Corporate & Commercial ALERT

11 OCTOBER 2023

CLIFFE DEKKER HOFMEYR

INCORPORATING
KIETI LAW LLP, KENYA

IN THIS ISSUE

FOR MORE INSIGHT INTO OUR EXPERTISE AND SERVICES

KENYA

Private placement as an investment mechanism in Kenya

Recently, fintech firm Lipa Later Group announced the closure of a KES 500 million privately placed debt issuance as part of its innovative financing solutions. This announcement exemplifies private placement as an alternative investing mechanism to public offers. In light of this announcement, this alert spotlights the legal and procedural aspects of private placement and details reasons why companies should consider exploring private placement to seek external funding from investors.

What is private placement?

Private placement/offering is a type of funding of securities which are sold through a private offering rather than the conventional offering to the public. In Kenya, the Capital Markets (Securities) (Public Offers, Listing and Disclosures) Regulations, 2002 classify the type of offers that qualify as private placements.

An offer is considered a private offer where the securities are offered to not more than 100 persons; to members of a club or association with a common interest in the affairs of the club or association and use of the proceeds of the offer; or to a restricted circle of persons who are sufficiently knowledgeable to understand the risks involved in accepting the offer. In addition, offering securities of a private company to its employees or their families is also considered a private offering.

How can a company raise money through private placement?

Notably, private placements/offerings are not subject to onerous reporting requirements to the Capital Markets Authority and are thus considered a cost-effective way to raise capital without an initial public offering. Moreover, this investment mechanism is considered to be a quicker way to raise capital from a limited number of investors.

Section 30B of the Capital Markets Act requires an issuer of a private placement offer to submit a short-form prospectus to the Capital Markets Authority (Authority) for approval. Further, the issuer should file an information notice with the Authority where the minimum amount which may be paid under the offer is not less than the amount prescribed by the Authority. Similarly, the information notice is to be filed where the securities are denominated in an amount prescribed by the Authority.

The LEGAL 500
EMEA

Corporate, Commercial/M&A 2023 Rankings

Corporate & Commercial practice is ranked in Tier 1.

CDH Kenya's Corporate & Commercial practice is ranked in Tier 3.

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Willem Jacobs | David Pinnock

Recommended Lawyers:
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Justine Krige | Sammy Ndolo
David Thompson | Roxanna Valayathum
Njeri Wagacha

Next Generation Lawyers:
Justine Krige

Hall of Fame:
Ian Hayes

KENYA

Private placement as an investment mechanism in Kenya

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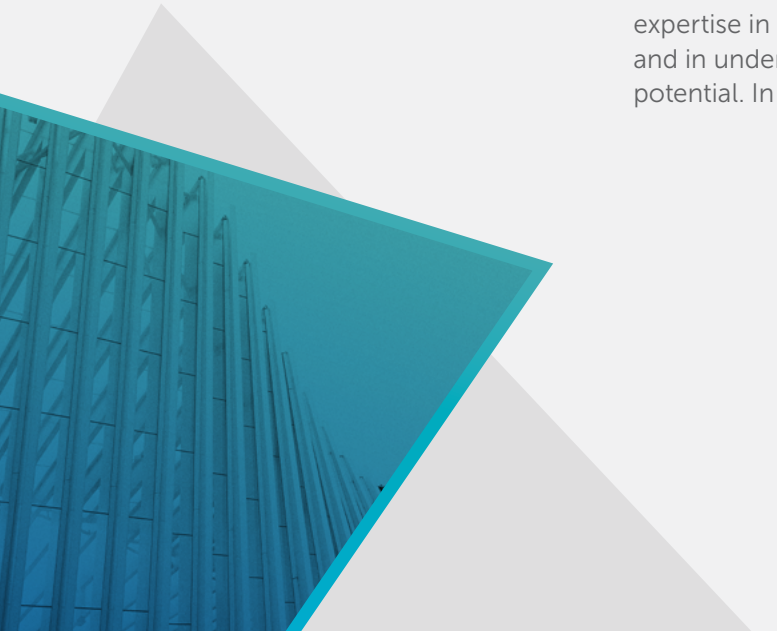

Private placement/offerings can be utilised by both small and big companies. Smaller companies can use this investment method where they lack the reputation or financial strength to appeal to a broad base of investors and cannot afford the expense of a public offering. Conversely, bigger firms can use private placements/offerings where a company needs significant funding and prefers seeking private investors with deep industry expertise.

Why private placement?

Private placement/offering enables companies to control the funding process and work directly with veteran investors who have extensive expertise in the company, its industry, and in understanding growth potential. In addition, companies avoid the need for an in-depth prospectus and detailed ongoing disclosure requirements that accompany public offers which enables them to have a short turnaround time and be less costly to set up.

Overall, start-ups and large companies can use private placement as an alternative investment channel to facilitate expeditious investment and avoid strenuous regulatory requirements for public offers. Companies looking to utilise this investment model should get legal advice to ensure that the offer complies with the requisites of a private placement/offering under the Capital Markets (Securities) (Public Offers, Listing and Disclosures) Regulations, 2002 and the Capital Markets Act.

Njeri Wagacha and Joseph Macharia

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SOUTH AFRICA

Inside out? A discussion on the case of *The Butcher Shop and Grill CC v Trustees for the time being of the Bymyam Trust*

Disregarding the corporate personality of a company is a well-established departure from the principle that a company is a separate legal entity distinct from its shareholders.

While the doctrine is part of our common law and rationale for its use can be found in case law, the courts were bestowed statutory entitlement to disregard the corporate personality of a company by virtue of section 20(9) of the Companies Act 71 of 2008 (Companies Act), which reads as follows:

> *"If, on application by an interested person or in any proceedings in which a company is involved, a court finds that the incorporation of the company, any use of the company, or any act by or on behalf of the company, constitutes an unconscionable abuse of the juristic personality of the company as a separate entity, the court may:*
>
> *(a) declare that the company is to be deemed not to be a juristic person in respect of any right, obligation or liability of the company or, of a shareholder of the company or, in the case of a non-profit company, a member the company, or of another person specified in the declaration; and*
>
> *(b) make any further order the court considers appropriate to give effect to a declaration contemplated in paragraph (a)."*

In the recent case of *The Butcher Shop and Grill CC v Trustees for the time being of the Bymyam Trust* [2023] (5) SA 68 (SCA), the Supreme Court of Appeal (SCA or the court) questioned whether section 20(9) of the Companies Act was a codification of the common law. In other words, did the section replace the common law in relation to when the corporate personality of a company may be disregarded? In line with previous judgments, the SCA affirmed that the section does not contain language which evidences an intention to replace the common law, nor does it define a set of circumstances in which a court may disregard the separate legal personality of a company, rather section 20(9) **supplements** the common law.

Having answered that question, the court drew from previous judgments in setting out the guiding principles for disregarding the corporate personality of a company:

- Firstly, a court has no general discretion to simply disregard a company's separate legal personality whenever it considers it just to do so.
- Secondly, as a matter of policy, the separate corporate personality ought to be upheld. 'Piercing' or 'lifting' of the corporate veil will not occur lightly, and then only when considerations of policy favour it.
- Thirdly, the balancing of policy considerations will only arise where there is some element of fraud, abuse or dishonesty in respect of the corporate personality.
- Fourthly, the purpose of piercing the corporate veil is to fix the persons responsible for abuse with liability. It also emphasised that, abuse of the distinction between the corporate entity and those who control it should result in some unfair advantage to them.

SOUTH AFRICA

Inside out? A discussion on the case of *The Butcher Shop and Grill CC v Trustees for the time being of the Bymyam Trust*

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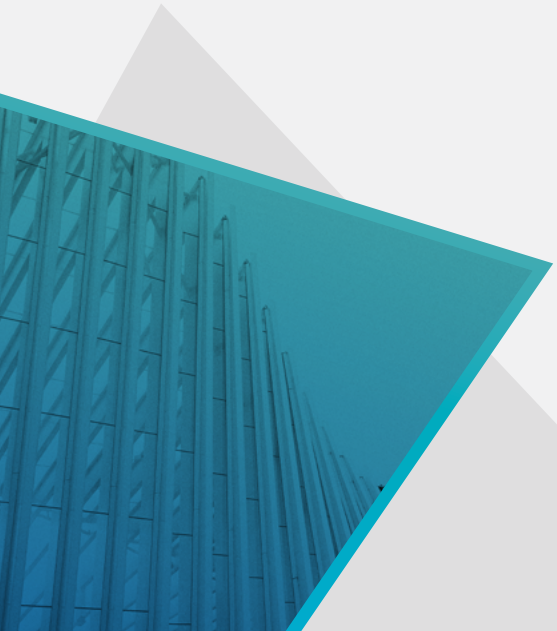

The doctrine is traditionally used as a remedy for "*outsiders*" wanting to hold those controlling the company on the "*inside*" responsible for its obligations, typically where there has been abuse of the juristic personality of the company through fraud or dishonesty. However, in this case the SCA had to delve further and consider whether, in our law, the doctrine was broad enough to encompass an "*inside out*" approach in order to be utilised as a remedy by shareholders of a company seeking to have the corporate identity of the company disregarded to advance the rights which would otherwise accrue to the company, as their rights. This type of remedy is also referred to as "*insider reverse piercing*" of the corporate personality of a company and even in international jurisdictions it is currently uncommon, if not rejected.

Facts

Briefly, the facts were as follows: the respondent, trustees for the time being of the Bymyam Trust (Trust), concluded a lease agreement with The Butcher Shop and Grill CC (Butcher Shop) in respect of certain premises for the purpose of conducting business as The Butcher Shop and Grill (the restaurant).

The Trust subsequently became aware that the premises were occupied by Apoldo Trading (Pty) Ltd (Apoldo), which was conducting the business of the restaurant. The Trust and the Butcher Shop then entered into an addendum to the lease agreement wherein the Trust granted consent to the subletting arrangement with Apoldo. The Butcher Shop agreed to remain responsible for all the terms and conditions of the lease and Apoldo agreed to be "*jointly and severally equally responsible*".

Due to the COVID-19 national lockdown restrictions the Butcher Shop withheld payment of rent. In 2020, the Trust launched an application in the Western Cape High Court (High Court) in which it claimed payment of amounts due (the main application) and the Butcher Shop opposed and filed a counter application. The Butcher Shop's case was that its loss of the use and enjoyment of the premises due to the lockdown restrictions caused it a significant loss of turnover in its business, which entitled it to remission of rent. Insofar as the sub-tenancy of Apoldo was concerned, it based its case upon the following two contentions:

- a lessee is entitled to claim remission of rental arising from the loss of a sub-lessee's beneficial occupation on account of *vis major or casus fortuitus*; and
- in the alternative, that the Butcher Shop and Apoldo were in effect, Mr Pick (Pick), their sole shareholder, in corporate guise and therefore one business entity. The common law either recognises or ought to recognise as a remedy in equity the entitlement of the Butcher Shop to claim rental remission due to the loss of beneficial occupation suffered by Apoldo.

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Inside out? A discussion on the case of *The Butcher Shop and Grill CC v Trustees for the time being of the Bymyam Trust*

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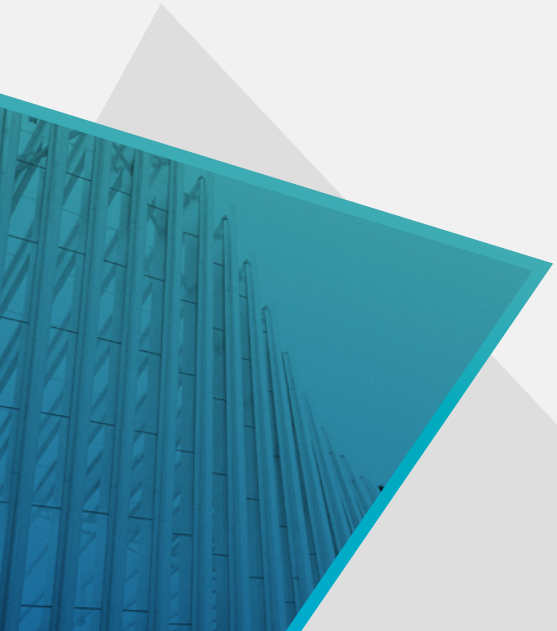

The High Court dismissed the counter application and granted an order in the main application for the Butcher Shop to make payment, but it successfully obtained leave to appeal to the SCA.

Findings

Regarding the first contention, the SCA stated that unless parties to a lease agreement limit or exclude the right to claim remission of rent in circumstances of *vis major*, a tenant is entitled to claim remission of rent if it is prevented from making use of the property either entirely or to a considerable extent due to a *vis major*, provided that the loss of enjoyment of the property is the direct and immediate result of the *vis major*. The court found that the lease agreement between the Trust and Butcher Shop did not exclude the right to claim for remission of rent arising from a *vis major* event such as that relied upon by the Butcher Shop, however the effect of the Apoldo sub-tenancy was that it precluded a claim by the Butcher Shop for remission based on loss suffered by the sub-tenant Apoldo.

It should be noted that relief in the main application was still properly granted by the High Court against the Butcher Shop for payment since the lease agreement precluded withholding payment of the base rental.

The second contention gave rise to the SCA's consideration as to whether the Butcher Shop could put up the loss suffered by Apoldo as a defence to the Trust's claim for rent payable by the Butcher Shop. Counsel submitted that Pick, as the sole shareholder, conducted a family business and he did so via the two corporate entities. Seen from this perspective, there was no *de facto* distinction between the Butcher Shop and Apoldo. The involvement of Apoldo in the conduct of the business was accepted by the Trust, indicating that the Trust treated the Butcher Shop and Apoldo as a single trading entity, and this called for equitable treatment of the two corporate entities. Counsel argued that common law principles which allow a separate legal personality to be disregarded, ought to apply and were sufficiently flexible, otherwise the common law ought to be developed in order to make available the remedy in circumstances such as those in the *Butcher Shop* case.

In reaching its conclusion on the second contention, the SCA, in relation to the distinction between a company and its shareholders cited the view in *Ochberg v Commissioner for Inland Revenue* [1931] AD 215 at 232 where it was held that a company, being a juristic person, remains a juristic person separate and distinct from the person who may own all the shares, and must not be confused with the latter. To say that a company sustains a separate persona and yet in the same breath to argue that in substance the person holding all the shares is the company

SOUTH AFRICA

Inside out? A discussion on the case of *The Butcher Shop and Grill CC v Trustees for the time being of the Bymyam Trust*

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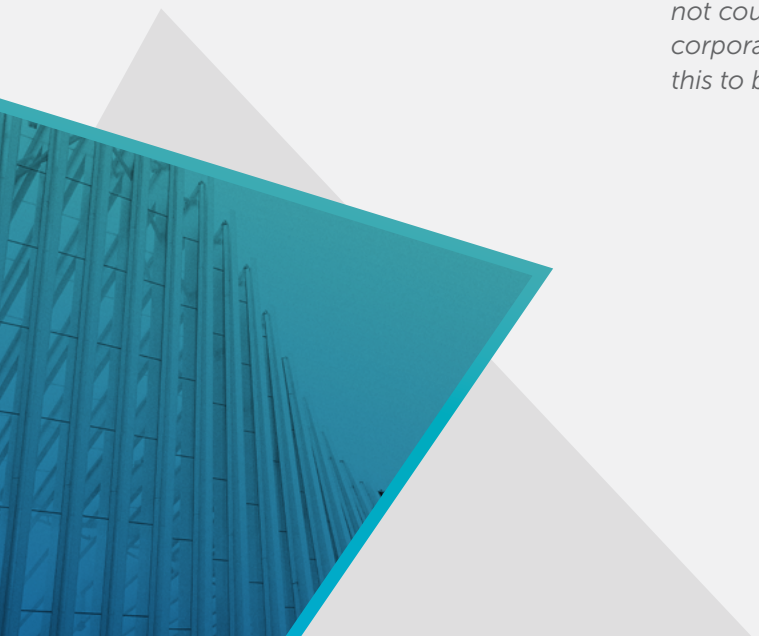
is an attempt to have it both ways, which cannot be allowed. Also citing a similar view expressed in the English case of *Tunstall v Steigmann* [1962] 2 All ER 417 (CA) where the concept of reverse piercing was rejected, the court held that:

> *"... what the Butcher Shop sought was to disregard, for its own benefit, the separate corporate personality of Apoldo, in circumstances where their joint shareholder [Pick] has deliberately arranged that Apoldo operates the restaurant even though the Butcher Shop is the Trust's tenant. The common law does not countenance disregarding corporate identities to allow this to be done."*

Regarding the development of the common law, the SCA held that the existence and effect of section 20(9) of the Companies Act cannot be overemphasised. Having recognised that the section supplements the common law and does not replace it, the court confirmed that while the term *"unconscionable conduct"* broadens the reach of the doctrine, the section clearly contemplates some form of misuse or abuse of a separate corporate identity as a necessary condition for the application of the remedy. In the court's view, the legislature enacted section 20(9) of the Companies Act in the form that it did and in doing so it did not introduce a general discretion to disregard the separate corporate personality of a company, instead it chose to confirm, even if in broader formulation, an essential requirement for the granting of the remedy, namely some form of unconscionable conduct.

The court held that two further considerations militated against the judiciary's development of the common law to accommodate the position of the Butcher Shop: firstly, *"the existence of separate corporate identities and the consequences which attach thereto are by no means inherently unfair or unjust and nor is there anything to suggest that the enforcement of the obligations undertaken by the Butcher Shop will bring about an injustice"*, and secondly *"our law does not countenance a casuistic resort to equity and fairness to circumvent statutory provisions or the rules of the common law"*.

The Butcher Shop's appeal was accordingly dismissed with costs.



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Inside out? A discussion on the case of *The Butcher Shop and Grill CC v Trustees for the time being of the Bymyam Trust*

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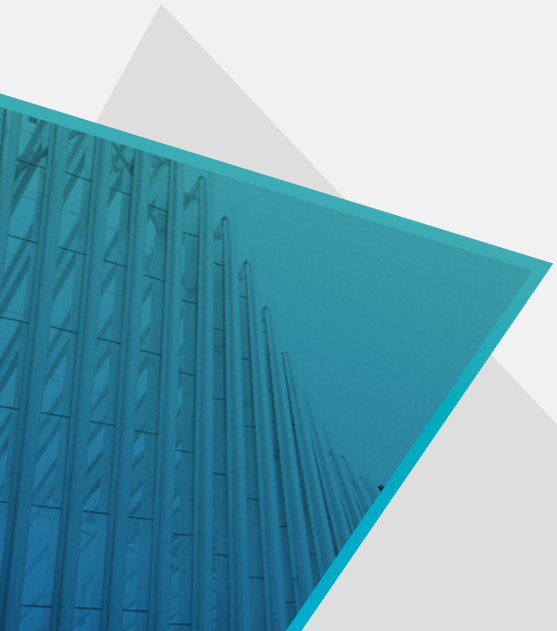
Conclusion

Although one may argue that strict allegiance to the separate legal entity concept does not necessarily address the concerns of today's complex economic realities, the judgment confirms that at present our courts are still reluctant to offer an "*inside out*" approach to the doctrine of disregarding the corporate personality of the company, referred to as insider reverse piercing, on the basis that it does not fall within the traditional rationale and grounds for disregarding the corporate personality of a company at common law and in terms of section 20(9). Particularly, that in relation to insider reverse piercing, the point of departure is that where one chooses to conduct business via a corporate entity then one cannot have it both ways in the sense that one claims entitlement to take benefit of any advantages that the formation of the corporation gives, without at the same time accepting the liabilities and natural consequences arising therefrom.

Perhaps the *dictum* from the leading English case of *Prest v Pretrodel Resources Ltd and Others* [2013] UKSC 34 where it was pointed out that "*[it] is not an abuse to cause a legal liability to be incurred by the company in the first place. It is not an abuse to rely upon the fact (if it is a fact) that a liability is not the controller's because it is the company's*" bears relevance, although not expressly cited by the SCA in this judgment.

Zakiya Shaik and Dane Kruger



CONSISTENTLY SUCCESSFUL

DealMakers

2022
1st by M&A Listed Deal Flow.
3rd by M&A Listed Deal Value, M&A Unlisted Deal Value, M&A Unlisted Deal Flow and General Corporate Finance Deal Value.

2021
1st by M&A Deal Flow.
2nd by General Corporate Finance Deal Flow.
2nd by BEE Deal Value.
3rd by General Corporate Finance Deal Flow.
3rd by BEE Deal Flow.
4th by M&A Deal Value.

2020
1st by M&A Deal Flow.
1st by BEE Deal Flow.
1st by BEE Deal Value.
2nd by General Corporate Finance Deal Flow.
2nd by General Corporate Finance Deal Value.
3rd by M&A Deal Value.
Catalyst Private Equity Deal of the Year.

2019
M&A Legal DealMakers of the Decade by Deal Flow: 2010-2019.
1st by BEE M&A Deal Flow.
1st by General Corporate Finance Deal Flow.
2nd by M&A Deal Value.
2nd by M&A Deal Flow.

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