[851] therefore the position in the USA was considered in drafting the 2008 Act.

The UK has influenced the South African takeover regulation somewhat in respect of investors, apart from the replication issues discussed above. The 2008 Act has shareholder protection rules and this is a result of one of the purposes of this Act, namely the promotion of investment in the South African markets. This is critical in the South African context, as having takeover regulations that protect investors' interests attracts investment to that jurisdiction.[852]

Therefore it is recommended that the shareholder protection rules in the 2008 Act be relaxed so as not to conflict with the fundamental transactions.[853] This is because much work has been done and it was found in this study that shareholder protection rules are aligned with international trends. All of this was done to modernise South African company law so that it could cater for the current business environment in the South African and foreign jurisdictions.[854]

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[849] *Ibid.*
[850] In this study, as indicated above, it was found that in the UK the takeover regulations were mostly influenced by institutional investors in consideration of their interests in companies as shareholders. In the USA their state takeover regulations were influenced by boards of companies. Since states looked to maximise the number of companies that were incorporated in their states, they cared a great deal about managerial preferences.
[851] For example, it was indicated in paragraph 4.2.2.3 of Chapter 4 that the appraisal remedy in its form in the 2008 Act's' draft bill was analysed and criticised.
[852] This was discussed in paragraph 2.2 of Chapter 1.
[853] This is to be discussed further under paragraph 5.3.2 and 5.3.3 of this chapter.
[854] DTI *supra* n1 at 3.

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It is also of significance that these rules have been in practice for some time and have become entrenched in South African practices, considering the fact that they have been applied for at least a decade if not decades and in that over time several amendments have been made to them. Furthermore, in regard to market practices, the 2008 Act did attempt to take into consideration South Africa's corporate setting, since it considered the Constitution[855] as it regulates the relationship between economic citizens and has fundamental implications for company law. Furthermore, the reformed company law needed to be consistent with the Constitution.[856]

In addition to the above, the Competition Act[857] and the Broad-Based-Black-Economic Empowerment Act[858] were considered. The reformed company law's agreement with the Broad-Based Black Economic Empowerment Act was considered as far as effecting economic social change within the South African jurisdiction was concerned.[859] Also considered was the environment in which business is conducted in the South African jurisdiction, taking into account other laws that regulate specific

[855] The Constitution of the Republic of South Africa, 1996.
[856] This was discussed in paragraph 1.1.2 of Chapter 1.
[857] The Competition Act 89 of 1998.
[858] The Broad-Based Black Economic Empowerment Act 46 of 2013.
[859] See paragraph 1.2.2 of Ch. 1.

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features in the corporate sector. These were labour legislation, in particular the Labour Relations Act,[860] the Skills Development Act[861] and the Employment Equity Act.[862]

Even though in the corporate law reform process it was noted that the harmonisation of the 2008 Act with international jurisdictions was desirable, it may not always be appropriate, especially for South African conditions. Harmonisation with major trading partners and the South African Development Community was pursued.[863] However,

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[860] The Labour Relations Act of 1995. Botha "Evaluating the Social and Ethics Committee: Is Labour the Missing Link? (Part 2)" (2017) *Tydskrif vir Hedendaagse Romeins-Hollandse Reg* 1-19 at 10. It is submitted that in the case of fundamental transactions, specifically in the sale of business or mergers, employee involvement is not contemplated in the 2008 Act; rather it is left to the process of consultation in terms of the Labour Relations Act. It is stated that sections 197 and 197A of the Labour Relations Act provide for the transfer of a business as a going concern and the automatic transfer of employment contracts. However, it is also submitted that neither section 197 nor section 197A provides for the disclosure of information or consultation regarding the transfer or undertaking and therefore this should be addressed as a matter of urgency. It is also recommended that the 2008 Act should provide for consultation and disclosure of information whenever transfer of an undertaking as a going concern or a merger occurs. It is highlighted that such a provision would not only adhere to the current solvency and liquidation requisites that must be met whenever there is a merger, which primarily protect creditors of a company, but would extend to employees and provide them with an opportunity of accessing information relating to a proposed merger. In addition to provisions, a notice period should be given to trade unions or employee representatives so workers could be allowed to vote or rather express an opinion on the proposed merger. In Botha "Evaluating the UK's Employee Shareholder Status Provisions in the Context of the South African Position" (2015) *Journal of Contemporary Roman-Dutch Law* 556-576 at 557 the issue of labour relations in the aspect of the 2008 Act is discussed further with the objective of evaluating the introduction of the notion of employee shareholders in the UK in the context of the labour and corporate law framework in South Africa. The 2008 Act brought about major changes to governance with regard to employee participation. It is highlighted that it entrenched specific rights of employees to a point where it extended these employees' rights. Employees are now given meaningful rights of participation in the governance of companies as a matter of company law as opposed to just separate legislation that has to do with labour relations law only. In an article by Botha, "Evaluating the Social and Ethics Committee: Is Labour the Missing Link? (Part 1)" (2016) *Tydskrif vir Hedendaagse Romeins-Hollandse Reg* 580-593 at 583-584 it stated that companies must comply with employee/labour legislation that deals with among others safety and health at work, equal opportunities and related matters. Furthermore, it is stated that employees now have an important role to play in advancing the interests of companies in terms of advancing the interests of the company as a whole. This is demonstrated in various reports based on corporate governance in the South African jurisdiction and the 2008 Act. It is stated that now companies have to take note of the fact that whenever they are making decisions, they need to consider the protection and rights granted to employees by other enactments. These include rights afforded to employees by the 2008 Act itself. It is indicated that the 2008 Act highlights that new rights have been created in respect of employee participation. Previously employees were not recognised in company law as stakeholders and only had the Labour Relations Act as a form of protection to enforce their rights against companies. It is stated that even though the 2008 Act has enabled employees to participate in diverse ways by exercising and enforcing their rights in companies, it has failed to grant employees a real voice when it comes to decision-making; employees are visible in issues of human rights but it does not go further to reach the realisation of true industrial democracy. In issues such a business rescue plan it addresses the fact of worker participation in the formulation of the business rescue plan, but it fails in as far as extending participation to the approval of the business rescue plan, since employees cannot vote on the issue. It is submitted that only if trade unions were granted sufficient participation in approval of the business rescue plan would the process be more meaningful.

[861] The Skills Development Act 97 of 1998.

[862] The Employment Equity Act 55 of 1998.

[863] DTI *supra* n1 29.

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as highlighted above, one can conclude that the process was in line with the Indian approach in recommending rules that are aligned with each jurisdiction's corporate setting and market practices.[864]

In a way the business practices and local conditions of a legislative and non-legislative nature in the South African jurisdiction were taken into consideration, since the provisions that regulate the business takeovers sector need to correspond with non-legislative market practices as well and span the gap between reality and idealism. Idealism refers to striving for what is thought to be international best practices for takeover regulation and enacting these practices "as is" as opposed to modifying them to be suitable for the South African jurisdiction in terms of its market practices. Therefore, it is recommended that the current shareholder protection rules be relaxed so as not to conflict with fundamental transactions.[865]

5.3.2 Recommendation on approval by shareholders and court

5.3.2.1 Recommendation on shareholders' approval

It is recommended that specific provisions of section 115 of the 2008 Act as far as fundamental transactions are concerned be amended. The proposed amendment is similar to provisions that apply under section 61(3) (b) of the 2008 Act, which have to do with a demand for a meeting. The section will provide that a shareholders' meeting must be called for the approval of a fundamental transaction only if demands for such a meeting are made, and signed by holders of 10% of the voting rights entitled to be exercised in relation to the fundamental transaction proposed.[866]

Currently section 115 (1)-(2)(a) of the 2008 Act as far as fundamental transactions are concerned reads as follows:

> "115. (1) Despite section 65, and any provision of a company's Memorandum of Incorporation, or any resolution adopted by its board or holders of its securities, to the contrary, a company may not dispose of,

[864] This submission is discussed in paragraph 2.4.5 of Chapter 2.
[865] This is to follow in paragraph 5.3.2 of this chapter and further.
[866] This submission is similar to one that was made in the USA regarding the approval requisite of mergers in the Model Business Corporation Act. This was discussed in paragraph 3.2.3 of Chapter 3. This answers one of the purposes of this study, since one of its intentions was to gather knowledge of the different ideas from the experience of different jurisdictions and prepare these for future legal reform, with the aim of developing mercantile law.

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or give effect to an agreement or series of agreements to dispose of, all or the greater part of its assets or undertaking, implement an amalgamation or a merger, or implement a scheme of arrangement, unless -

(a) the disposal, amalgamation or merger, or scheme of arrangement -

(i) has been approved in terms of this section; or

(ii) is pursuant to or contemplated in an approved business rescue plan for that company, in terms of Chapter 6; and

(b) to the extent that Parts B and C of this Chapter, and the Takeover Regulations, apply to a company that proposes to -

(i) dispose of all or the greater part of its assets or undertaking;

(ii) amalgamate or merge with another company; or

(iii) implement a scheme of arrangement,

the Panel has issued a compliance certificate in respect of the transaction, in terms of section 119(4)(b), or exempted the transaction in terms of section 119(6).

(2) A proposed transaction contemplated in subsection (1) ~~must~~ be approved -

(a) by a special resolution adopted by persons entitled to exercise voting rights on such a matter, at a meeting called for that purpose and at which sufficient persons are present to exercise, in aggregate, at least 25% of all of 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, as contemplated in section 64(2). "[867]

Therefore section 115 (1)-(2) (a) of the 2008 Act as far as fundamental transactions are concerned should be amended to read as follows:

[867] The words that have been struck out are the ones that have been amended.

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"115. (1) Despite section 65, and any provision of a company's Memorandum of Incorporation, or any resolution adopted by its board or holders of its securities, to the contrary, a company may not dispose of, or give effect to an agreement or series of agreements to dispose of, all or the greater part of its assets or undertaking, implement an amalgamation or a merger, or implement a scheme of arrangement, unless -

(a) the disposal, amalgamation or merger, or scheme of arrangement-

(i) has been approved in terms of this section; or exempted in terms of subsection 2(a)(ii) of this section where there are no demands for a meeting to approve such a transaction,

(ii) is pursuant to or contemplated in an approved business rescue plan for that company, in terms of Chapter 6; and

(b) to the extent that Parts B and C of this Chapter, and the Takeover Regulations, apply to a company that proposes to -

(i) dispose of all or the greater part of its assets or undertaking;

(ii) amalgamate or merge with another company; or

(iii) implement a scheme of arrangement,

the Panel has issued a compliance certificate in respect of the transaction, in terms of section 119(4)(b), or exempted the transaction in terms of section 119(6).

(2) A proposed transaction contemplated in subsection (1) may be approved -

(a) (i) by a special resolution adopted by persons entitled to exercise voting rights on such a matter, at a meeting called for that purpose and at which sufficient persons are present to exercise, in aggregate, at least 25% of all of 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, as contemplated in section 64(2);

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(ii) in which the meeting for such approval is called by a board of a company, or any other person specified in the company's Memorandum of Incorporation or rules, and only if one or more written and signed demands for such a meeting are delivered to the company, and

(iii) each such demand describes the fundamental transaction approval as a purpose for which the meeting is proposed; and

(iv) in aggregate, demands for substantially the same purpose are made and signed by the holders, as of the earliest time specified in any of those demands, of at least 10% of the voting rights entitled to be exercised in relation to the fundamental transaction approval to be considered at the meeting.

(v) A company's Memorandum of Incorporation may specify a lower percentage in substitution for that set out in subsection (2) (a) (iii)." [868]

Furthermore, section 65(11) of the 2008 Act would need to be amended to allow the above. This section of the 2008 Act currently reads as follows:

"(11) A special resolution is required to -

(a) amend the company's Memorandum of Incorporation to the extent required by section 16(1)(c) and section 36(2)(a);

(b) ratify a consolidated revision of a company's Memorandum of Incorporation, as contemplated in section 18(1)(b);

(c) ratify actions by the company or directors in excess of their authority, as contemplated in section 20(2);

(d) approve an issue of shares or grant of rights in the circumstances contemplated in section 41(1);

(e) approve an issue of shares or securities as contemplated in section 41(3);

[868] The underlined words indicate insertions.

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(f) authorise the board to grant financial assistance in the circumstances contemplated in section 44(3)(a)(ii) or 45(3)(a)(ii);

(g) approve a decision of the board for re-acquisition of shares in the circumstances contemplated in section 48(8);

(h) authorise the basis for compensation to directors of a profit company, as required by section 66(9);

(i) approve the voluntary winding up of the company, as contemplated in section 80(1);

(j) approve the winding up of a company in the circumstances contemplated in section 81(1);

(k) approve an application to transfer the registration of the company to a foreign jurisdiction as contemplated in section 82(5);

(l) approve any proposed fundamental transaction, to the extent required by Part A of Chapter 5; ~~or~~

(m) revoke a resolution contemplated in section 164(9)(c)." [869]

It will then need to be amended to read as follows:

""(11) A special resolution is required to -

(a) amend the company's Memorandum of Incorporation to the extent required by section 16(1)(c) and section 36(2)(a);

(b) ratify a consolidated revision of a company's Memorandum of Incorporation, as contemplated in section 18(1)(b);

(c) ratify actions by the company or directors in excess of their authority, as contemplated in section 20(2);

(d) approve an issue of shares or grant of rights in the circumstances contemplated in section 41(1);

[869] The words that have been struck out are the ones that have been amended.

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(e) approve an issue of shares or securities as contemplated in section 41(3);

(f) authorise the board to grant financial assistance in the circumstances contemplated in section 44(3)(a)(ii) or 45(3)(a)(ii);

(g) approve a decision of the board for re-acquisition of shares in the circumstances contemplated in section 48(8);

(h) authorise the basis for compensation to directors of a profit company, as required by section 66(9);

(i) approve the voluntary winding up of the company, as contemplated in section 80(1);

(j) approve the winding up of a company in the circumstances contemplated in section 81(1);

(k) approve an application to transfer the registration of the company to a foreign jurisdiction as contemplated in section 82(5);

(l) approve any proposed fundamental transaction, to the extent required by Part A of Chapter 5, if it was undertaken in terms of section 115(1); or

(m) revoke a resolution contemplated in section 164(9)(c)." [870]

The suggested amendments would allow a company to deal with time-constrained fundamental transactions efficiently and not be hindered by the delay of the process involved in the approval requisite under section 115 of the 2008 Act, as indicated in paragraph 3.2.3 of Chapter 3. In other words, the amendment will eliminate the delay caused by the approval requisite. This is because rather than having the approval requisite in all fundamental transactions, there will be a simplification of the system, which will allow a vote in all fundamental transactions only if a certain percentage of shareholders request a vote in reaction to the fundamental transaction proposal by the board of directors. This still preserves the shareholder protection rule but relaxes it to deal with the concerns raised in this study.

[870] The underlined words indicate insertions.

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Furthermore, specific provisions of section 65 of the 2008 Act should be amended as far as resolution thresholds for approving fundamental transactions are concerned. This should be done to balance the said shareholder protection rules with all implicated fundamental transactions. Currently those specific provisions of section 65 read as follows:

> "(7) For an ordinary resolution to be approved by shareholders, it must be supported by more than 50 percent of the voting rights exercised on the resolution.
>
> (8) Except for an ordinary resolution for the removal of a director under section 71, a company's Memorandum of Incorporation may require -
>
> (a) a higher percentage of voting rights to approve an ordinary resolution; or
>
> (b) one or more higher percentages of voting rights to approve ordinary resolutions 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 highest established requirement for approval of an ordinary resolution on any matter, and the lowest established requirement for approval of a special resolution on any matter.
>
> (9) For a special resolution to be approved by shareholders, it must be supported by at ~~least 75 percent~~ of the voting rights exercised on the resolution.
>
> (10) A company's Memorandum of Incorporation may permit-
>
> (a) a different percentage of voting rights to approve any special resolution; or
>
> (b) one or more different percentages of voting rights to approve special resolutions 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 highest established requirement for approval of an

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ordinary resolution on any matter, and the lowest established requirement for approval of a special resolution on any matter." [871]

Therefore as a result of the proposed amendments, those specific provisions applicable to section 65 should read as follows:

"7) For an ordinary resolution to be approved by shareholders, it must be supported by more than 50% percent of the voting rights exercised on the resolution.

(8) Except for an ordinary resolution for the removal of a director under section 71, a company's Memorandum of Incorporation may require -

(a) a higher percentage of voting rights to approve an ordinary resolution; or

(b) one or more higher percentages of voting rights to approve ordinary resolutions 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 highest established requirement for approval of an ordinary resolution on any matter, and the lowest established requirement for approval of a special resolution on any matter.

(9) For a special resolution to be approved by shareholders, it must be supported by at least 60 percent of the voting rights exercised on the resolution.

(10) A company's Memorandum of Incorporation may permit -

(a) a different percentage of voting rights to approve any special resolution; or

(b) one or more different percentages of voting rights to approve special resolutions concerning one or more particular matters, respectively,

provided that there must at all times be a margin of at least 5 percentage points between the highest established requirement for approval of an

[871] The words that have been struck out are the ones that have been amended.

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ordinary resolution on any matter, and the lowest established requirement for approval of a special resolution on any matter." [872]

These suggested amendments will make sure that the special resolution, if it reflects the wishes of the shareholders in an MOI, can reach the 55% resolution threshold as opposed to the current 60%.[873] The 55% threshold will mean that fundamental transactions are approved with ease if it is the wish of the shareholders, while at the same time offering the opportunity to adjust the threshold for greater protection.

These suggested amendments will also ensure that shareholder protection in terms of resolution thresholds is relaxed in line with ensuring compatibility and harmonisation of South African law with international best trends,[874] since the jurisdictions discussed that have far more experience in takeover law have less stringent resolution thresholds than the South African jurisdiction.[875] Furthermore, the amendments will bring about balance in shareholder protection and fundamental transactions as a result of the relaxation.

5.3.2.2 Recommendation on court approval

It is recommended that specific and related provisions of section 115 and 164 of the 2008 Act as far as fundamental transactions are concerned be amended. The proposed amendment is similar to provisions that apply under the DGCL in respect of a merger.[876]

Currently section 115 (3) of the 2008 Act reads as follows:

> "(3) Despite a resolution having been adopted as contemplated in subsections (2)(a) and (b), a company may not proceed to implement that resolution without the approval of a court if -
>
> (a) 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

[872] The underlined words indicate insertions.
[873] Since it was shown in paragraph 3.2.3 of Chapter 3 that the special resolution cannot get to the 50% mark as per the current provisions, only to 60%. The possibility of reaching the 50% resolution threshold mark will be similar to that of the Model Business Corporation Act.
[874] This is one of the purposes of the study as indicated in paragraph 4 of Ch. 1.
[875] This was indicated in paragraph 5.2.2.1 of this chapter.
[876] It was found that in the jurisdiction from which the statutory merger was absorbed, the court approval provisions do not apply, rather an appraisal remedy.

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vote, any person who voted against the resolution requires the company to seek court approval; or

(b) the court, on an application within 10 business days after the vote by any person who voted against the resolution, grants that person leave, in terms of subsection (6), to apply to a court for a review of the transaction in accordance with subsection (7)." [877]

Therefore section 115 (3)(a) and (b) of the 2008 Act, as far as a statutory merger is concerned, should be amended to read as follows:

"(3) Despite a resolution having been adopted as contemplated in subsections (2)(a) and (b), excluding an amalgamation or merger resolution, a company may not proceed to implement that resolution without the approval of a court if-

(a) 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 court approval; or

(b) the court, on an application within 10 business days after the vote by any person who voted against the resolution, grants that person leave, in terms of subsection (6), to apply to a court for a review of the transaction in accordance with subsection (7)." [878]

Also, section 164(2) of the 2008 Act needs to be amended to affirm the right of exclusivity of an appraisal right against a proposed statutory merger. It currently reads as follows:

"(2) If a company has given notice to shareholders of a meeting to consider adopting a resolution to -

(a) amend its Memorandum of Incorporation by altering the preferences, rights, limitations or other terms of any class of its shares in any manner

[877] The words that have been struck out have been amended.
[878] The underlined words are the proposed insertions in the section.

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materially adverse to the rights or interests of holders of that class of shares, as contemplated in section 37(8); or

(b) enter into a transaction contemplated in section 112, 113, or 114,

that notice must include a statement informing shareholders of their rights under this section."[879]

These provisions need to be amended to read as follows:

> "(2) If a company has given notice to shareholders of a meeting to consider adopting a resolution to-
>
> (a) amend its Memorandum of Incorporation by altering the preferences, rights, limitations or other terms of any class of its shares in any manner materially adverse to the rights or interests of holders of that class of shares, as contemplated in section 37(8); or
>
> (b) enter into a transaction contemplated in section 112, 113, or 114, <u>of which section 164 will have right of exclusivity for a transaction contemplated in terms of section 113,</u>
>
> that notice must include a statement informing shareholders of their rights under this section." [880]

These suggested amendments will attempt to minimise if not eliminate the delay caused by long court processes and ensure that the appeal processes contained in the 2008 Act are exhausted first to avoid litigation in takeover bids, as intended by the DTI policy guidelines.[881] In line with achieving this, these suggestions will harmonise the takeover rules in this aspect with international best practices. In so doing it will ease the possibility of this shareholder protection rule frustrating a proposed statutory merger, in view of the fact that the court approval process in South Africa could be employed as a delay mechanism to frustrate a proposed time-constrained fundamental transaction, as highlighted in paragraph 3.3 of Chapter 3.

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[879] The words that have been struck out are replaced by the proposed insertions.
[880] The underlined words are the proposed insertions in the section.
[881] DTI policy guidelines at 41.

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Furthermore, it is recommended that certain provisions of section 115 be amended and some be cross-referenced to section 163. These provisions currently read as follows:

> "(3) Despite a resolution having been adopted as contemplated in subsections (2)~~(a) and (b),~~ a company may not proceed to implement that resolution without the approval of a court if -
>
> (a) 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 court approval; or
>
> (b) the court, on an application within 10 business days after the vote by any person who voted against the resolution, grants that person leave, in terms of subsection (6), to apply to a court for a review of the transaction in accordance with ~~subsection (7).~~
>
> (4) For the purposes of subsections (2) and (3), any voting rights controlled by an acquiring party, a person related to an acquiring party, or a person acting in concert with either of them, must not be included in calculating the percentage of voting rights -
>
> (a) required to be present, or actually present, in determining whether the applicable quorum requirements are satisfied; or
>
> (b) required to be voted in support of a resolution, or actually voted in support of the resolution.
>
> (5) If a resolution requires approval by a court as contemplated in terms of subsection (3)(a), the company must either -
>
> (a) within 10 business days after the vote, apply to the court for approval, and bear the costs of that application; or
>
> (b) treat the resolution as a nullity.
>
> (6) On an application contemplated in subsection (3)(b), the court may grant leave only if it is satisfied that the applicant -

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(a) is acting in good faith;

(b) appears prepared and able to sustain the proceedings; and

(c) has alleged facts which, if proved, would support an order in terms of subsection (7).

(7) On reviewing a resolution that is the subject of an application in terms of subsection (5)(a), or after granting leave in terms of subsection (6),~~ the court may set aside the resolution only if-~~

~~(a) the resolution is manifestly unfair to any class of holders of the company's securities; or~~

~~(b) the vote was materially tainted by conflict of interest, inadequate disclosure, failure to comply with the Act, the Memorandum of Incorporation or any applicable rules of the company, or other significant and material procedural irregularity~~." [882]

The proposed amendments to these provisions read as follows:

"(3) Despite a resolution having been adopted as contemplated in subsections (2), a company may not proceed to implement that resolution without the approval of a court if -

(a) 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 court approval; except in instances that are provided in subsection 2(b);

(b) the court, on an application within 10 business days after the vote by any person who voted against the resolution, grants that person leave, in terms of subsection (6), to apply to a court for a review of the transaction in accordance with section 163(1).

(4) For the purposes of subsections (2) and (3), any voting rights controlled by an acquiring party, a person related to an acquiring party,

[882] The words that have been struck out are deleted and replaced by the proposed amendments.

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or a person acting in concert with either of them, must not be included in calculating the percentage of voting rights -

(a) required to be present, or actually present, in determining whether the applicable quorum requirements are satisfied; or

(b) required to be voted in support of a resolution, or actually voted in support of the resolution.

(5) If a resolution requires approval by a court as contemplated in terms of subsection (3)(a), the company must either-

(a) within 10 business days after the vote, apply to the court for approval, and bear the costs of that application; or

(b) treat the resolution as a nullity.

(6) On an application contemplated in subsection (3)(b) in accordance with section 163(1), the court may grant leave only if it is satisfied that the applicant-

(a) is acting in good faith;

(b) appears prepared and able to sustain the proceedings; and

(c) has alleged facts which, if proved, would support an order in terms of subsection (7) and section 163(2).

(7) On reviewing a resolution that is the subject of an application in terms of subsection (5)(a), or after granting leave in terms of subsection (6), the court may make any interim or final order it considers fit as contemplated in section 163(2), if it satisfied with one or more of the grounds in terms of section 163(1)

[Subsection 7 (a) and (b) amended and substituted by provisions in subsection 163(1).],"[883]

It is recommended that the grounds for setting aside a resolution in terms of section 115(7) be accommodated under section 163(1), especially section 115(7)(b) and not

[883] The underlined words are the proposed insertions.

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necessarily section 115(7)(a), in view of the fact that section 115(7)(a) is the same as section 163(1)(a) and (b). Currently section 163(1) reads as follows:

> “**163. Relief from oppressive or prejudicial conduct or from abuse of separate juristic personality of company**
>
> (1) A shareholder or a director of a company may apply to a court for relief if -
>
> (a) any act or omission of the company, or a related person, has had a result that is oppressive or unfairly prejudicial to, or that unfairly disregards the interests of, the applicant;
>
> (b) the business of the company, or a related person, is being or has been carried on or conducted in a manner that is oppressive or unfairly prejudicial to, or that unfairly disregards the interests of, the applicant; or
>
> (c) the powers of a director or prescribed officer of the company, or a person related to the company, are being or have been exercised in a manner that is oppressive or unfairly prejudicial to, or that unfairly disregards the interests of, the applicant.”

It is proposed that the section should read as follows in order to accommodate provisions of section 115(7):

> **“163. Relief from oppressive or prejudicial conduct or from abuse of separate juristic personality of company**
>
> (1) A shareholder or a director of a company may apply to a court for relief if -
>
> (a) any act or omission of the company, or a related person, has had a result that is oppressive or unfairly prejudicial to, or that unfairly disregards the interests of, the applicant;
>
> (b) the business of the company, or a related person, is being or has been carried on or conducted in a manner that is oppressive or unfairly prejudicial to, or that unfairly disregards the interests of, the applicant; or

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(c) the powers of a director or prescribed officer of the company, or a person related to the company, are being or have been exercised in a manner that is oppressive or unfairly prejudicial to, or that unfairly disregards the interests of, the applicant.

(d) a vote in a resolution of a company was materially tainted by conflict of interest, inadequate disclosure, failure to comply with the Act, the Memorandum of Incorporation or any applicable rules of the company, or other significant and material procedural irregularity."[884]

These amendments will ensure that any party that brings an application against the adopted resolution has grounds for it, as the process will be subject to leave and not just because 15% voted against the resolution, as is the current stance under section 115 (3)(a), without any grounds required from the party requesting that a company should get court approval for the resolution. This will be in line with the rule of law in court, which requires that he who alleges must prove; the onus is on the one who alleges. This will also pose the risk of a potential cost order, should the action of the party that brings the resolution before court be solely based on vexatious claims and this method is used with the intention of frustrating a proposed fundamental transaction.

Furthermore, it will remove the predicament that subjects the resolution to scrutiny suggesting that unfairness was involved. The claim of unfairness comes from the fact that under section 115(7)(a) and (b) it is advised that court may make an order against the resolution, if it was found that it was unfair towards other shareholders or the voting was materially tainted, there was conflict of interest, etc.

These amendments will also ensure that the process is aligned with international practices and in line with the corporate law reform process objective of avoiding litigation[885] by providing a single course for court and eliminating provision duplication. In that way these amendments will limit all vexatious requests that a company should seek court approval for a resolution in favour of a fundamental transaction that are made with the intent to delay and frustrate proposed fundamental transactions.

[884] The underlined words are the proposed insertions.
[885] DTI policy guidelines at 41.

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5.3.3 Recommendation on dissenting shareholders

5.3.3.1 Recommendation on the appraisal remedy

It is recommended that section 164 of the 2008 Act be amended to accommodate fundamental transactions under section 164(17)(b) of the 2008 Act. This will enlist fundamental transactions as one of the factors that a court should consider when it makes an order in response to an application by a company stating that it will not be able to pay the fair market value of the dissenting shareholders' shares immediately. Currently the subsection reads as follows:

> "(17) If there are reasonable grounds to believe that compliance by a company with subsection (13)(b), or with a court order in terms of subsection (15)(c)(v)(bb), would result in the company being unable to pays its debts as they fall due and payable for the ensuing 12 months -
>
> (a) the company may apply to a court for an order varying the company's obligations in terms of the relevant subsection; and
>
> (b) the court may make an order that -
>
> (i) is just and equitable, having regard to the financial circumstances of the company; and
>
> (ii) ensures that the person to whom the company owes money in terms of this section is paid at the earliest possible date compatible with the company satisfying its other financial obligations as they fall due and payable."

Section 164(17) of the 2008 Act should be amended as follows:

> "(17) If there are reasonable grounds to believe that compliance by a company with subsection (13)(b), or with a court order in terms of subsection (15)(c)(v)(bb), would result in the company being unable to continue with the proposed fundamental transaction or pays its debts as they fall due and payable for the ensuing 12 months -
>
> (a) the company may apply to a court for an order varying the company's obligations in terms of the relevant subsection; and

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(b) the court may make an order that -

(i) is just and equitable, having regard to the financial circumstances of the company;

(ii) ensures that the person to whom the company owes money in terms of this section is paid at the earliest possible date compatible with the company satisfying its other financial obligations as they fall due and payable; and

(iii) ensures that the proposed fundamental transaction is not frustrated."[886]

These suggested amendments will ensure that the reasons why the dissenting shareholder is exiting the company in the first place are catered for. It will ensure that the court considers non-frustration of the proposed fundamental transaction when making an order under section 167(17)(b) of the 2008 Act, not just debts as they fall due in the ensuing months, but also the current transaction proposal that led to the right of appraisal being exercised in the first place. Most significantly, these amendments will expressly emphasise the latter.

5.4 Conclusion

The researcher believes that the adoption of the above recommendations would enhance the balance between shareholder protection rules and fundamental transactions. Their adoption would be a key feature in the 2008 Act, as it would provide solutions to the problems that have been raised in this study regarding conflict between shareholder protection provisions, on the one hand, and fundamental transaction provisions on the other hand. This is because the conflict between the two rules tends to frustrate the realisation of what these very rules are intended for.

Furthermore, it will assist in making sure that the 2008 Act is aligned with international trends, since one of the purposes of the DTI policy guideline was to ensure compatibility and harmonisation with the best practice jurisdictions internationally. It will also contribute to the existing body of knowledge, particularly in respect of the

[886] The underlined words are the proposed insertions.

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takeover law regime in South Africa, but from a conflict of rules perspective, as hypothesised above.

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