

# SOME IMMEDIATE IMPLICATIONS OF THE NEW COMPANIES ACT

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## I INTRODUCTION

This article is intended to deal with selected aspects of the Companies Act 71 of 2008 (hereafter “the Act”)<sup>1</sup> insofar as they relate to pre-existing companies and those requirements of the Act which apply immediately, notwithstanding the two year period contemplated by Schedule 5 of the Act (hereafter “Schedule 5 of the Act”). As part of the Transitional Arrangements<sup>2</sup> for the implementation of the Act, Schedule 5 of the Act provides<sup>3</sup>:

‘During the period of two years immediately following the general effective date –

- a) If there is a conflict between –
  - i) a provision of this Act, and a provision of a pre-existing company’s Memorandum of Incorporation, the latter provision prevails, except to the extent that this schedule provides otherwise;
  - ii) a binding provision contemplated in sub-item (3) and this Act, the binding provision prevails; or
  - iii) a provision of an agreement contemplated in sub-item(3A), and this Act or the Company’s Memorandum of Incorporation, the provision of the agreement prevails, except to the extent that the agreement, or the Memorandum of Incorporation provides otherwise; and ...’

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<sup>1</sup> Signed into law by the President of the Republic of South Africa on 8 April 2009 and gazetted on 9 April 2009. The Act came into effect on 1 May 2010 by Proclamation (see S225 of the Act)

<sup>2</sup> S 224(3) read with Schedule 5 of the Act

<sup>3</sup> Item 7(5) of Schedule 5 of the Act

Schedule 5 of the Act goes on to provide that<sup>4</sup>

Despite anything to the contrary in a Company's Memorandum of Incorporation, the provisions of this Act in respect of:

- (a) the duties, conduct and liability of Directors apply to every director of a pre-existing company as from the effective date;
- (b) rights in terms of this Act of shareholders to receive any notice or have access to any information apply as from the effective date to every pre-existing company;
- (c) meeting of shareholders or directors, and adoption of resolutions apply from the effective date to every pre-existing company; and
- (d) Chapter 5 applies from the effective date to every pre-existing company except to the extent that it is exempted by or in terms of that chapter.

In respect of actions by shareholders prior to the general effective date<sup>5</sup> in respect of approval of any distribution, financial assistance, insider share issues or options, the Act applies even if such actions have been approved by the company's shareholders before the general effective date but where the actions of shareholders have not been completed by the effective date<sup>6</sup>.

In addition, the Act has further immediate implications for directors and prescribed officers, any secretaries and auditors of pre-existing companies. In this regard, Schedule 5 of the Act provides<sup>7</sup>:

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<sup>4</sup> Item 7(5) of Schedule 5 to the Act

<sup>5</sup> Item (1)(1)(a) of Schedule 5 of the Act defines the 'general effective date' as 'the date on which Section 1 of this Act came into operation. Section 1 of the Act came into operation on 1 May 2011 by proclamation.

<sup>6</sup> Item 7(6) of Schedule 5 to the Act

<sup>7</sup> Item 7(2) of Schedule 5 to the Act

‘(2) A person contemplated in sub-item(1) who, in terms of this Act is ineligible to be, or disqualified from being, a director, alternate director, prescribed officer, company secretary or auditor is regarded as having resigned from every such office in any company as from the effective date.’

And,

‘(3) As from the effective date a pre-existing company is deemed to have a number of vacancies on the board equal to the difference between -

- (a) the minimum number of directors required by or in terms of this Act; and
- (b) the actual number of directors of that pre-existing company immediately before the effective date, if that number is less than the minimum referred to in paragraph (a).<sup>8</sup>

This article does not purport to deal with the implications of the Act for pre-existing companies insofar as directors, prescribed officers, company secretaries or auditors are concerned. These implications are far reaching and warrant an article on their own. This article intends to deal with the implications of the Act for pre-existing companies in respect of the following aspects:

- II The pre-existing company’s constitutional documents;
- III Fundamental transactions<sup>9</sup>; involving pre-existing companies;
- IV Rights of shareholders of existing companies in respect of notice, access to company information, meetings and adoption of resolutions<sup>10</sup>;

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<sup>8</sup> Item 7(3) of Schedule 5 to the Act

<sup>9</sup> Sections 112 to 116 of the Act read with Item 7(5)(d) of Schedule 5 to the Act. These transactions are: S112-Proposals to dispose of all or greater part of assets or undertaking; S113-Proposals for amalgamation or merger; S114-Proposals for Scheme of arrangement

- V Transactions relating to distributions, financial assistance, insider share issues, or options.<sup>11</sup>

## II THE PRE-EXISTING COMPANY'S CONSTITUTIONAL DOCUMENTS

The Act contemplates the uninterrupted continuation of pre-existing companies without the need of any pre-existing company to do anything or to “re-register” so to speak. The Act provides that:<sup>12</sup>

‘As of the general effective date, every pre-existing company that was, immediately before that date –

- (a) incorporated or registered in terms of the Companies Act 1973 (Act 61 of 1973) or
- (b) was recognised as an ‘existing company’ in terms of the Companies Act 1973 (Act 151 of 1973),

continues to exist as a company, as if it had been incorporated and registered in terms of this Act with the same name and registration number previously assigned to it, subject to item 4.’

The reference to item 4<sup>13</sup> relates to the powers of pre-existing companies in respect of its issued shares. In respect of nominal or par-value shares, the Act<sup>14</sup> now provides that a share does not have a nominal or par value subject to the Transitional Arrangements<sup>15</sup>. The issue of nominal or par-value shares is not dealt with specifically or at

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<sup>10</sup> Item 7(5) (b) and (c) of Schedule 5 to the Act

<sup>11</sup> Item 7(6) of Schedule 5 to the Act

<sup>12</sup> Item 2(1) of Schedule 5 to the Act

<sup>13</sup> Note 12 above

<sup>14</sup> S 35(2) of the Act

<sup>15</sup> Item 6 of Schedule 5 to the Act

length other than to point out that the Act does away with the concept in keeping with the Guidelines for Corporate Law Reform.<sup>16</sup>

The transitional arrangements contain a number of deeming provisions to facilitate the continued operation of certain companies, for example Section 21<sup>17</sup> companies in terms of the old Act, personal liability companies in terms of the old Act (Section 53(b)<sup>18</sup> and also goes on to provide for the newly defined State Owned Company<sup>19</sup>.

Pre-existing companies have two years immediately following the general effective date<sup>20</sup> to file an amendment (without charge) to such company's Memorandum of Incorporation in order to harmonise the Memorandum of Incorporation with the provisions of the Act<sup>21</sup>.

In this regard, the Act requires that any agreement entered into by the shareholders must be consistent with the provisions of the Act and the company's Memorandum of Incorporation and to the extent that it is not, it is void<sup>22</sup>. Pre-existing companies are however, notwithstanding the provisions of Section 15.7 of the Act afforded some latitude by the transitional provisions which provide that for a two year period after the

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<sup>16</sup> South African Company Law for the 21<sup>st</sup> Century, Guidelines for Corporate Law Reform (Notice 1183 of 2004). The guidelines record the stated intent as follows: "The rules relating to capital require review. The continued need for the concept of par value has been questioned within South Africa and has been abolished in other jurisdictions. Par value was originally developed in the early days of companies to ensure "equitable contribution," i.e., equal pro rata payment by shareholders for shares issued by the corporation. The par value may have been intended to represent some sort of measure of value. This purpose was long ago abandoned as economically unrealistic. Par value and its corollary, stated capital (par value per share multiplied by the total number of shares outstanding), were employed as part of an equation determining whether the corporation could pay dividends or make other distributions to its shareholders. Under this equation, a corporation may not pay a dividend or make another distribution unless the sum of its assets at least equals the sum of its liabilities and its stated capital. To put it in other words, a corporation could make distributions only out of "surplus". With the development of low-par and no-par share, this reason for par value has also fallen away. Today, it is widely recognised that par value is economically insignificant and artificial."

<sup>17</sup> Item 4(1)(a) of Schedule 5 to the Act

<sup>18</sup> Item 4(1)(b) of Schedule 5 to the Act

<sup>19</sup> Item 4(1)(c) of Schedule 5 to the Act

<sup>20</sup> See note 5 above

<sup>21</sup> Item 4(2) of Schedule 5 to the Act

<sup>22</sup> Section 15.7 provides "The shareholders of a company may enter into any agreement with one another concerning any matter relating to the company, but any such agreement must be consistent with this Act and the Company's Memorandum of Incorporation, and any provision of such agreement that is inconsistent with this Act or the Company's Memorandum of Incorporation is void to the extent of the inconsistency."

general effective date, agreements by shareholders of pre-existing companies adopted before the general effective date continue to apply on their terms for a period of two years or until changed by the shareholders who are parties to the agreement<sup>23</sup>. Such agreements will also continue to apply after the two year period to the extent consistent with the Act and the company's Memorandum of Incorporation<sup>24</sup>.

Consequently, while pre-existing companies have some latitude in respect of pre-existing shareholders agreements for two years, any new or amended shareholders agreement after the general effective date will trigger a need to examine consistency with and compliance of the proposed agreement, change or otherwise with the provisions of the Act.

The latitude afforded pre-existing Companies in respect of their constitutional documents do, however, not trump the provisions of the Act and the schedule in certain important respects. These are outlined by the subsequent sections of this article and to the issue of nominal or par value shares<sup>25</sup> directors, prescribed officers, company's secretaries or auditors<sup>26</sup> which issues are not canvassed in this article.

In general then, as far as a company's constitutional documents are concerned, the Act provides<sup>27</sup>:

'During the period of two years immediately following the general effective date-

- (a) if there is a conflict between –
  - (i) a provision of this Act, and a provision of a provision of a pre-existing company's

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<sup>23</sup> Item 4(3) and Items 4(3A)(a) of Schedule 5 to the Act

<sup>24</sup> Item 4(3A)b of Schedule 5 to the Act

<sup>25</sup> See note 16 above

<sup>26</sup> See note 4 above

<sup>27</sup> Item 4(4) of Schedule 5 of the Act

- Memorandum of Incorporation, the latter provision prevails, except to the extent that this schedule provides otherwise, \*\*
- (ii) a binding provision contemplated in sub-item (3) and this Act, the binding provision \*\* prevails; or
  - (iii) a provision of an agreement contemplated in sub-item (3A), and this Act or the company's Memorandum of Incorporation, the provision of the agreement prevails, except to the extent that the Agreement, or the Memorandum of Incorporation, provides otherwise; and
- (b) Despite Chapter 7, until a pre-existing company has filed an amendment contemplated in sub-item (2)(a), neither the Commission nor the Panel may issue a compliance notice to that company with respect to conduct that is –
- (i) inconsistent with this Act; but
  - (ii) consistent with the provision that prevails over this Act in terms of paragraph (a)

Consequently, while a pre-existing company is not obligated to amend its constitutional documents prior to expiry of the two year period on 29 April 2013, the significant exceptions in respect of which compliance is required with the Act will leave pre-existing companies in the uncomfortable position of being required to have regard to the new Act on those issues where the act overrides the position, where, in the ordinary course their constitutional documents would regulate the position. Consequently, ongoing assessment and vigilance will be required by pre-existing companies to ensure compliance with the new Act. Given the risks inherent in such an approach, it may well be preferable for pre-existing companies to file an amended Memorandum of Incorporation to bring the existing companies constitutional

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\*\* my emphasis

documents in line with the Act. In doing so however, such company will become subject to the compliance with the Act in the form of notices issued by the Commission or Panel in respect of conduct that is inconsistent with the Act.<sup>28</sup>

### **III FUNDAMENTAL TRANSACTIONS AND THE IMPLICATIONS FOR PRE-EXISTING COMPANIES**

These transactions relate to proposals to dispose of all or the greater part of the assets or undertaking of a company<sup>29</sup>, proposals for amalgamation or merger<sup>30</sup>, and schemes of arrangement<sup>31</sup>. In respect of these transactions notwithstanding any provision to the contrary, in the company's own constitutional documents, the provisions of the Act will apply from the effective date except to the extent exempted by Chapter 5.<sup>32</sup>

Some of the implications for pre-existing companies in relation to the fundamental transactions are as follows:

#### **1. Trigger of appraisals rights for dissenting shareholders**

The Act provides that if a company has given notice to shareholders of a meeting to consider adopting a resolution to enter into a transaction contemplated by Chapter 5, Section 112 (proposals to dispose of all or greater part of the assets of the undertaking), Section 113 (proposals for amalgamation or merger), or Section 114 (Scheme of Arrangement), such notice must include a statement informing shareholders of their rights in terms of Section 164 of the Act)<sup>33</sup>. In broad terms Section

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<sup>28</sup> See note 26 above

<sup>29</sup> S 112 of the Act

<sup>30</sup> S 113 of the Act

<sup>31</sup> S 114 of the Act

<sup>32</sup> Item 7(5)(d) of Schedule 5 to the Act

<sup>33</sup> S 164 (2)(b) of the Act

164, which deals with dissenting shareholders appraisal rights, provides for a procedure in terms of which a dissenting shareholder may demand fair value for the shares held by such shareholder<sup>34</sup>, if such shareholder has objected to the resolution opposing the fundamental transaction and the company proceeds to adopt the resolution, provided such dissenting shareholder complies with the procedural requirements outlined in Section 164 to the Act<sup>35</sup>. Subject to certain conditions, once a dissenting shareholder has sent the demand contemplated<sup>36</sup>, such shareholder shall have no further rights in respect of the shares other than to be paid their fair value subject to certain conditions<sup>37</sup>. The company is then required to submit a written offer to pay an amount considered by the company's directors to be the fair value of the relevant shares, once again, subject to certain conditions<sup>38</sup>. The dissenting shareholder then has thirty business days to accept such offer of fair value in respect of the shares<sup>39</sup>. While the dissenting shareholder is not obliged to accept the fair value offer, if the dissenting shareholder does so, the company is obliged to effect payment to the dissenting shareholder within ten business days, on tender of the share certificates or in the case of un-certificated shares, the dissenting shareholder must direct the transfer to the company or its agent.<sup>40</sup> Should there be reasonable grounds to believe that the effect of the payment by the company of the dissenting shareholders' shares would result in the company being unable to pay its debts as they fall due for the ensuing twelve months, then the company would need to apply to Court for an Order varying the company's obligation<sup>41</sup>.

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<sup>34</sup> S 164(5) of the Act

<sup>35</sup> S 164(5)(b)(ii) of the Act

<sup>36</sup> See note 34 above

<sup>37</sup> S 164(9) of the Act

<sup>38</sup> S 164(11) of the Act

<sup>39</sup> S 164(12) of the Act

<sup>40</sup> S 164 (9) read with S 164(13)(b)

<sup>41</sup> S 164(17)

Consequently, for an existing company contemplating any fundamental transaction, the appraisal rights held by minority dissenting shareholders gives rise to a significant added dimension for consideration prior to proposing any such fundamental transaction.

## 2. **Statutory merger**

The Act sets out by way of statute the merger procedure<sup>42</sup>. For pre-existing companies not only is the procedure now laid out for amalgamation or merger, there are important new requirements. One of the cornerstones of the new Act is a capital maintenance regime based on solvency and liquidity<sup>43</sup>. This cornerstone is carried through the Act's provisions in the context of amalgamations or mergers. The Act now requires that companies may merge or amalgamate as long as each amalgamated or merged company will satisfy the solvency and liquidity test<sup>44</sup>. The requirement for the board to consider the solvency and liquidity of the company following any merger or amalgamation is new, and, applies notwithstanding any provision of the Company's Memorandum of Incorporation to the contrary<sup>45</sup>.

An important new feature of the immediate application of the statutory merger procedure<sup>46</sup> is the statutory vesting of ownership and transfer of liabilities by operation of law on the strength of the merger or amalgamation agreement concluded

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<sup>42</sup> S 113 of the Act

<sup>43</sup> S 4(1) of the Act

<sup>44</sup> S 113(1) read with S 113(4)

<sup>45</sup> S 115(1)

<sup>46</sup> S 113 read with S 115 of the Act

by the company or companies concerned. No further legal formalities are required to effect vesting/transfer<sup>47</sup>.

In the context of fundamental transactions, the shareholder approval requirements set out in the new Act will also apply, notwithstanding the provisions of a Memorandum of Incorporation to the Contrary. This is dealt with separately below.

#### **IV RIGHTS OF SHAREHOLDERS OF EXISTING COMPANIES IN RESPECT OF NOTICE, ACCESS TO COMPANY INFORMATION AND ADOPTION OF RESTRICTIONS**

##### **1. Rights of Shareholders to receive notice**

In keeping with the electronic age, notice provisions are considerably modernised. It is sufficient for notice to be transmitted electronically provided that notice may be conveniently printed at a reasonable time and at a reasonable cost.<sup>48</sup> This is however subject to the regulations which provide that<sup>49</sup>:

‘A notice or document to be delivered for any purpose contemplated in the Act or these regulations may be delivered in any manner -

- (a) contemplated in Section 6(10) or (11); or
- (b) set out in Table CR 3<sup>50</sup>

The table CR3 to the regulations provides for the methods and times for delivery of documents to various persons, bodies

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<sup>47</sup> S 116(7) and S 116(8) of the Act

<sup>48</sup> S 6(10) of the Act

<sup>49</sup> Regulation 7 to the Act

<sup>50</sup> Annexure 3 to the Regulations of the Act: Methods and Times for Delivery of Documents

including the Commission<sup>51</sup>, the State, employees and trade unions.

As far as timing is concerned, the Act provides for notice of at least fifteen business days in the case of public companies, non-profit companies, with voting members, and, in all other cases, ten business days.<sup>52</sup> This is subject to a company's Memorandum of Incorporation which may provide for longer or shorter minimum periods of notice<sup>53</sup>. There is also now considerable flexibility in respect of waiver of notice<sup>54</sup>. Thus far, in as much as notice is concerned, pre-existing companies would have little immediate concern, however the Act is now clear in its codification of what is required to be disclosed in the notice of the meeting apart from the usual provisions as to the date, time and place, the Act stipulates that the general purpose of the meeting and any specific purpose, if applicable, be disclosed in the notice<sup>55</sup>. Further, if a resolution is to be considered at the meeting, a copy of the proposed resolution and the percentage voting rights required to carry the resolution must also be disclosed<sup>56</sup>. Importantly, however, material defects in the giving of notice or the failure in the delivery of the notice will not invalidate any action taken at the meeting<sup>57</sup>.

## 2. Access to Company Information

In terms of the Act right of access is not limited to "members" or "shareholders". The Act now provides that any person who holds or who has a beneficial interest<sup>58</sup> in any securities<sup>59</sup> in

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<sup>51</sup> S1 of the Act – "Commission" means the Companies and Intellectual Property Commission established by Section 185"

<sup>52</sup> S 62(1) of the Act

<sup>53</sup> S 62(2) of the Act

<sup>54</sup> S 62(2A) of the Act

<sup>55</sup> S 62(3)(a)&(b) of the Act

<sup>56</sup> S 62(3)(c) of the Act

<sup>57</sup> S 62(6) of the Act

<sup>58</sup> S 1 of the Act – see page 13 of text below for definition

respect of profit companies or who are members of non-profit companies, have a right of inspection and to copy information contained in certain records of the company<sup>60</sup>. Not only is the right of access expanded to those holding a beneficial interest, the right would also apply in respect of “securities”. This is defined as ‘any shares, debentures or other instruments, irrespective of their form or title, issued or authorised to be issued by a profit company’<sup>61</sup>. ‘Beneficial interest’ is also defined broadly, and, -

‘when used in relation to a company’s securities means the right or entitlement of a person, through ownership, agreement, relationship or otherwise, alone or together with another person to –

- (a) receive or participate in any distribution in respect of the company’s securities;
- (b) exercise or cause to be exercised, in the ordinary course, any or all of the rights attaching to the company’s securities; or
- (c) dispose or direct the disposition of the company’s securities, or any part of the distribution in respect of the securities,

but does not include any interest held by a person in a unit trust or collective investment scheme in terms of the Collective Investment Schemes Act, 2002(Act 45 of 2002)<sup>62</sup>.

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<sup>59</sup> S 1 of the Act – see page 13 of text below for definition

<sup>60</sup> S 26(1) of the Act

<sup>61</sup> S 1 of the Act

<sup>62</sup> S 1 of the Act

The right of access is to be exercised in accordance with the Promotion of Access to Information Act<sup>63</sup> or provisions of Section 26<sup>64</sup> of the Act and in accordance with the regulations<sup>65</sup> which provide for procedural formalities.

Information may be sought in respect of the records of the company in relation to the following:

- (i) The Company's Memorandum of Incorporation and amendments to it and any rules made by the Company<sup>66</sup>
- (ii) The records in respect of the Company's Directors<sup>67</sup>.
- (iii) Reports to annual general meetings and annual financial statements<sup>68</sup>.
- (iv) Notice and Minutes of Annual General Meetings, notice and minutes of shareholders meetings, including resolutions, and documents made available to the holders of securities in relation to each resolution, and written communication sent by the Company to all holders of the company's securities<sup>69</sup>.
- (v) The securities register of profit companies/members' register of non-profit companies<sup>70</sup>.

In addition to the rights outlined in Section 26 of the Act any Memorandum of Incorporation may establish additional rights<sup>71</sup> to information, subject to the Promotion of Access to Information Act<sup>72</sup>.

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<sup>63</sup> Act 2 of 2000

<sup>64</sup> S 26 of the Act

<sup>65</sup> Regulation 24(3) & (4) to the Act

<sup>66</sup> S 26(1)(a) of the Act

<sup>67</sup> S 26(1)(b) of the Act

<sup>68</sup> S 26(1)(c) of the Act

<sup>69</sup> S 26(1)(d) of the Act

<sup>70</sup> S 26(1)(e) of the Act

<sup>71</sup> S 26(3) of the Act

<sup>72</sup> Act 2 of 2000

### 3. **Meetings of shareholders and adoption of resolutions**

The Act introduces flexibility regarding the manner and form of Shareholders meetings<sup>73</sup>, quorum and the exercise of proxy rights<sup>74</sup>. In general, the provisions of the Act with regard to the procedural issues in relation to shareholders meetings reflect modernisation of company law in accordance with the stated intent of the Guidelines for Corporate Law Reform<sup>75</sup>.

It is however in the context of the adoption of Resolutions that pre-existing companies will need to pay particular attention to the provisions of the Act. The adoption of Resolutions apply from the effective date to every pre-existing company<sup>76</sup>. The Act provides that every resolution of the shareholders will be either an ordinary or a special resolution<sup>77</sup>. In respect of a special resolution, the Act provides that if such resolution is to be regarded as approved by shareholders, the resolution must be supported by at least 75% of the voting rights exercised on the resolution<sup>78</sup>. Although the Act provides that a Company's Memorandum of Incorporation may permit a different percentage of voting rights to approve any special resolution or one or more different percentages of voting rights to approve special resolutions concerning one or more particular matters, the Act provides that there must, at all times, be a margin of at least ten percentage points between the highest established requirement for approval of an ordinary and special resolution in respect of any matter<sup>79</sup>.

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<sup>73</sup> S 63 of the Act

<sup>74</sup> S 64 of the Act

<sup>75</sup> See footnote 16 \above

<sup>76</sup> Item 7(5)(d) of Schedule 5 to the Act

<sup>77</sup> S 65 (1) of the Act

<sup>78</sup> S 65(9) of the Act

<sup>79</sup> S 65 (10) of the Act

In order for an ordinary resolution to be approved, such resolution must be supported by more than fifty per cent of the voting rights exercised on the resolution<sup>80</sup> subject to a Company's right, in its Memorandum of Incorporation, to require a higher percentage of voting rights to approve ordinary resolutions concerning one or more particular matters<sup>81</sup>. This is subject to the proviso that the Company's Memorandum of Incorporation may not require a higher percentage of voting rights to approve an ordinary resolution for the removal of a Director than fifty per cent plus one.<sup>82</sup>

In the context of the percentages now endorsed by the Act for ordinary and special resolutions, of significance to pre-existing companies will be the latitude, in the Memorandum of Incorporation, to provide for a higher percentage of voting rights in respect of ordinary resolutions<sup>83</sup>, and, in the context special resolutions to provide for a different percentage of voting rights to approve the special resolution,<sup>84</sup> provided that the margin of ten percentage points between the highest established requirement for the approval of an ordinary resolution and the lowest established requirement for approval of a special resolution is maintained. While special resolutions may be higher or lower in terms of percentage, the Memorandum of

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<sup>80</sup> S 65(7) of the Act

<sup>81</sup> S 65 (8) of the Act

<sup>82</sup> S 65(8) read with S 71 of the Act which provides:

“1. despite anything to the contrary in a Company's Memorandum of Incorporation Rules, or any agreement between a company and a Director, or between any shareholders and a Director, a Director may be removed an ordinary Resolution adopted at a shareholders meeting by the persons entitled to exercise voting rights in an election of that Director, subsection 2.

2. Before the shareholders of a company may consider a Resolution contemplated in Sub-section 1-

a) the Director concerned must be given notice of the meeting and the resolution, at least equivalent to that which a Shareholder is entitled to receive, irrespective of whether or not the Director or Shareholder of the Company;

b) the Director must be afforded a reasonable opportunity to make a presentation, in person or through a representative, to the meeting, before the Resolution is put to a vote.”

<sup>83</sup> S 65(8)(a) of the Act

<sup>84</sup> S 65(10) of the Act

Incorporation may not provide for a lower percentage for special resolutions than sixty percent plus one, if the provisions of the Act in relation to matters for ordinary resolutions of fifty per cent plus is maintained. Similarly, while the Memorandum of Incorporation may determine the percentage required for special resolutions of up to one hundred per cent, in such case the required percentage for ordinary resolutions could not be higher than ninety per cent plus one.

In the light of the requirements for special resolutions, with regard, in particular to the approval of fundamental transactions contemplated by Chapter 5 of the Act<sup>85</sup>, and the need for a special resolution to authorise the Board to grant financial assistance<sup>86</sup>, pre-existing companies may well be better served by amending the Memorandum of Incorporation, sooner rather than later.

## **V TRANSACTIONS RELATING TO DISTRIBUTIONS, FINANCIAL ASSISTANCE, INSIDER SHARE ISSUES OR OPTIONS**

As one of the transitional provisions, the approval of any distribution, financial assistance, insider share issues or options are with effect from the effective date subject to the Act<sup>87</sup>. The application of the Act to these transactions arises even if the action in relation to the distribution or financial assistance has been approved by the shareholders before the effective date of the Act, notwithstanding anything to the contrary in the Company's Memorandum of Incorporation<sup>88</sup>.

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<sup>85</sup> Item 7(5)(d) of Schedule 5 to the Act read with S112, S113 and S114 of the Act

<sup>86</sup> Item 7(5)(6) of Schedule 5 to the Act read with S65(11)(f) of the Act

<sup>87</sup> Item 7(5)(d) of Schedule 5 to the Act

<sup>88</sup> See 87 above

'Distribution' is widely defined in the Act as meaning "a direct or indirect:

- (a) transfer by a company of money or other property of the company, other than its own shares, to or for the benefit of one or more holders of any of the shares, or to the holder of a beneficial interest in such shares, or that company or of another company within the same group of companies, whether -
  - (i) in the form of dividend;
  - (ii) as a payment in lieu of a capitalisation share, as contemplated in Section 47;
  - (iii) as consideration for the acquisition –
    - (aa) by the company of any of its shares, as contemplated in Section 48; or
    - (bb) by any company within the same group of companies of any shares of a company within that group of companies; or
  - (iv) otherwise in respect of any of the shares of that company or of any other company within the same group of companies, subject to Section 164(19);
- (b) incurrence of a debt or other obligation of a company for the benefit of one or more holders of any of the shares of that company or of any other company within the same group of companies; or
- (c) forgiveness or waiver by a company of a debt or other obligation owed to the company by one or more holders of any of the share of that company or of another company within the

same group of companies, but does not include any such action taken upon the final liquidation of the company”<sup>89</sup>

All distributions as so defined must be authorised by the Board<sup>90</sup>. In this regard, the provisions of the Act now provide, in keeping with a capital maintenance regime with a cornerstone of insolvency and liquidity, that the Board satisfy itself as to the solvency and liquidity<sup>91</sup> of the company immediately after completing the proposed distribution<sup>92</sup>. The Board is not only compelled to apply the solvency and liquidity test<sup>93</sup> but the provisions of the Act go further and provide that the Board of the Company is required by resolution to acknowledge that it has done so. If the distribution contemplated by the Board Resolution has not been completed within one hundred and twenty business days after the Board acknowledged the Company’s insolvency and liquidity, the Board must reconsider the solvency and liquidity with respect to the remaining distribution(s) to be made pursuant to the original resolution, order or obligation and the Board is further required not to proceed or continue with such distribution unless such further resolution acknowledging that it has done so, has been adopted<sup>94</sup>.

In applying the solvency and liquidity test, the Board is required to consider ‘all reasonably foreseeable financial circumstances of the company’<sup>95</sup>. This would include circumstances not yet disclosed or appearing in the accounting records or financial statements of the company although these must obviously be considered and the Act provides as much<sup>96</sup>. The introduction of the solvency and liquidity test when seen in the context of the codified standards for Directors conduct<sup>97</sup> and the liability of Directors<sup>98</sup> has far reaching immediate

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<sup>89</sup> S 1 of the Act.

<sup>90</sup> S 46(1) of the Act

<sup>91</sup> S 4 of the Act

<sup>92</sup> S 46(1)(e) of the Act

<sup>93</sup> See note 91 above

<sup>94</sup> S 46(3) of the Act

<sup>95</sup> S 4(1) of the Act

<sup>96</sup> S 4 (2)(a) of the Act

<sup>97</sup> S 76 of the Act

implications for pre-existing companies in the context of approval of distributions and financial assistance, in particular. In applying the solvency and liquidity test a director contemplating financial assistance, for example<sup>99</sup>, is required to carefully weigh up voting for or against the making of such decision. The Act now provides that if a Director (which includes an alternate Director) had been present at a meeting or participated in the making of a decision other than at a meeting (Section 74) and failed to vote against the resolution in respect of which financial assistance was provided to any person as contemplated by Section 44 of the Act, such conduct may give rise to personal liability of the director to the Company.<sup>100</sup>

In assessing the liability of the Director, in such circumstances, of further significance in terms of the provisions of the new Act, is the definition of 'knowing' employed in Section 71(3)(e). The Act defines 'knowing' as follows:

"knowing, knowingly or knows when used in respect to a person, and in relation to a particular matter, means the person either –

- (a) had actual knowledge of the matter; or
- (b) was in a position in which the person reasonably ought to have –
  - (i) had actual knowledge;
  - (ii) investigated the matter to an extent that would have provided the person with actual knowledge; or
  - (iii) taken other measures which, if taken, would reasonably be expected to have provided the

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<sup>98</sup> S 77 of the Act

<sup>99</sup> S 44(6) of the Act

<sup>100</sup> S 77(3)(e)(iv)

person with the actual knowledge of the matter.”<sup>101</sup>

Consequently, it is not only a question of actual knowledge on the part of a Director but all knowledge which should have been known to a Director after a reasonable investigation or other measures.

Pre-existing companies will also need to comply, notwithstanding any provision to the contrary in the existing Memorandum of Incorporation, with the provisions of the Act insofar as they relate to financial assistance for subscription of securities<sup>102</sup>, loans or other financial assistance to Directors<sup>103</sup>, distributions contemplated by Section 46<sup>104</sup>, capitalisation of shares<sup>105</sup>, and company or subsidiary acquiring the company’s shares<sup>106</sup>. Of particular relevance for the pre-existing companies would be the new provisions in the Act, with regard to the nature of the resolution required, when the resolution would remain operative for, and in general the application of the solvency and liquidity test in approving the particular transaction.

The consequence of not adhering the provisions of the Act are far reaching. The resolution or the agreement in breach of the provision of the Act would be void<sup>107</sup>. For Directors, the consequences involve personal liability<sup>108</sup>.

## VI CONCLUSION

While pre-existing companies are not compelled to proceed to amend their constitutional documents prior to the 29<sup>th</sup> of April 2013, they would

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<sup>101</sup> S 1 of the Act

<sup>102</sup> S44 of the Act

<sup>103</sup> S 45 of the Act

<sup>104</sup> S 46 of the Act

<sup>105</sup> S 47 of the Act

<sup>106</sup> S 48 of the Act

<sup>107</sup> S 44(6), S 45(6) of the Act

<sup>108</sup> S 44(5) and S45(6), S46(6) and S48(7) of the Act

be well advised to do so. The inherent risk of companies acting on the strength of their constitutional documents where the Act contains provisions of immediate application to the contrary pose an unacceptable risk to shareholders and directors. The submission of an amended Memorandum of Incorporation would have the further benefit of, incidentally and as part of the process of amendment, promoting cognisance on the part of shareholders and directors of the Act and its provisions and of their obligations in terms thereof. It is self evident that this knowledge should be gleaned sooner rather than later.