DLA CLIFFE DEKKER HOFMEYR

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A THOUGHT ON ROUND-ROBIN RESOLUTIONS

Resolutions of shareholders of companies may be passed in one of three ways:

1. at a meeting under s61 of the Companies Act, No 71 of 2008 (Act);
2. by way of a 'round-robin' written resolution under s60 of the Act[1]; and
3. if there is a sole shareholder it may pass the resolution summarily and without procedural formalities under s57 of the Act.

With regard to s60 round-robins, what exactly is the number of votes required to pass the resolution?

Before the Act came into force (1 May 2011) the common law doctrine of unanimous assent typically regulated the question, and one needed unanimity (unless the company's articles or shareholders agreement provided otherwise). Round-robins are now statutorily regulated by s60 of the Act.

Firstly, in terms of s1 of the Act, both the definitions of ordinary and special resolution contain the phrase "...of the voting rights exercised..." and do not mention anything along the lines of a majority of the quorum necessary for ordinary and special resolutions to be passed. From this wording one can therefore safely conclude that whether a decision has been passed by ordinary or special resolution, as the case may be, depends on the actual votes exercised and that abstentions from these resolutions are not treated in South African company law as 'no' votes, they are indeed treated as abstentions.

This conclusion raises an interesting question when a company decides to make use of the convenience offered by s60 by proposing resolutions to be voted on a round-robin basis by its shareholders.

Take an example where a company has 100 shares in issue. Assume that its Memorandum of Incorporation does not say anything specific about round-robins, and therefore that the default position in the Act applies. It submits a resolution for consideration to its shareholders entitled to exercise voting rights in relation to this resolution as allowed for in s60(1)(a) of the Act. However, only one shareholder holding five shares in the company responds in writing in the affirmative after the resolution was submitted (within the 20 business days prescribed in s60(1)). Is it not the case that the voting rights exercised in relation to the resolution were therefore in favour of such resolution and thus passed unanimously? The argument would be that the remaining shareholders, by not responding, abstained from voting.

[1] One must however use meetings for annual general meetings (s60(5)), and arguably also for fundamental transactions (s115) given that the mechanics of the appraisal rights under s164 operate in the context of a meeting.

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Section 60 of the Act provides as follows:

"(1) A resolution that could be voted on at a shareholders meeting may instead be-

(a) submitted for consideration to the shareholders entitled to exercise voting rights in relation to the resolution; and

(b) voted on in writing by shareholders entitled to exercise voting rights in relation to the resolution within 20 business days after the resolution was submitted to them.

(2) A resolution contemplated in subsection (1)-

(a) will have been adopted if it is supported by persons entitled to exercise sufficient voting rights for it to have been adopted as an ordinary or special resolution, as the case may be, at a properly constituted shareholders meeting; and

(b) if adopted, has the same effect as if it had been approved by voting at a meeting."

The authors of *Henochsberg*[2] interpret the wording in s60(2)(a) as giving 'the impression that the minimum majority will be as at a minimum quorate meeting, ie by the requisite majority of the votes at a meeting where the minimum quorum (eg 25% of all the votes) and not all the votes, is present.' Even if this was the case, if one shareholder holding 25 shares in the company from the example provided earlier writes back to the company, a resolution would be unanimously passed, as he constituted the 'quorum' (if that concept can be notionally applied in the round-robin scenario). Other commentators are of the view that the requisite majority of all shareholders must be obtained under s60, but that is not what the wording of the section suggests.

In other jurisdictions the legislation dealing with round-robin resolutions either provides that a round-robin resolution must be unanimous (Canada and Australia) or it clearly states that it must be a majority of all the issued shares (UK).

Private companies will in many instances be unbothered by the ambiguity in s60 of the Act, because more often than not one manages to obtain an outright majority or even unanimity. That then puts the question beyond doubt. However, in recent times some listed companies have been exploring the utility of s60 of the Act, albeit in exceptional circumstances (which is not disallowed by the Johannesburg Stock Exchange (JSE) except for elections of directors and resolutions required to be passed in terms of the JSE Listings Requirements). In the listed environment, it is not always easy to obtain a majority of all shareholders to vote in favour of a resolution, due to the number of shareholders that choose not to participate in the voting process. In such a scenario, there are essentially three views or approaches which could be adopted by a court:

- The resolution needs to be supported by the majority of all issued shares;
- Shareholders holding at least such number of shares as would constitute a quorum (the default position in the Act is 25%) must respond in the voting process, and out of those shareholders one needs the majority of the votes exercised to be cast in favour of the resolution. This approach essentially aims at 'simulating' the mechanics of an actual meeting, and is in our view the preferred interpretation; or
- Any number of shareholders may respond in the voting process, and as long as a majority of the votes exercised were cast in favour, the resolution is passed.

It is also very important in every case to consider what the company's memorandum of incorporation provides in respect of written resolutions and whether it contains more onerous provisions in this regard.

Standre Bezuidenhout and Yaniv Kleitman

[2]Delport *et al Henochsberg on the Companies Act 71 of 2008* (December 2013 - SI 7) at 228

continued

SCA CASE ON NON-CESSION / NON-TRANSFER CLAUSES

When a company is placed in liquidation, a number of the ordinary principles of our law of obligations (in particular, contract) are to some extent turned on their heads. A liquidator steps in and has a duty to recover all amounts owing to the company and to sell its assets for the benefit of the creditors. This duty often comes into conflict with arrangements and obligations that a company may have entered into prior to its insolvency, and there are of course a number of rules in insolvency law which deal with those conflicts and with which party's interests take precedence. One legal question which has involved a fair amount of debate in the cases is whether an anti-cession clause in a pre-existing agreement is binding on a liquidator. The recent Supreme Court of Appeal (SCA) case of *Born Free Investments 364 (Pty) Ltd v Firstrand Bank Ltd*[3] elucidated several important principles in this regard which will have an important influence in the field of contract law, possibly also in the specific area of drafting of companies' shareholders agreements and memoranda of incorporation.

Born Free instituted proceedings against Firstrand Bank (FRB) as the cessionary of two claims from the liquidators of two companies. The two companies had borrowed moneys from FRB. Born Free alleged that FRB repudiated the loan agreements and that as a result those companies suffered losses north of R160 million. It is those claims that Born Free, pursuant to cessions to it from the liquidators of those companies, asserted against FRB. In answer to Born Free's claims, FRB denied the validity of the cession on the basis that its (FRB's) contract with each of the borrowers contained a *pactum de non cedendo* (anti-cession or non-cession clause) in these terms: "You shall neither cede any of your rights nor assign any of your obligations under this agreement without our prior written consent". There were other defences that FRB raised, but the validity of the cession was the decisive one in this matter. FRB's defence found favour with the high court, Born Free subsequently appealed to the SCA.

- The SCA held that a distinction must be drawn between a *pactum de non cedendo* which prohibits the cession of an existing right, ie one which pre-existed the conclusion of the *pactum*, on the one hand, and a *pactum de non cedendo* of a right which, by means of the *pactum* itself, was created *ab initio* (or inherently) as a non-transferable right, on the other. In the case of the first *pactum*, that which relates to an existing right, it will not always be enforceable; in particular, it will not bind the liquidator from executing a valid 'involuntary' cession of the right to a third party in the course of carrying out his duties as liquidator. However, in the case of the second *pactum*, that which relates to a right which was created ab initio as a non-transferable right, the *pactum* is valid and enforceable against the world because the right is simply inherently incapable of being transferred by anyone – the prohibition is part of the 'make-up' of the very right itself.

- The question then was whether the rights which the liquidators had ceded to Born Free had been created *ab initio* as non-transferable rights. To the SCA, the non-cession clause in question was clear and unambiguous. The old adage, *nemo plus iuris ad alium transferre potest quam ipse habere* (a person cannot transfer more or greater rights than those held by him) had to apply and therefore the liquidator simply did not have the right or power in the first place to transfer the rights in question.

[3](973/12) [2013] ZASCA 166 (27 November 2013).

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An interesting context in which these principles, now clarified in Born Free, find application is pre-emptive rights (or rights of first refusal) and other restrictions pertaining to the transfer of shares in a company. This will impact the flexibility that a liquidator has to sell shares that form part of the liquidated company's assets. Typically in the context of private companies, the memorandum of incorporation or shareholders agreement would place various restrictions on shareholders in respect of the transfer of their shares. Given that a share is a bundle of rights and obligations which is sold and delivered by way of cession (see *Botha v Fick*[4]), how would non-transferability clauses be dealt with by a liquidator of a shareholder? Applying the principles in Born Free, one imagines that a distinction should be drawn between the scenario where the restriction is contained in the share rights themselves as between the company and the shareholder (and hard-wired into the memorandum of incorporation as part of the preferences, rights and limitations attaching to those shares – s37(4) of Companies Act, No 71 of 2008 (Act)) and the scenario where the pre-emptive rights are in a shareholders agreement which is entered into after the share rights have been determined.

Admittedly the above distinction may be difficult draw in some cases in the context of share transfers, but it may have important practical consequences.

The Born Free case undoubtedly brings this issue back into sharp focus and it will be very interesting to see how it influences the drafting of contractual prohibitions on the transfer of shares or other types of incorporeal assets.

Yaniv Kleitman and Zunaid Lundell

THE RESPONSIBILITY OF BROKERS IN RELATION TO MARKET ABUSE

On 28 February 2014 certain proposed amendments to the Johannesburg Stock Exchange (JSE) Derivatives[5] Rules (Rules) were gazetted for comment. The proposed amendments seek to bring the Rules in line with the Financial Markets Act, No 19 of 2012 (FMA) which commenced in June last year, and they also address,amongst other things, the role of JSE derivatives members (brokers) in preventing market abuse as contemplated in Chapter 10 of the FMA.

'Market abuse' as contemplated in the FMA falls into two categories:

1. insider trading (s78 – dealing in securities listed on a regulated market while knowing that one is in possession of inside information), and

2. prohibited practices (s89 – essentially practices that are aimed at creating an artificial price for a security).

Some of the statutorily listed examples of prohibited practices have acquired certain descriptions over the years such as 'cornering the market', 'washed sales', 'marking the close' and other manipulative acts and practices.

It is proposed that, in order to avoid unnecessary overlap or duplication, s7.200 and s7.210 of the Rules be amended to remove the provisions in relation to prohibited trading practices that are already addressed in the FMA: the intention is that a breach of the relevant provisions of the FMA by a member or its employees will be dealt with by the FSB's Directorate of Market Abuse and the FSB Enforcement Committee, and there is no need to duplicate the offence in the JSE rules and to take action in terms of the JSE's enforcement rules as well. S7.200 now places emphasis on the gatekeeping role that members play in preventing market abuse through the introduction of provisions that require members to take specific steps to prevent and detect market abuse. Positive steps are envisaged. The following measures are sought to be introduced:

[4] 1995 (2) SA 750 (A).

[5] A "derivative" means any financial instrument or contract that creates rights and obligations and whose value depends on or is derived from the value of one or more underlying asset, rate or index, on a measure of economic value or on a default event

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- A member must give consideration to the circumstances of orders placed by clients before entering such orders in the JSE derivatives trading system and must take reasonable steps to satisfy itself that such orders and any resultant trades will not result in a breach of the provisions of s80 of the FMA (prohibited trading practices);

- A member must ensure that all of its employees involved in the receipt of orders from clients and the execution of transactions in derivative securities on the JSE derivatives trading system are familiar with the market abuse provisions in s77 to s80 of the FMA and that those employees receive adequate training and guidance to enable them to recognise and avoid entering into any transaction on behalf of the member or its clients which will result in, or is likely to result in, a breach of those provisions;

- A member's compliance monitoring procedures must specifically include procedures to monitor orders entered into, and transactions executed on, the JSE derivatives trading system by the member and its employees, with the objective of identifying and taking appropriate action in relation to orders or trades that, in the reasonable opinion of the member, may constitute a breach of the provisions of s78 and s80 of the FMA.

The role of JSE members in the combat against market abuse has for long been an area of focus of the relevant regulatory authorities. The proposed amendments are a clear indication of the JSE's movement in a direction which places a greater burden and responsibility on its members in this context, which resembles trends in other jurisdictions. Interested persons had 14 days from the date of publication of the proposed amendments to submit their comments to the Financial Services Board. It will be interesting to observe the outcome of the process.

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