DLA CLIFFE DEKKER HOFMEYR

CORPORATE GOVERNANCE ALERT

January 2013

IN THIS ISSUE

COMPLIANCE AND MOI REQUIREMENTS FOR PRIVATE COMPANIES WITH ISSUED DEBT INSTRUMENTS

In our September 2012 Alert, we dealt with the imminent deadline for companies to harmonise their company constitutional documents to comply with the new Companies Act, No 71 of 2008 (Companies Act).

The two year 'grace period', during which the old constitutional documents trumped the Companies Act in the case of any inconsistency between the two, terminates at the end of April 2013. A company will need to adopt a new memorandum of incorporation (MOI) for this purpose.

In this alert, we draw particular attention to the requirements for the MOIs and other material compliance aspects, relating to private companies that have issued debt instruments, such as bonds, notes, debentures and other debt securities and that may or may not be trading on a stock exchange. This was highlighted in April last year in a non-binding advisory opinion issued by the CIPC Readers may access the opinion at the following link:

www.cipc.co.za/Notices_files/Non_binding_opinion_Limitation_of_listing_Debt_instruments_on_JSE_v1.pdf

South Africa has a number of significant private companies that, while not listed, have significant bond issues and/or other publicly traded debt instruments. For example, last year Mercedes-Benz South Africa sold R1.5 billion of debt due in October 2015 at 112 basis points over the three-month Johannesburg interbank agreed rate (Jibar). Mercedes-Benz SA has issued up to R4.1 billion of bonds, the most since at least 1999 (see http://www.iol.co.za/business/business-news/mercedes-benz-sa-bonds-to-fund-expansion-1.1398074). Rand Merchant Bank served as mandated lead arranger and joint bookrunner in a flexible R1.56 billion multi-tranche, high-yield bond for Idwala Industrial Holdings (Pty) Ltd (see http://www.rmb.co.za/aboutDeals.asp). This bond is listed and traded on the JSE.

For the purposes of background, the distinction between a private company and a public company under the previous Companies Act, No 61 of 1973 (Previous Act) was that a private company had to restrict, in its articles, the transfer of its shares and prohibit offers of its shares to the public. However, a public company's shares could be freely tradable and transferable. The significance of being categorised as either private or public was that public companies were subject to greater public scrutiny, compliance, governance and accountability requirements under the Previous Act (and this remains the case). All public companies were also subject to regulation by the Securities Regulation Panel (now the Takeover Regulation Panel, or TRP) when a takeover or merger of the company was proposed, whereas for private companies it depended on the size of their share capital and number of beneficial shareholders.

BUT, a change in the Companies Act has brought about a significant difference in classifying private and public companies. For private companies, the Companies Act provides that in order to be classified as such, their MOIs must restrict the transfer of all 'securities', an expanded term that includes shares, hybrid and debt instruments, and not only shares such as ordinary and preference shares (s8 read with the definition of 'securities' in s1). Thus, companies who have any debt instruments in issue and that are freely tradable must accept that they are no longer private companies – they are instead public companies.

What does this mean for such (formerly private but now public) companies? Some of the material implications are:

- The MOI must be revised to be in line with that of a public company.
- When preparing a new MOI, the MOI must reflect that the company is now public and that there is no restriction on the transferability of its securities. A company may retain a restriction on the transferability of shares, but that doesn't change the fact that it is still a public company as not all securities are restricted (the debt instruments are still freely transferable).
- The company is subject to the accountability provisions in chapter 3 of the Companies Act, dealing with auditors and audit committees (the members of which must be elected by shareholders). The board must also appoint a company secretary.

continued

DLA CLIFFE DEKKER HOFMEYR

- The board composition of the company will need to be reviewed to comply with the Companies Act's requirements (as read with King III). The criteria for members of the audit committee are that they need to be independent non-executive directors, and the chairman of the company ought not to be the chairman of the audit committee.
- The company must have annual general meetings of shareholders while private companies are not obliged to do so under the Companies Act.
- The company is automatically a 'regulated company' which is subject to regulation by the TRP when any 'affected transactions' (primarily takeovers) are proposed in respect of the company. A private company, however, is only 'regulated' if over 10% of its voting securities (or securities convertible into voting securities) were transferred among unrelated persons in the past 24 months. A significant additional layer of regulation thus applies when an offer is made in respect of a regulated company.
- The company must implement and publicise whistle-blower systems required under s159 of the Companies Act.
- The company must allow its shareholder meetings to be accessible electronically (s61(10)).
- The pre-emptive right (in favour of existing shareholders) for issues of fresh shares under s39 does not by default apply to public companies (except listed companies but that it because of the JSE Listings Requirements).

Regarding social and ethics committees, the distinction is rather between listed and unlisted companies (not private versus public). All listed companies must have social and ethics committees whereas in the case of unlisted companies (public or private) it depends on the company's public interest score (if it reached 500 in any two of the last five years, it is required to have a social and ethics committee).

Each company (particularly those that are now 'public' by virtue of the change in the position under the Companies Act) must be assessed on an individual case-by-case basis according to its requirements and nuances, both in respect of its MOI and general corporate governance aspects.

It should also be borne in mind that private companies that have debt instruments listed on the JSE would have had to comply at all times with the JSE Listings Requirements and may therefore, with regards to governance, in any event already have many of the requisite structures and committees in place in order to meet the requirements of a public company. However, this cannot simply be assumed and the position in respect of each company and its group must be assessed.

Please contact any of our experts on the Companies Act and Corporate Governance for advice on these or related matters.

Thina Siwendu and Yaniv Kleitman

CONTACT US

For assistance on any aspect relating to the Corporate Governance services, please contact:

Chris Ewing
Chairman
Corporate and Commercial
T +27 (0)11 562 1158
E chris.ewing@dlacdh.com

Francis Newham
Director
Corporate and Commercial
T +27 (0)21 481 6326
E francis.newham@dlacdh.com

Yaniv Kleitman
Senior Associate
Corporate and Commercial
T +27 (0)11 562 1219
E yaniv.kleitman@dlacdh.com

André de Lange
Director
Corporate and Commercial
T +27 (0)21 405 6165
E andre.delange@dlacdh.com

Thina Siwendu
Director
Corporate and Commercial
T +27 (0)11 562 1326
E thina.siwendu@dlacdh.com

BBBEE STATUS: LEVEL THREE CONTRIBUTOR