COMPANY LAW TIPS AND TRAPS

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1 PRESCRIBED OFFICERS

During consultation with clients, the question often arises as to which individuals in a company would be considered to be a Prescribed Officer in terms of the Companies Act 71 of 2008 (“the Act”), and what does this mean for such an individual? Is it merely a selection based on random function, or is there a logic and motivation driving who such individuals will be? You would have seen they have the same obligations as directors.

This article will set out to address the abovementioned questions in the light of the provisions of the Act, as well as relevant case law addressing this issue.

1.1 PRESCRIBED OFFICERS IN TERMS OF THE ACT

“The Act introduces the definition of a Prescribed Officer which, in terms of Regulation 38 of the Act, is a person who, despite not being a director of a company, exercises general executive control and management over the whole, or a significant portion of the business activities of a company or a person who regularly participates, to a material degree, in the exercise of general executive control and management over the whole, or a significant portion, of the business and activities of the company. This is the case irrespective of any particular title given by the company to the office held by the individual in the company or the function performed by the individual in the company.

The effect of being a Prescribed Officer in terms of the Act would be that such an individual would be subject to the same duties and liabilities of directors, including adherence to Section 75 and Section 76 of the Act, relating to personal financial interests and director’s standards of conduct. This would entail that such an individual would owe fiduciary duties to the company to act in the company’s best interest, not to make a secret profit or misappropriate opportunities that should be opportunities of the company.

1.2 APPLICABLE CASE LAW

In the matter of Volvo (Southern Africa) (Pty) Ltd v Yssel [2009] JOL 24109 (SCA), the court had to decide whether an individual rendering services to the appellant owed a fiduciary duty to the appellant. In this particular case, the appellant required a manager for its information technology division. The respondent was placed by a personnel placement agency in such position. During the course of rendering services to the appellant, the respondent entered into an agreement with the relevant personnel placement agency in terms of which the respondent would earn a commission if he arranged for personnel placed by other labour brokers at the appellant, to be transferred to the particular personnel placement agency that

placed the respondent. The respondent did not disclose this commission to be earned by him to the appellant.

The question before the court was whether the respondent owed a duty to the appellant to disclose such secret commission and whether the respondent was under a fiduciary duty to act in the best interests of the appellant and not his own.

In its judgment, the court did not refer to the provisions of the Act. However, the court sets out the following reasons for finding that the respondent did, in fact, owe a fiduciary duty to the appellant:

- The respondent occupied the most senior position in the appellant's information technology division.
- The fact that there was no contractual relationship between the appellant and the respondent is not of meaningful consequence. It is the position to which the respondent was appointed, as opposed to the contractual relationship, that determined what the appellant could expect from the respondent.
- The respondent attended to arrange matters between the appellant and its staff as an incident of his function as manager of the division.
- It is because of his position as manager of the division that the appellant could be induced to relax the care and vigilance it would generally have exercised if it was dealing with a stranger.

1.3 CONCLUSION

If one considers both the requirements of Regulation 38 of the Act, as well as the reasons for the judgment handed down in Volvo (Southern Africa) (Pty) Ltd v Yssel [2009] JOL 24109 (SCA), it has to be concluded that the determination of who will be a Prescribed Officer in term of the Act is not determined merely as a selection based on random function. In my view, the logic and motivation applied by the court Volvo (Southern Africa) (Pty) Ltd v Yssel [2009] JOL 24109 (SCA) fuels how the requirements of Regulation 38 of the Act should be applied. It is clear that an individual should only be deemed to be a Prescribed Officer if there is good reason to state that such individual stands in a position of trust to the company, and as such, such an individual should not allow their own interests to prevail over the best interest of the company."

Phillip Kruger

2 REMOVAL OF DIRECTORS

2.1 SECTION 71 IN THE ACT IS EQUIVALENT TO SECTION 220 IN THE 1973 ACT

S71(1) is a crucial ***unalterable provision*** which entrenches the fundamental common law principal that the ***shareholder is king*** by allowing the shareholders to ***remove a director at any time and for any reason they think fit***. It provides that despite anything to the contrary in a company's MOI or rules, or any agreement between a company and Director or between any shareholder and director, ***a director may be removed by an ordinary resolution***, adopted at a shareholders meeting by the persons entitled to exercise voting rights in the election of that director.

Only the person's entitled to exercise voting rights in election of a particular director may remove that director. The way this works is that the director must be given an opportunity to prevent removal from happening by ***stating his case at the meeting*** where the vote is going to take place. It is not necessary for the resolution to give reasons as to why the shareholders want the director removed.

At this point it would be a good idea to understand what s 66(4) says – a company's MOI may provide for the director appointment and ***removal of one or more directors*** by any person who is ***named in the MOI***. This means that the person so named may appoint and remove directors. It appears that this person has a right to appoint 50% of the directors as the other 50% must be appointed by the shareholders.

The MOI cannot provide that a higher percentage on the voting rights for the removal of a director i.e. more than 50% of the voting rights is required to remove the director.

The old Act provided that in order to remove a director 28 days special notice was required. This requirement has been abolished in the 2008 act.

As well as the above in terms of s 71(3) the board has been given the power to remove a Director even in limited circumstances. It provides that if a company has more than two directors which is obligatory for public companies and non-profit companies and a **shareholder** or a **director** has alleged that a director has become ***ineligible*** or ***disqualified*** or has become ***incapacitated*** to the extent that the director is unable to perform the functions of a director and he is unlikely to regain that capacity within a reasonable time – (these cannot be grounds as contemplated in s 69(8)(a) which are the disqualification grounds), or has neglected or been derelict in a performance of the functions of a director, they can be removed.

The board (other than the director concerned) must determine the matter by resolution, i.e. the remaining directors may determine whether or not the allegation is correct by a simple majority vote and may remove the director.

Prior to the meeting the ***director must be given notice*** of the meeting including a copy of the proposed resolution setting out the reason for it with sufficient specificity to reasonably permit the director to prepare and present a response. The director concerned 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 the vote.

Unlike s 71(1) the board may remove a director in the circumstances described in 71(3) irrespective of whether the Director concerned was originally appointed or elected by shareholders.

Where the situation has occurred that the ***person who originally appointed the director*** as specified in s 66(4)(a) (i) or who voted in favour of the director may make an application to court who may either confirm the board's determination or remove the director from office on the grounds specified in 71(3).

One cannot remove a director by around robin resolution under S60 as in this way the director cannot present his case.

S 71(3) does not apply if a company has fewer than three directors. In the circumstances contemplated in s 71(3) any director or shareholder of such a company may apply to the tribunal to make a termination as contemplated in s 71(3). There is another innovation in that various people can apply to court to declare a Director either delinquent or thus prohibited from being a director or under **probation** and thus restrict the serving as a director within the condition of that probation.

S 162 sets out this remedy, it is available to a company, a shareholder, director, company secretary or prescribed officer of a company as well as a registered trade union that represent the company's employees or another representative of a company's employees. Any of these persons may apply to court for an order declaring a director of that company or person who within 24 months immediately preceding the application was a director of that company. For more information on this you need to read s 162.

3 RULES OF THE COMPANY

The **Rules** of a company is a new concept that comes out of the United States or Canada. Rules are very similar to bi-laws in a City Council. They are an addition to the constitution of the city council and would probably deal more with operational details not contained in the constitution of the city council.

The rules of a company are in fact an extension of the MOI and are designed to govern the internal affairs of the company. The problem with rules are that there are no examples and no definition of what should be included in the rules. The rules may deal with any corporate governance issues not contained in the act or in the MOI. The rules cannot be in conflict with the act or the MOI.

The rules and the MOI are in fact binding on the following in terms of S15(6);

- between the company and each shareholder
- between or among the shareholders
- between the company and each director or prescribed officer of the company in exercise of their functions within the company
- any other person serving the company as a member of a board committee in exercise of their respective functions of the board within the company.

The last two are new and overrides the long-established principle that the company's constitution is binding on a company and its shareholders only and only in the capacity of shareholders not directors. Owing to this change each party can enforce the MOI or the rules against one another in any lawful manner, this could be by way of an interdict or a damage claim arising from a breach.

The rules create a contract between the abovementioned parties in the abovementioned capacities. Please note that if the director or shareholder act in another capacity to the company then the rules can't be applied.

The rules can be changed or created quite easily without changing the MOI. Remember the rules are ***over and above***, or one can say an ***extension of the MOI***. It should be noted that the ***MOI will always take precedence*** over the rules. Where there are rules inconsistent with the MOI or the Act, these rules will be void to the extent of the inconsistency. The rules are still subject to anti-voidance sections of the Act. Rules cannot be used to alter the ***unalterable***

provisions of the act. One can make unalterable provisions stronger by inserting clauses in the MOI.

The advantage of having rules is that the directors can in fact ***compile*** and ***publish*** the rules and once the rules have been published, they are binding on the company. Regulation 16(1) provides that any rules of a company must be filed on Form Cor 16.1 within 10 business days after being published by the company.

See s15(4)(b), the board may change or append rules in any manner. It is important to know that the rules must be ***ratified*** at the next available shareholders meeting by way of an ordinary resolution. After the rules have been ratified the necessary form has to be filed with the CIPC. Regulation 16.2 is to indicate the rules have been ratified or rejected. It is not necessary to call a shareholders meeting to specifically ratify the rules, the ratification can wait until the next shareholders meeting.

Before the rules have been ratified, they are nevertheless still binding even though they are at an interim stage. What happens when the rules fail to be ratified (I.e. the shareholders vote against the rules or a particular rule) at the next general meeting? The position in this case is that even though they were in an interim stage everyone can rely on them to that point as everyone is bound by them. Once a rule has failed the ratification vote they are therefore no longer binding from that point in time. Once a rule has failed ratification it cannot be reintroduced by the directors for a further 12 months unless approved in advance by an ordinary shareholders resolution.

The advantage of compiling rules is that the directors can do it very easily without going to shareholders and the rules can be binding whilst waiting for ratification. In smaller companies it could be that ratification takes a long time because there are no shareholders meeting to ratify the rules.

Rules would deal with matters of meetings, the maximum number of Directors and potentially anything in relation to the corporate governance not in conflict with the MOI or the Act.

Some examples could be;

- Authority level of chairman of the board and frequency of director's meetings.
- Financial and marketing strategy
- Succession planning

4 REGULATION 31 CONVERSION OF PAR VALUE SHARES

4.1 INTRODUCTION

Where a pre-existing company (a company that was formed under the old companies act) has par value shares at the effective date (the date the Companies Act 2008 came into existence) on 1 May 2011 and the board of directors wish to increase the authorised number of the par value shares then they have to adopt the procedure as set out in terms of Regulation 31 of the Companies Act 2008.

4.2 THE LAW

Schedule 5, Section 6 (2) says that **par value** shares may continue to exist forever after the effective date subject to any regulations made by the minister.

Where directors wish to increase the authorised share capital as there are not enough shares to issue the formalities of Regulation 31 must be carried out.

It is important to note that many of the Companies Act Regulations refer to the various sections in the act on ***how to*** carry out the procedures. This particular regulation 31 does not appear to be based on the act as it appears to be an afterthought actually extending the requirements of the law with even SARS having some input in regard to some tax issues.

In terms of section 36(2)(a) of the act a ***change of the authorised share capital*** is in fact an amendment to the MOI and requires a special resolution and submission of form **CoR 15.2** together with the **special resolution**.

Form CoR 31 and regulation 31 (3) appear to be in conflict with this section as the regulation says that when a company has par value shares for which no shares are in issue a director's resolution and form **CoR 31** will be sufficient to request the CIPC to change the share class from par value to no par value. It appears Form CoR 31 is in conflict with the act as even though no shares are in issue this is a change to the MOI and it would seem to be necessary to file a special resolution and form CoR 15.2 to make this change. This regulation specifically allows a director's resolution in place of a shareholder's resolution, where you have the situation of a share class where no shares are in issue as no shareholders are affected by this. It is necessary to file the CoR 31 and CoR 15.2 and the director's resolution changing the MOI.

Please also note that in terms of Regulation 31 (5) (b) the directors may issue **par value shares** if there are ***sufficient authorised*** shares available. Where no changes in the share capital is envisaged par value shares can remain in existence forever as there is no minister's regulation to this affect.

Regulation 31 (5) (c) says that an amendment to the MOI may be filed at no charge in order to change a class provided that sub-regulations 6 to 11 are complied with. This regulation kicks in when a company wishes to increase its authorised share capital.

4.3 SARS

It is interesting that sub-regulation 6(a) says that this amendment must not be designed substantially or predominantly to ***evade the requirements of any applicable tax legislation*** and 6(b) says that such conversion will ***only be approved by a special resolution adopted by the holders of the shares for each such class*** and ***a further resolution adopted by a meeting of the company shareholders*** called for that purpose.

4.4 BOARD REPORT

Sub-regulation 7 deals with the ***board report*** that must be sent out with the proposed special resolution to convert par value shares to no par value shares. The following items should be dealt with in the board report.

a. The report must state ***all information that may affect the value*** of the securities caused by the proposed conversion; and

b. The report must ***identify the class of holders*** of the company securities affected by the proposed resolution and;

c. The report must ***describe the material effects*** that the proposed conversion will have on the ***rights of any holders*** of shares, and;

d. The report must ***evaluate any material adverse effects*** of the proposed arrangement ***against any compensation*** to those persons who receive compensation owing to the conversion.

It appears that the board report is designed to indicate if there is a change to any of the rights of shareholders which ***may trigger a capital gains event*** as the board report and the special resolution must be filed at SARS.

Regulation 31 (8) says that the company must ***publish a special resolution*** contemplated in sub-regulation (6) together with the ***report required*** by sub regulation (7) which must be made available to the shareholders before the meeting (which ***must have proper notice***) at which

the resolution is to be considered. It appears that the ***notice cannot be waived*** in this instance.

The special resolution and the report must be filed with the CIPC as well as the South African Revenue Service by emailing the special resolution and board report to ***regulation31@sars.gov.za***. We suggest that a certified copy of the email proving submission to SARS or a copy of the documents with the SARS official stamp will reduce the chance of rejection by the CIPC.

Sub Regulations 9 to 11 deals with various instances where applications can be made to court to obtain a declaratory order in regard to this conversion.

4.5 SPECIAL RESOLUTION

I have set out an example of the kind of wording that should be used in regard to the Special Resolution of a smaller company. Perhaps one should put in a preamble as to the reasons why the special resolution needs to be taken.

REASON FOR THE SPECIAL RESOLUTION

The Companies Act 2008 regulations do not allow the increase of authorised par value shares where there are no further authorised par value shares to issue. The directors have decided that in order to comply with the requirements of the act that the share capital of the company must be converted from par value to no par value shares.

SPECIAL RESOLUTION 1

Resolved that the authorised Ordinary Share Capital comprising of 10,000 shares which have a par value of R1 each is converted to 10,000 Ordinary Shares of no par value, each share to rank pari passu in every respect with the existing shares of the company.

Comment – it's important to show that all the rights and limitations remain the same on the conversion. SARS are looking for a capital gain event.

SPECIAL RESOLUTION 2

The authorised Ordinary Share Capital of 10,000 shares of no par value be increased to 100,000 shares of no par value to rank pari passu in every respect with the existing shares of the company.

Comment – it's a good idea to increase the authorised number at the same time.

ORDINARY RESOLUTION

3. Resolved that subject to the passing of special resolution number 1 that the Ordinary Share Capital account of R10,000 and the Share Premium account related to this share capital of R40,000 both be transferred to the stated capital account of the company.

Comment; It may be that the company wishes to retain the share premium account as they may want to repay this to shareholders at a later time. Consider this in relation to an actual buy back of shares. It will be much easier to just pay back the share premium as opposed to buying back shares because of the compliance issues in a share buyback. There is no reason why the share premium account cannot be retained.

REPORT TO ACCOMPANY THE SPECIAL RESOLUTION

An example of the board report in the case of companies which are small companies and where shareholders rights are not affected will be as follows:

"Owing to the fact that the board of directors need to increase the authorized share capital of the company to allot more shares it is proposed that the ordinary 10,000 shares of par value be converted to 10,000 ordinary shares of no par value in order to meet the requirements of the Companies Act 2008.

10,000 issued ordinary shares of par value, details of which are contained in the share register which is available for inspection at the registered address of the company will be affected. The share certificates of par value as indicated in the share register will all be cancelled and a new class of shares of no par value will be created and the shares will be re-issued under the same certificate numbers on registration of the special resolution.

There is no effect on any of the rights of any shareholder.

Owing to the fact that no rights of any shareholder have been affected by this conversion no compensation has been paid out."

4.6 SUBDIVISION OF SHARES

In the case of a subdivision of shares whether they are ***par or no par value***, is that the ***number of shares in issue are increased*** (i.e. more shares are created by the sub division), and the share capital ***value remains the same***. The Companies Act 2008 does not deal with the subdivision of shares at all. We however need to differentiate the position between ***par value*** and ***no par value*** shares as subdivision is slightly different.

Where the shares are, ***par value*** a conversion of the shares must first take place as a subdivision of the authorised shares is also necessary. This is necessary as the number of authorised shares must be increased in order to carry out the subdivision. We therefore need

to look at the requirements of Regulation 31 and comply with them first ensuring that all the shares are converted to NPV shares before we run this procedure.

In a ***par value*** share situation, the authorised shares are subdivided as well as the issued shares because of the nominal value of the shares. As we can't increase the number of authorised par value shares, we must convert the shares in terms of regulation 31 first making sure that there are a sufficient number of authorised shares. The increase in the number of authorised shares must be part of the conversion process. In my opinion a subdivision of no par value shares is only performed on the issued shares and is not necessary to do so on the authorised shares as there is no value placed on the authorised shares. We would just need to make sure that the authorised shares are sufficient in number to do the subdivision of the shares.

On conversion, from PV to NPV it is required to have a special resolution and of course the board report with all the necessary points as specified in Regulation 31 above.

There is a view that one can't do a subdivision of no par value shares. I disagree because this may very well be of commercial necessity to prepare for a transaction or to create better trading conditions for a share that is listed. You certainly can do a conversion of no par value shares that have been issued as there is a value. A subdivision is really just an increase in the number of shares, without affecting the total value of the share capital account. One could also do it by allotting additional shares at no value but this certainly does not make any sense. Please remember we are talking about no par value shares in this instance.

I do not see why we are unable to do this; there is nothing in the law that prevents this from being done in my view.

This is how you do the subdivision of par value shares;

Let's say you have a company with 1000 shares which have a par value of R1 each and authorised shares of 10000. I.e. total capital is R1000 and the directors wish to create 10,000 shares by way of a sub-division.

1. Convert the 1000 PV shares to NPV shares and increase the authorised number of shares to 50000.

2. Prepare a special resolution and the board report for submission to CIPC and SARS to convert PV to NPV and increase the authorised number of the NPV shares as part of the same resolution. Remember this affects the MOI and needs to be submitted to the CIPC.

3. Do not mention subdivision of shares in the resolution submitted to the CIPC. This resolution must cover the conversion of the shares and an increase in the authorised share capital of the company only, say to 50,000 shares or whatever the requirement is.

4. After you have approval of the special resolution in 2 above you then prepare another special resolution sub-dividing the issued shares to the number you want. This means you increase the number of shares in issue but retain the total value of the shares. This special resolution does not need to be filed at the CIPC as all you are doing is increasing the number of shares in issue and the CIPC does not need to know about this in terms of the new Companies Act 2008.

4.7 CONCLUSION

Regulation 31 clearly was an afterthought with SARS getting involved. I don't see why there was this need for SARS to get involved in the companies act as they could quite as easily put this legislation into the income tax acts. This procedure was probably intended for larger companies but clearly affects all small companies unnecessarily creating a huge amount of additional company secretarial labour.

One also needs to look at all the tax consequences for the transactions above and the future tax situation of the shares converted or subdivided or share premium paid back.

4.8 QUESTION ON SHARE PREMIUM

A company converts its Par Value shares (PV) – 100,000 shares in issue to No Par Value (NPV) shares in terms of **Regulation 31**. There is a rand balance on the share capital and on the share premium account, of R100,000 each. Is it necessary to move the balance of share premium to the NPV share capital account – stated capital or can the company leave it as a share premium account?

ANSWER

It would be a good idea to leave the balance in share premium with a view to a future payback of capital when the company is in a position to do so instead of paying a dividend. By doing it this way the company avoids appointing an independent expert or even going to the TRP because it's regulated as it does not fall into the ambit of a share buyback. Paying back share premium is just a method of paying back share capital without all the formalities. The directors would need to obviously comply with all the ***distribution rules*** including the ***solvency and liquidity test***.

The share capital account before the transaction is;

Share capital	R100,000	Par value shares of R1 each
Share Premium	R100,000	
Total Share Capital	R200,000	

After the transaction it could be as follows

Share capital – stated capital account	R100,000	100,000 No Par value shares of R1 each
Share Premium	R100,000	
Total Share Capital	R200,000	

However, we could make it look like this;

Share capital NPV	R10,000	10,000 No Par value shares of R1 each
Share capital PV	R90,000	90,000 par value shares of R1 each transfer to share premium.
Share premium	R100,000	
Total Share Capital	R200,000	

The share capital of the company in the above instance is 10,000 shares of no par value of R1 each. The R90,000 is retained in the old share capital account and should be transferred to the share premium account.

5 S45 - LOANS OR OTHER FINANCIAL ASSISTANCE TO DIRECTORS

5.1 INTRODUCTION

S 45 is the equivalent of S226 in the old Act and s 45(2) provides that except to the extent that the companies MOI provides otherwise and subject to s45(3) and s45(4) the board may also authorize the Board of companies to approve direct or indirect financial assistance to

- a director or prescribed officer
- a director or prescribed officer of a company which is related or inter-related to the company
- a company or corporation who is related or inter-related to the company
- a member or corporation who is related or inter- related to the company
- a person who or which is related to the company or any of the above.

S 45 like s 44 does not define financial assistance, all that it says is that financial assistance includes lending money, guarantee a loan or other obligation and securing any debt obligation but does not include lending money in the ordinary course of the business or of a company whose primary business is the lending of money, or an accountable advance to meet legal expenses of a matter concerning the company or to meet anticipated expenses to be incurred

by the person on the person's behalf or an amount to defray the personal expenses for the removal at the company's request.

The fundamental difference between s 44 and s 45 is that s 44 is for the financial assistance for the subscription or purchase of securities whereas the purpose of s 45 is for financial assistance for ***any particular purpose***. The Act does not provide a description of financial assistance in s 45(2) and the words direct or indirect widens the type of financial assistance that may be given. One also needs to look at the definition of ***related or inter-related***.

The way the wording of the section is couched is that it applies to a much wider group of people including intergroup loans which are everyday incurrences in larger groups of companies. There is also a danger that such loans may be in the hands of controlling shareholders which if made could be detrimental to the company.

The experts feel that the situation in regard to S45 is too wide and a practical consequence is that in a group of companies the company will have to table a special resolution every second or bi-annual shareholders meeting for approval of loans to other companies that form part of the group. Another thing that has to happen is that despite the special resolution with every loan the board has to satisfy the **solvency and liquidity test** as well as the fact that the terms of the financial assistance as proposed are **fair and reasonable** to the company.

The board also has to make sure that whatever terms there are in the MOI have been complied with.

5.2 S45 – ADDITIONAL DISCLOSURES

There is also a new disclosure in terms of S45(5) which is not a requirement in S44 which provides that if a resolution in terms of S45(2) is adopted the company must provide written notice of that resolution to all shareholders unless every shareholder is also a director and to any trade union, representing its employees.

There are two conditions where this is applicable, this disclosure must be provided within 10 business days after the resolution is adopted, if the total value of all the total debts or obligations of assistance contemplated in the resolution together with any other previous resolutions during the financial year exceeds one tenth of 1 % of the company's net worth at the time of the resolution or within 30 business days after the end of the financial year in any other case.

In terms of S 45(6) if the granting of such financial assistance is in conflict with any term in the MOI then the transaction is void.

5.3 KEY TAKE AWAYS FORM THE STEINHOFF CASE

The recent Steinhoff case (detailed below) sheds important light on Section 45 of the Act, which must be considered by the board when contemplating the approval of financial assistance in terms of Section 45 thereof.

The key takeaways from the Steinhoff case, which are relevant in respect of Section 45 financial assistance, can be summarized as follows:

- A foreign company falls within the meaning of a "corporation" as set out in Section 45(2) of the Act.
- The solvency and liquidity test, set out in Section four of the Act, must be applied with reference to the documentation and information available to the board at the time that such financial assistance was approved, and not with the benefit of hindsight.
- The restatement of a debt on different terms and conditions, and involving at least one different party, is the creation of a fresh debt and will need to be specifically approved by the board in terms of Section 45 of the Act, even where the previous financial assistance was approved by the board.
- Failure to comply with the provisions of Section 45 of the Act will render the financial assistance void and may result in personal liability for the individual members of the board who authorized such financial assistance, in certain circumstances.

5.4 Take Aways From The Constantia Case

- The decision of the SCA in the Constantia case is significant in that has substantially and, some might say, radically reduced the universe of transactions to which section 45 might otherwise apply and which practitioners have considered to fall within the ambit of section 45. The approach until the SCA's decision in the Constantia case would have been to conservatively treat every transaction with a related person with a financial element (e.g. a sale to a related person at a discounted price or a donation) as "financial assistance" for the purposes of section 45. The judgment removes a sizable burden from boards of directors having to consider whether transactions falling outside of those expressly mentioned in the definition of "financial assistance" would constitute "financial assistance". Boards should more easily be able to determine whether the transaction in question involves lending money, guaranteeing a loan or other obligation or securing a debt or obligation. However, it must be noted that "securing" does not only mean so-

called "hard" security (such as a mortgage bond, cession in security or share pledge), but any agreement or transaction which secures a debt or obligation (e.g. in the Constantia case, the indemnity was seen as a method of providing security). It is also important to take into account that if a transaction is designedly disguised so as to escape the provisions of section 45 but actually falls within those provisions, it is in fraudem legis and will be considered to be within the provisions of section 45.

- In conclusion, the judgment in the Constantia case is noteworthy for the boards of directors of all South African companies. It provides clarity as to the definition of "financial assistance" under section 45 of the Companies Act. It also provides warning as to the risks of non-compliance with the substantive requirements of the section 45 and that care must be taken to ensure that all such requirements are met strictly when entering into a transaction to which section 45 applies.
- Michelle du Plessis (Trainee Lawyer, White & Case, Johannesburg) contributed to the development of this publication.

5.5 EXAMPLE OF THE SPECIAL RESOLUTION REQUIRED

This special resolution is with the courtesy of Murray and Roberts

Provision of financial assistance to any company related or inter-related to the Company or to any juristic person who is a member of or related to any such companies

“RESOLVED THAT, as a general approval, the Company may, in terms of section 45(3)(a)(ii) of the Companies Act, 71 of 2008, as amended (“Companies Act”) and subject to compliance with the remainder of section 45 of the Companies Act, provide any direct or indirect financial assistance (‘financial assistance’ will herein have the meaning attributed to it in section 45(1) of the Companies Act) that the board of directors of the Company may deem fit to any related or inter-related company or to any juristic person who is a member of or related to any such companies (‘related’ and ‘inter-related’ will herein have the meaning so attributed in section 2 of the Companies Act) (on the terms and conditions, to the recipient/s, in the form, nature and extent, and for the amounts that the board of directors of the Company may determine from time to time).”

Reason for and effect of special resolution number 1:

The reason for and effect of special resolution number 1 ("Special Resolution"), if adopted, will be to confer authority on the board of directors of the Company to authorise financial assistance to companies related or inter-related to the Company, or to any juristic person who is a member of or related to any such companies generally as the board of directors of the Company may deem fit, on the terms and conditions, and for the amounts that the board of directors may determine from time to time, for a period of about fifteen months up to and including the 2012 annual general meeting of the Company from the date of adoption of the Special Resolution, and in particular as specified in this special resolution. The granting of the general authority would obviate the need to refer each instance of provision of financial assistance in the circumstances contemplated in the Special Resolution for ordinary shareholder approval.

This general authority would assist the Company with, inter alia, making inter-company loans to subsidiaries of the Company, or inter-related companies, as well as granting letters of support and guarantees in appropriate circumstances. This would avoid undue delays and attendant adverse financial impact on subsidiaries, or inter-related companies, as it would facilitate the expeditious conclusion of negotiations.

This general authority would be valid up to and including the 2012 annual general meeting of the Company. In the event that the Special Resolution is adopted by the ordinary shareholders of the Company, thereby conferring general authority on the board of directors of the Company to authorise financial assistance to companies related or inter-related to the Company or to any juristic person who is a member of or related to any such companies, then the board of directors of the Company shall not authorise any financial assistance contemplated in such Special Resolution unless the board:

1. is satisfied that immediately after providing the financial assistance, the Company will satisfy the solvency and liquidity test contemplated in section 4 of the Companies Act (section 45(3)(b)(i)); and

2. is satisfied that the terms under which the financial assistance is proposed to be given are fair and reasonable to the Company (section 45(3)(b)(ii)); and

3. has ensured that any conditions or restrictions in respect of the granting of financial assistance set out in the Company's Memorandum of Incorporation have been satisfied (section 45(4)).

This Special Resolution does not authorise the provision of financial assistance to a director or prescribed officer of the Company.