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CORPORATE & COMMERCIAL **ALERT**

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Private companies as regulated companies: The "*forget-me-not*" hurdle that may trip you up

Lurking behind the apparent lies the often forgotten and far-from-straightforward concept of private companies being deemed regulated companies – as well as the consequences thereof.

Even before a client has fully explained their brief to an M&A lawyer, the cogs are already grinding away as we consider (amongst other things) the transaction structure and the possible conditions that the transaction needs to be subject to.

The most common conditions usually relate to the corporate action required and the regulatory approvals that may need to be obtained. In any event, conditions to a transaction can largely be grouped into (i) conditions negotiated between clients or mutually agreed conditions (e.g. sign-off on the due diligence); and (ii) conditions required by law (e.g. competition approval).

Lurking behind the apparent lies the often forgotten and far-from-straightforward concept of private companies being deemed regulated companies – as well as the consequences thereof. This concept is dealt with in section 118 of the Companies Act 71 of 2008 (Companies Act) as read with section 91 of the Companies Regulations 2011, promulgated in terms of section 223 of the Companies Act (Companies Regulations).

Qualifying criteria

In terms of section 118(1)(c), a private company will be deemed to be a regulated company if it meets either one of two criteria.

Firstly, the percentage of the issued securities of a company that have been transferred, other than by transfer between or among related or inter-related persons, within a period of 24 months, immediately before the date of a particular affected transaction or offer that exceeds the prescribed percentage of 10% of the issued securities of that company (in terms of Regulation 91(1)) (Deeming Provisions).

Secondly, whether the Memorandum of Incorporation of the company expressly provides that the company and its securities are required to comply with sections 117 to 127 and the takeover regulations contained in Chapter 5 of the Companies Regulations (Takeover Regulations).

It is worth noting that the analysis set out above may fall away as the Companies Amendment Bill, 2018 (which is not binding law at this stage) proposes that section 118(1)(c)(i) is replaced by the test contained in section 84(1)(c) (relating to whether or not a private company is required by the Companies Act or Companies Regulations to have its annual financial statements audited every year).

Calculating the prescribed percentage

As a word of caution, in performing an analysis to determine whether a private company is a regulated company in terms of the Deeming Provisions, particular attention should be paid to Regulation 91(2)(a). The legislature appears to have employed terms relating to how the prescribed percentage of 10% is calculated that are incongruent with the apparent intention of such provisions – a purposive interpretation may need to be employed.

Additionally, one should also exercise particular caution when a transaction comprises a series of many indivisible, or individual, steps and transfers, where if each one is not properly accounted for and marked against the share transfer history of the company as evidenced in its share register, it could inadvertently cause a particular step to confer "*regulated company*" status and require compliance (outlined below) where the need for such compliance could have been avoided.

Private companies as regulated companies: The *"forget-me-not"* hurdle that may trip you up*...continued*

Practically, in order to avoid unnecessary costs, complications and delays, parties usually apply for an exemption in terms of section 121(1)(b) read with section 119(6).

From a transactional perspective, in addition to the transaction-specific requirements that a regulated company is subject to, the primary over-arching provisions that apply to a regulated company are found in:

- section 119, which effectively mandates the panel to regulate any affected transaction or offer in accordance with Parts B and C of Chapter 5 of the Companies Act as well as the Takeover Regulations (without regard to the commercial advantages or disadvantages of any transaction or proposed transaction); and
- section 121 which requires an offeror to:
    - comply with all reporting or approval requirements set out in in Part C of Chapter 5 of the Companies Act (unless exempted by the panel); and
    - not give effect to an affected transaction unless the panel has either issued a compliance certificate with respect to such transaction or granted an exemption for such transaction.

Practically, in order to avoid unnecessary costs, complications and delays, parties usually apply for an exemption in terms of section 121(1)(b) read with section 119(6). This exemption application is made by writing to the panel and sets out the facts of the transaction and the grounds on which such exemption should be granted (enumerated in section 119(6)). If exemption is unlikely (considering section 119(6)), compliance with the relevant provisions must take place and a compliance certificate sought from the panel.

As touched on above, it is this granting of an exemption or compliance certificate (as the case may be) that would be a condition to which the affected transaction would be subject. A failure to include this suspensive condition may result in a scenario where an affected transaction would become unconditional and effective without first complying with section 121, leading to a possible contravention of the Companies Act with its concomitant penalties and sanctions.

Accordingly, given the ramifications of non-compliance, section 118 should be front of mind when considering the suspensive conditions to a transaction. A proper analysis in terms of the Deeming Provisions should be undertaken in the context of the transaction to avoid any adverse unintended consequences.

Nikhil Sham, overseen by Brian Jennings

"*Wily confidence tricksters*" to face a consumer class action

The Law Clinic sought an order to "*certify*" a class action on behalf of those consumers, in order to undo these purported agreements, and effectively reverse thousands of debit order transactions.

For many South Africans, the bills are piling up and there is not enough money to pay them. Google searches for "*loans*" yield a plethora of results, including websites such as www.loanchoicesa.co.za and www.loanhubsa.co.za, eager to assist unsuspecting customers with obtaining a short-term loan, promising "*no credit checks*" or "*loan fees*" involved. All that users need to do is complete a contact form, provide their bank details, and click a checkbox to indicate acceptance of jargon-filled terms and conditions.

Thousands (if not tens of thousands) of South Africans have filled out such forms online on a multitude of websites, all operated by Lifestyle Direct Group, the brainchild of Mr Damian Malander.

Those who completed these online forms have a common complaint: on their understanding they had contacted the relevant website for loan assistance, however, they began to notice deductions from their bank accounts in the form of debit orders. When they queried the debit orders, consumers were informed, to their surprise, that they had authorised the debit orders as part of a subscription for a "*telephonic legal advice service*". No short-term loan had been approved or granted. When they tried to cancel the purported agreement, they were stonewalled, and then harassed with threats in the event that the debit orders were not honoured.

These are the facts which drove the Stellenbosch University Law Clinic (Law Clinic) to bring a class action before the Western Cape High Court on behalf of consumers who unwittingly subscribed for "*telephonic legal advice services*" having been led to believe that they had simply enquired as to their eligibility for a loan. The Law Clinic sought an order to "*certify*" a class action on behalf of those consumers, in order to undo these purported agreements, and effectively reverse thousands of debit order transactions. The Law Clinic also sought an interdict prohibiting the companies from conducting similar schemes, pending the final determination of the class action.

The class action

The "*certification*" of a class action suit is the first step in obtaining relief for aggrieved consumers. The Law Clinic sought (and obtained) certification of an "*opt-out*" class action to be instituted against the various companies running the "*loan*" websites (respondents). None of the respondent companies were registered credit providers or registered legal practitioners. All of these companies are associated with a group company, Lifestyle Direct Group, the first respondent, and Malander, the eighteenth respondent.

By the time that the matter was heard by the Western Cape High Court (per Gamble J), the Law Clinic's certification application had narrowed down to two discrete issues, namely the commonality of issues and the appropriateness of the remedy.

"*Wily confidence tricksters*" to face a consumer class action*...continued*

In order to bring a class action, an applicant is required to show that there is a commonality of issues.

Commonality of issues

In order to bring a class action, an applicant is required to show that there is a commonality of issues. Put differently, the members of the class (i.e. the consumers in this case) must have claims against the respondents which are the same, or substantially the same. In considering whether this criterion had been met, the court held that it is not necessary for every member of the class to have an identical cause of action, with identical facts and identical relief. Rather, if there are some issues of either fact or law that are common to all the members of the class, this is sufficient to satisfy the commonality criterion.

On the facts before it, the court found that the scheme run by the respondents fulfilled this criterion, having regard to, amongst other things, the respondents' *modus operandi* and the consumer law issues under the Consumer Protection Act 68 of 2008 (CPA) and the common law. The court also considered the fact that similar evidence would need to be lead in thousands of cases before separate courts if certification was to be refused. It referred to the Canadian Supreme Court authority in terms of which it was held that the essential question is "*whether allowing the suit to proceed as a representative one will avoid duplication of fact-finding or legal analysis*". This test was found to be satisfied in that the consumers were all ultimately allegedly misled into concluding "*agreements*" in the same manner.

Appropriateness

A further factor in determining a class action proceeding is the criterion of "*appropriateness*" – i.e. whether class action proceedings are the appropriate procedural device for putative plaintiffs to obtain relief. The court first sought to define the class being represented, having found that this definition provides the foundation for a class action. Importantly, the court agreed that in order for membership of a class to be determined through objective criteria, it is necessary that this class be defined with sufficient precision.

On the facts, the court found at least three objective criteria that could be used to establish membership of the class, namely: (i) whether the member's bank account had been debited by the respondents; (ii) whether the member had been subject to harassment regarding the payment of the debit orders; and (iii) whether the member had intended to conclude an agreement with the respondents. Having persuaded itself that the class could be objectively and precisely defined, the court went on to find that the class was large in size and the claims were relatively small. On this basis, the court confirmed the appropriateness of the class action.

The last issue that the court had to consider in relation to the certification, was whether the class action should be an "*opt-in*" or "*opt-out*" action. An opt-in action requires that persons take active steps to be part of the class action, whilst

"*Wily confidence tricksters*" to face a consumer class action*...continued*

This issue has not yet been tested by our courts, and the upcoming trial and subsequent judgment promise to make it a landmark case.

an opt-out action automatically binds the members of the class, unless they decide to actively opt-out. The court found that the case before it was well suited to an opt-out class action, and ordered the publication of the class action in several newspapers, online websites, and radio stations countrywide.

The consumer law issues

The certification of the class action is merely the first step in vindicating the rights of thousands of South Africans who fell victim to what was, in effect, a scam. The next step (subject to any appeal against the certification order) was the ventilation of consumer law issues raised by the Law Clinic in terms of the CPA and the common law.

Although the court did not consider the merits of the substantive issues raised by the Law Clinic, it did make certain preliminary findings in relation to the four causes of action upon which the class action is likely to be based:

Firstly, the Law Clinic intends to argue in due course that the agreements concluded with the respondents on the various websites, were *prima facie* in contravention of sections 40, 41 and 48 of the CPA. These sections of the CPA deal with "*unconscionable conduct*", "*false, misleading or deceptive representations*", and "*unfair, unreasonable or unjust contract terms*" respectively. The relief sought is found in section 52 of the CPA, which gives courts a wide variety of powers to restore money or property, compensate consumers for losses, and to require the supplier to cease any practice.

Secondly, as an alternative to its argument under the CPA, the Law Clinic will rely on the common law and argue that the agreements were unlawful and based on a fraudulent misrepresentation. If successful, they will seek declaratory relief, entitling them to restitution and damages.

The third issue, which will feature in due course, is that the conduct of the respondents, by demanding payment from the consumers, is unconscionable in terms of section 40 of the CPA or unlawful according to common law. If successful, the class will be entitled to relief in terms of section 52(3)(b)(iii) of the CPA, which gives courts the power to require the supplier to cease any practice.

Finally, the Law Clinic will argue that Malander (as the controlling mind of the respondent companies) abused the respondents' corporate personalities to perpetrate what was described as a scam.

Apart from the interesting consumer law issues that this case will deal with, the Law Clinic may also seek to argue that the "*click wrap contracts*" as defined in the Electronic Communications and Transactions Act 25 of 2002 in this case were invalid. "*Click wrap contracts*" essentially entail agreements that are concluded electronically by clicking on a box on a website (and thereby agreeing to certain terms and conditions) prior to submitting an online form. This issue has not yet been tested by our courts, and the upcoming trial and subsequent judgment promise to make it a landmark case.

Subject to an appeal against the certification order, the class action is likely to proceed in the course of 2022. Companies and consumers are encouraged to keep an eye on the proceedings as we are likely to see interesting developments in South African consumer law, both under the CPA and the common law.

Justine Krige and Kara Meiring

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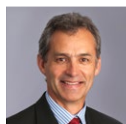

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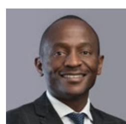

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Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

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